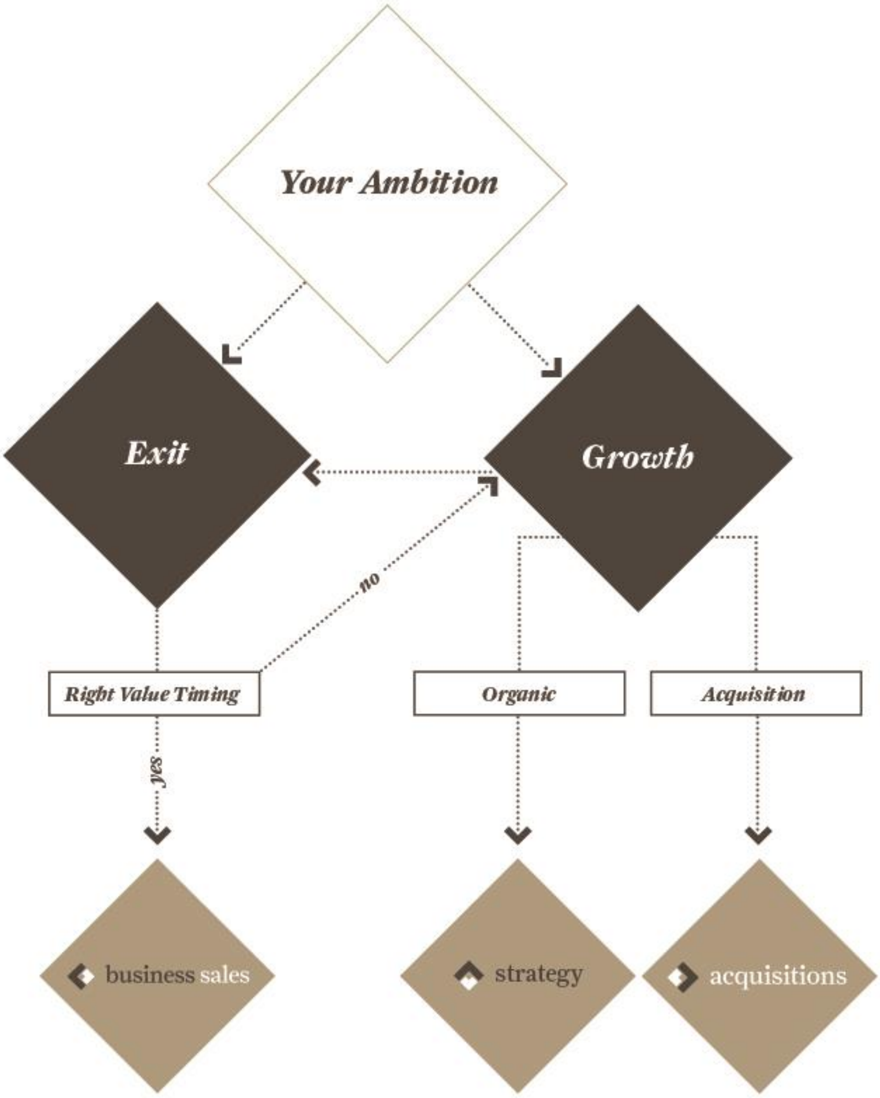
AVONDALE
BUSINESS SALES
ACQUISITIONS
STRATEGY

The Next Strategic Move

For many business owners selling a business to exit is the ultimate reward for years of hard work. Maximising your exit requires strategy, leadership and expertise. Most of the wealth in the world is capital wealth and not income, and realising this wealth can be an important part of a company owner's journey and the peak of an ambition.

There are lots of questions to be answered before you even enter into the sales process; is it the best time to sell, is your company worth what you want it to be, do you need to wait until it is and how do you increase the value pre-sale and how do you find the best strategic buyers to ensure optimum value? The diagram below depicts possibly journeys that a business owner may make in pursuing their objectives. This guide will enable you to start answering these questions and place you in a more informed position when discussing your options with professional advisers.



