



Building Value in Your Business

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What is your Business Worth?

The business is generally the owner's most valuable asset.

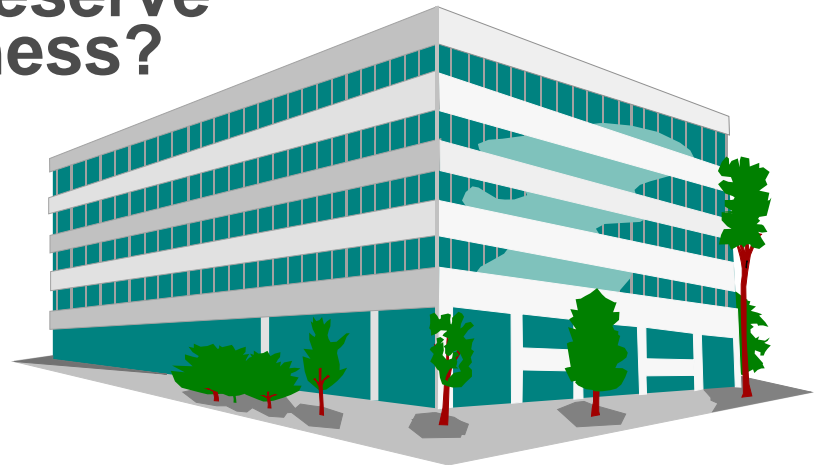
Financial security depends on maximizing value and converting that asset to cash.

Having a plan can help maximize the value when it is time to transition or exit the business.

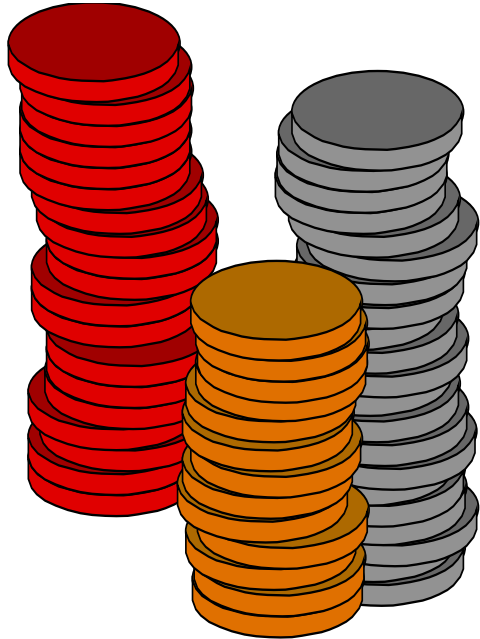


Best Case...

- **You own a business.**
 - You run it profitably
 - You keep tight control on operations
 - You have a great product or service
 - Can someone else do the same with your business without you?
- **What will create and preserve value within your business?**
- **What allows you to transfer your business profitably**



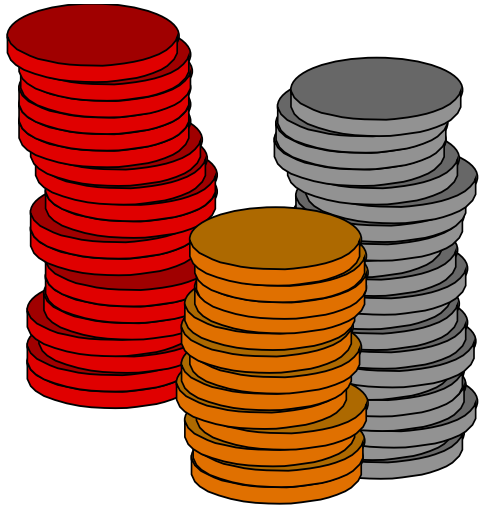
Business Value



***The value of a business
is based upon the perspective
of the person buying it.***

Willing Buyer & Willing Seller

Business Value



Like any investment, the value of a business is the benefits received by the buyer (usually cash flow) divided by the rate of return desired.

Simple Example

- Business generates cash flow to owner of \$200,000.
- Buyer desires a 20% rate of return on investment.
- Buyer would be willing to pay \$1,000,000.

The Driver of Value

What benefits will the buyer receive from owning the company?