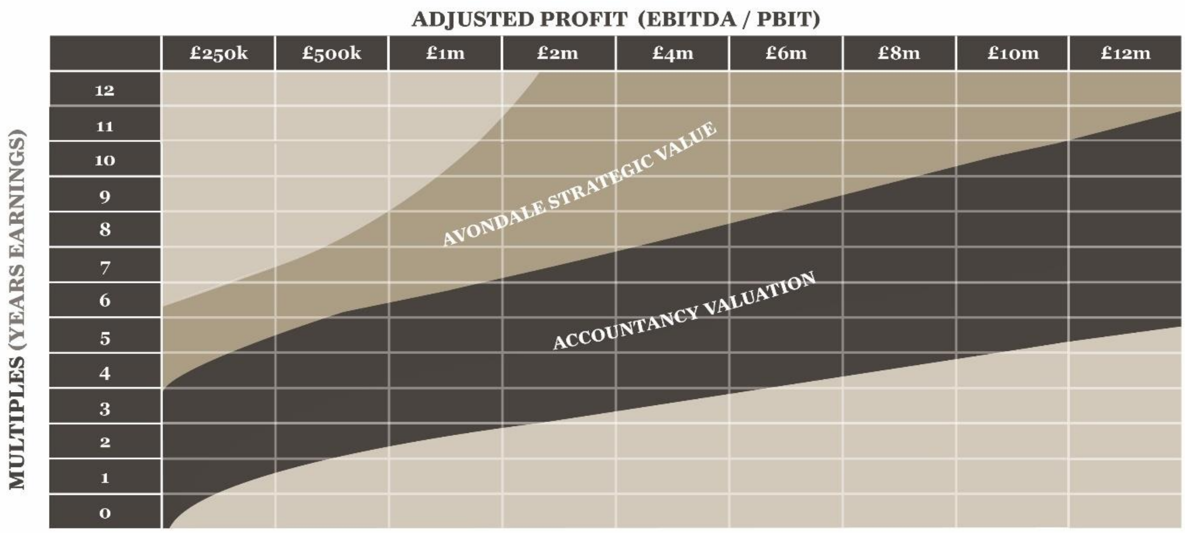
Valuation

Critical to making an informed decision as to whether you should sell your business now or in the future is understanding how much the company is worth. Every good adviser should provide you with a value estimation. Ensure you feel that this is accurate and not inflated purely to secure your instruction. If the valuation isn't right for you at this time; what are your options? Your adviser should be able to provide you with an alternative plan to ultimately achieve your goals in line with your personal aspirations.

There are many valuation formulas such as asset based valuations, discounted cash flow forecasts, intellectual property and dividend formulas. However, typically in unquoted businesses, the most usual method is to use a multiple of one year's "adjusted" and sustainable profits. The chosen multiple is the number of years it is considered acceptable to generate a payback on the investment. The multiple typically assumes a debt free/cash free balance sheet included in a deal, excluding freeholds but allowing for appropriate establishment costs and can be influenced by several factors (please see Value Enhancement Strategy on the following page).

A sustainable profit figure will be calculated, usually based on this year's and evidence based forecasts. Adjustments are then made to this figure to obtain the net profit to a buyer, rather than the one the current owner may have achieved. Adjustments can include directors' salaries, extraordinary expenses and/or costs for placing the business under management; buyer economies of scale and cross selling opportunities may also be considered, although this is more subjective and often down to negotiation.

The table below is a typical guide to the 'assumed' multiple range x the adjusted profit. The profit is usually expressed either profit before income and tax (PBIT) for capital intensive companies such as manufacturing, or earnings before interest, tax, depreciation and amortization (EBITDA) for service companies where depreciation is not usually a heavy cost.



EBITDA: Earnings before interest, tax, depreciation and amortisation
PBIT: Profits before interest and tax

Value Enhancement Strategy

How can you design the business to enhance value? Achieving optimum value requires careful business design and expert advice. A strategic value building programme should be carefully considered pre-sale in order to influence the multiple applied to your business by buyers. Below are examples of multiple influencers that can increase or decrease the sale value.

Many advisers with comprehensive strategic business growth services will be registered with the Government's Growth Accelerator programme enabling you to take advantage of funding.

Multiple influencers

Increase Value	**Decrease Value**
Recurring Revenue/Contracts	Unpredictable Revenue
Higher Profits	Low Profits
Dependable Management Team	Dependency on Owners
Good Spread of Clients	Reliance on Few Clients
Highly Expandable	Poor Expansion
Growth Sector	Declining Sector
Sustainable	Volatile
Barriers to Entry, Niche, Intellectual Property	Highly Competitive Market
Growth Record	Low Economies of Scale
Solid Systems	Poor Infrastructure
Long Term Growth Plans	Weak Long Term Strategy

Timing and Personal Financial Review

An exit is best when the business is in good shape but with plenty of expansion prospects, making it attractive to buyers. The value should meet the aspirations of shareholders at a time when they personally wish to explore other options and secure time wealth. However, it is important to be objective about when is right for the business rather than being driven purely by personal aspirations. In the equation also sits tax and certainty. That is to say, capital from a sale is more certain than future earnings and a business sale is usually tax effective.

Income vs Capital

Sale proceeds are usually highly tax effective, compared to income which is typically taxed at between 40% and 50% once both corporation tax and dividend tax have been applied. Whereas, entrepreneurs selling their business can claim entrepreneurs' relief, reducing the Capital Gains Tax payable to just 10%. To be eligible, a shareholder must have a 5% or more shareholding in a qualifying business, and have been involved for a year or more with a company as an employee or director. Every UK resident has a lifetime allowance of £10,000,000 of gain that will be taxed at this reduced rate of 10%.

Entrepreneurs' Relief creates a significant argument for business owners to make money through capital gain rather than through ongoing profits. It is imperative that you compare the true net proceeds on sale with the net income you would receive should you keep the company. Sellers also need to allow for professional costs, including a mergers & acquisition adviser, a tax adviser, and accountant and a lawyer. For smaller companies, the professional costs are usually between 5% and 10% of the proceeds, and some of these costs will be payable pre-sale.

The calculation can be highly complex as there are so many factors consider. The table below provides a simple, basic calculation and highlights the income versus capital for a company making a net profit of £1m and assuming a sale value of £5m.

* This demonstrates with a £5m gross sale value which provides £4,384,800 net sale proceeds, the owner would need to achieve net earnings of £570,208 for 7.7 years to equal the net sale proceeds.

1 Year's Income (uncertain)	
Net Profit	£1,000,000
- Corp Tax @20%	-£200,000
- Dividend After Corp Tax	-£232,000
Total Net earnings	*** £570,208**
No of Years Earnings	7.7

Capital (certain)	
£5,000,000	Assumes Multiple of 5
-£360,000	- Estimated Legal and Brokers Costs
-£464,000	Assuming Entrepreneurs' Relief at 10%
+£208.800	Interest at 5% for 1 Year
***£4,384,800**	**Total Net**

Note that tax rates and reliefs are subject to change.

If You Decide to Sell

Position business in best light

A good data pack will not only contain current and historic company information but also forecasts and financial modelling around potential synergies. It will ensure optimum positioning of the business and as all information is prepared in advance, it will also accelerate the entire process. From the data a good adviser will produce a business summary marketing the acquisition opportunity without divulging your identity and a carefully crafted Information Memorandum to drive value by highlighting unique opportunities and potential synergies in your business to potential buyers.

Research and create competitive environment

In order to exceed the estimated business value it is essential to secure the right buyers which will create competitive bids and significantly increase sale price.

Intelligent, bespoke research should be conducted to identify potential purchasers using a combination of global intelligence tools and a database of active financial and trade buyers. It is essential to think outside the box and look at synergistic buyers as well as those within the same sector.