Earnings

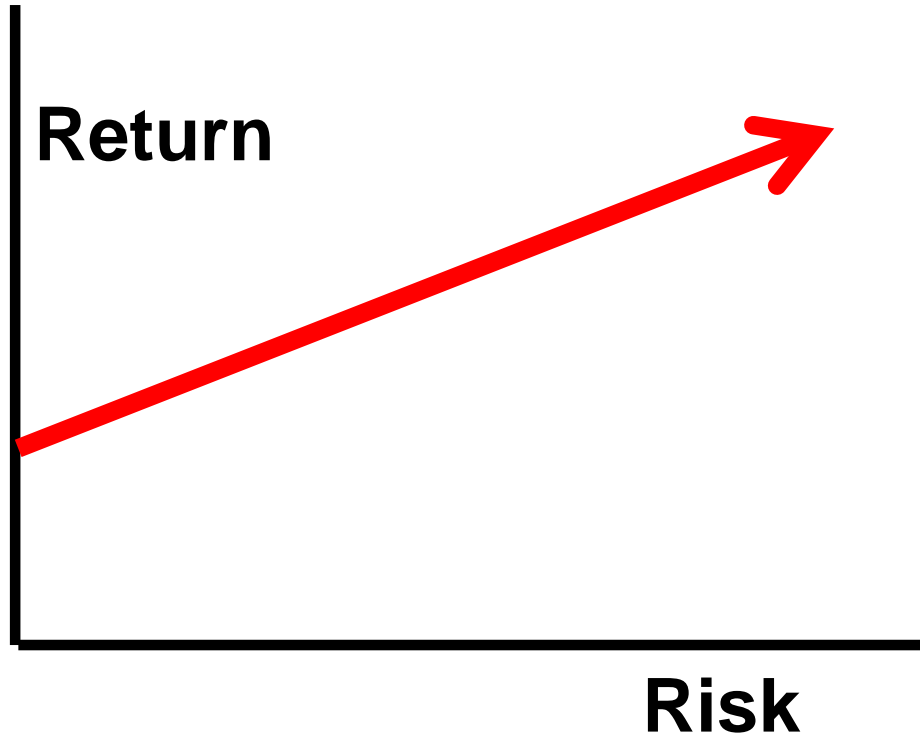
Cash Flow

Types of Buyers

Investment Value – Value to a specific investor

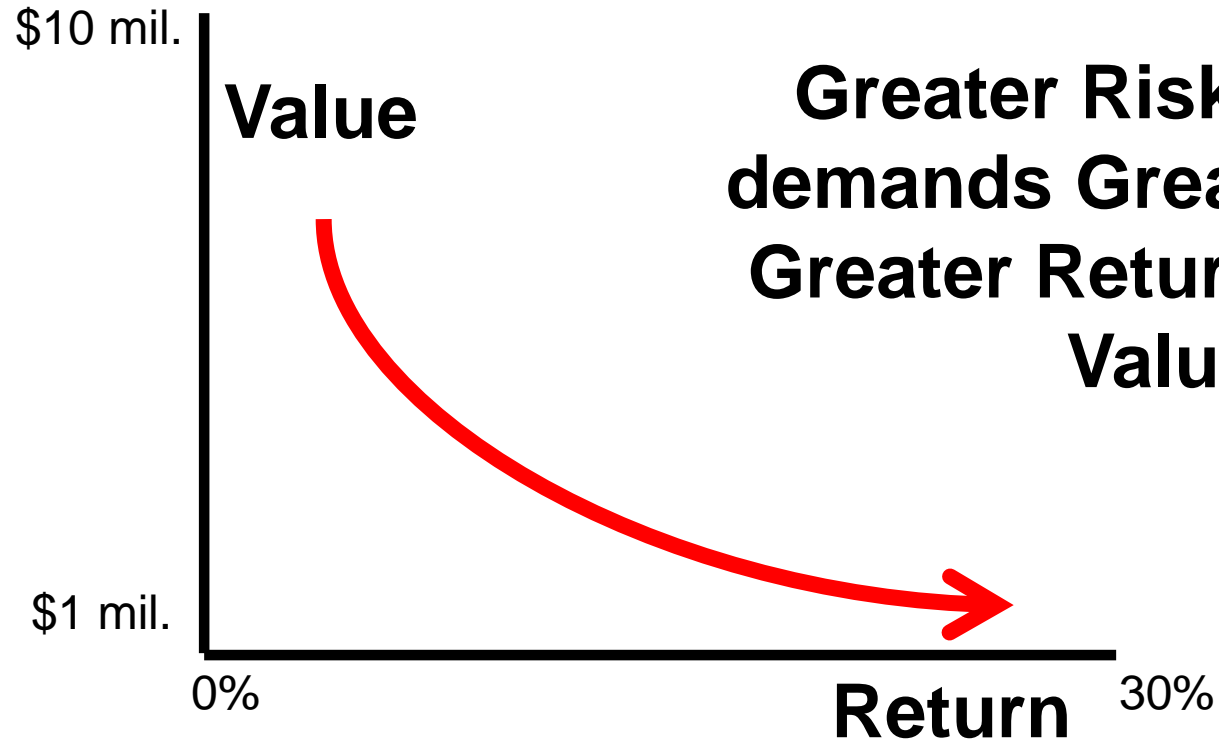
- **Financial Buyer** – Operate business as stand alone.
- **Strategic/Synergistic Buyer** – Blend into an existing business. Gain efficiencies and cost reductions.