Through synergies and economies of scale available, the business will be worth differing amounts to different buyers. The optimal purchaser is one who has a "we want, we need" motivation who drives their own shareholder value via an acquisition. Carefully position synergies to several, interested parties utilising financial modelling and future visioning to demonstrate the strategic and financial benefits of the acquisition to drive competitive interest in the business inviting offers to enable the market to drive the price.

Negotiate and structure the right deal

Agreeing an exceptional deal requires significant experience and expertise. This takes understanding of the other side's motivators, and the ability to "walk in their shoes". Win the big points and lose the small ones to secure optimum terms. This is best achieved in a non-adversarial environment, where listening creates understanding, but with very clear presentation of the alternatives and key selling points. Timing and effective delivery of negotiation strategy are critical to create a win/win situation.

Today, there are increasingly complex deal structures in sales, with earn outs and deferred payments. Considering how best to protect these positions is also critical, and expert advice from the start will be crucial in this respect. There is also a trend in partial exits or elevator deals which enables owners to both capitalise on their exit but also keep in the business game. It also helps the buyer take the company to the next level but on a de-risked basis which should also result in owning shares with a greater value in the future.

Project manage to completion

Once a transaction is agreed a crafted Heads of Terms summarising the deal will avoid later misunderstandings, and again an expert adviser is invaluable here. The improved data-pack produced early on in the process will have given transparency which will accelerate the offer agreed to completion phase. Nonetheless, careful project management is required to manage the project to completion, orchestrating all the parties, and creating a timetable. Deal fatigue or worse failure, can result if a poor dialogue or slow information occurs once terms are agreed. The parties need to continue to listen and aim at a win/win transaction with your adviser acting as the middle man and orchestrating all parties.

Selecting an Advisery Team

Undertaking your business sale is one of the most important financial decisions you will make and expert help will enable you to achieve maximum value and optimum deal structure. Ensure you appoint an adviser based on track record, ability to create highly strategic transactions at maximum value, experience, research resources, international approach and technical deal structure knowledge.

It is important to make sure fees are linked to success deliverables; avoid high non-performance based time fees. The right adviser will engage with your objectives right from the start and will take the time to truly understand your business to ensure you achieve your goals. The process is complex and requires significant understanding and care. The dedicated adviser will manage the steps enabling you to maintain focus on your business.

Selection Checklist

? Do the advisers have a genuine and proven track record in the market place?

? Do they provide references from their sold, current and off-market clients? (If they can’t provide then best avoid them).

? Will it be the same consultant throughout to ensure a trusted relationship and a true understanding of your business?

? Does the consultant and organisation have the technical expertise to sell your business at maximum value?

? Is their research approach thorough to maximise your market?

? Are the fees linked to key steps in the sale process, rather than time based or monthly retainers?

? What is the average number of projects per consultant and are they are able to invest sufficient time on your sale?

? Are they giving best advice and suggesting a variety of options to achieve your goals?

? Are they respected in the industry or a preferred partner?

Conclusion

Achieving a successful business sale is a pinnacle point in any business owner's journey. It is the most effective route to time and financial wealth as well as the beginning of new ventures.

Accomplishing a successful sale is a complex process; the earlier preparation starts, the higher the rewards will be. Appoint a professional adviser with a proven track record and ensure that your business value is aligned with your personal and business objectives. If it is not, make sure you fully understand the alternative options to achieving your goals and the implications of these. Once you start preparing for sale, it's crucial that your business and the process are designed to maximise exit value.

About Avondale

Established in 1991, Avondale provide unrivalled award-winning business sales and strategy growth solutions with a success rate second to none. We are the Institute of Director's preferred supplier of business sales, mergers and acquisitions.

Avondale have genuine business acumen and are not only able to provide outstanding transactions but also practical solutions and guidance to achieve, if not exceed our clients' expectations.

Our work is predominately obtained via recommendation, a reflection of our technical abilities, strong service ethos and principles led approach.