Investor Expectation



Greater Risk = Greater Return

Investor Expectation



Valuations Based on ROI

ROI is determined based on Risk of the investment (Discount Rate)

•Discount Rate/ROI=	<u>Co. 1</u>	<u>Co. 2</u>
•Risk free rate +	3%	3%
•Equity risk premium +	6%	6%
•Size premium+	6%	6%
•Company specific risks	<u>4%</u>	<u>10%</u>
TOTAL	<u>19%</u>	<u>25%</u>
Multiple of earnings	5.2	4

Valuations Based on ROI

Cash Flow	\$200,000	\$200,000
Capitalization Rate	<u>19%</u>	<u>25%</u>
Value	<u>\$1,053,000</u>	<u>\$800,000</u>

**Objective: Do the things that
reduce risk and assure stability**

Value Drivers

Implement a strategy to grow the company

- Revenue improvements
 - Develop new revenue stream
 - Develop annuity revenue – repeat customers
 - Diversify customer base – How large is your largest customer?
 - Develop add on products
 - Develop new markets/diversify markets – big fish or a little fish? Make the pond bigger.

Value Drivers

Implement a strategy to improve efficiency

- Develop operating systems that improve sustainability of cash flows -consistent systems and process
- Improve equipment & facilities efficient use and appearance
- Develop employee training program
- Develop employee retention program
- Pay down debt
 - Growth through high debt does not add value to owners

Value Drivers

- Build a solid management team.
 - Groom successors
 - Cross train
 - If management team is aging, build successors below them



What do I want to accomplish?

- The way to increase the ultimate value of the business is to:

–Increase Cash Flow

–Reduce Risk

Review the Value Drivers

	 <u>CASH</u>	 <u>RISK</u>
▪ New revenue stream	X	
▪ Annuity revenue – repeat customers	X	X
▪ Reduce costs	X	
▪ Pay down debt	X	X
▪ Develop operating systems		X
▪ Improve equipment & facilities		X
▪ Solid management team successors		X
▪ Develop employees – training		X
▪ Develop new Markets	X	X
▪ Develop special processes	X	X
▪ Solidify and diversify customer base	X	X

What's it Worth Now?

- Assume we increase cash flow from \$200,000 to \$300,000.
- We reduce risks by implementing operating improvements so the company risk factor is now 4% instead of 10%. The capitalization rate drops from 25% to 19%.
- The value of our business is now \$1,579,000.
($\$300,000$ divided by 19%)

We almost doubled the value!

Plan Strategically

- What's special about your firm?
- Acquire new niche services
- Develop strong customer ties
- Strengthen your team
- Build a stable income stream
- Strengthen operating systems

**NOT A
LAST
MINUTE
DEAL!**

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