



Strategic Planning – A Business Owner's Story

By Tom Gledhill

"If only I could find someone who could tell me what the buyers are looking for". I wish I had a nickel for all the times I said that in the years leading up to the sale of my company. Positioning your company for prospective buyers is the most critical element in maximizing your company's value. Without that knowledge – what the buyers want – you can't make the appropriate strategic decisions and you may leave a lot of money on the table.

I have some personal experience with this. I owned a software company that provided information technology to the health care market. In what I thought was a logical growth pattern, we expanded geographically into New York and New Jersey. We opened several sales offices in the area and hired salespeople to staff them. The cumulative cost of opening offices, hiring & training salespeople, travel, etc, was nearly a Million dollars. We also had to pay our trainers a premium (in addition to a per diem) as they didn't like to train in NY & NJ. We found that the market there wasn't willing to pay our standard rates, so we had to decrease our prices.

At about the same time we were being urged by some of our "early adopter" clients to develop an electronic medical record (EMR). We proceeded to do this at a cost of approximately \$750K and installed the system in three of our clients' facilities at an extremely reduced price. The extra support and maintenance required produced an additional set of costs not reflected in the above.

Our ultimate buyer already had sales offices in NY & NJ. They were interested in penetrating New England and they were having a hard time doing it. Whenever we competed against them in New England we beat them. Also, they had their own EMR. They were not interested in our technology; they were interested in our customer base, especially in New England.

So how does this affect value? In most cases, a company's value is a multiple of cash flow or EBITDA (Earnings Before Interest, Taxes, Depreciation, & Amortization). If we had NOT expanded into NY & NJ and NOT developed the EMR, we would have saved \$1.75 million which would have been added to EBITDA. Since value is a multiple of EBITDA, our company value would have increased substantially. An even better strategy would have been to take a fraction of the money that we spent penetrating NY & NJ and add a couple of more salespeople in New England, thus increasing our customer base in the buyer's desired territory. This most likely would have increased the multiplier effect, further increasing the company's value.



So what's the lesson learned here? Research the type of buyer that is most likely to buy your company. By knowing that, you can make the correct strategic decisions that will increase the value of your company. A good M&A Advisor (Intermediary) will help you identify the appropriate buyer type for your business (no, I didn't have a *good* intermediary!).

The most likely type of buyer for your company will depend on several factors – most notably the size of your company and the industry that you are in. We'll divide the universe of buyers into three broad types: *individual* buyers, *financial* buyers, and *strategic* buyers. Keep in mind that these buyer types can sometimes overlap with one another.

You will encounter individual buyers if your business is worth less than \$2 or \$3 million. They are usually not strategic buyers because they don't already own or operate a company. They were not a factor in my situation.

Financial buyers are generally more sophisticated buyers who are looking for an ROI in excess of 25-35% per annum. Financial buyers include Private Equity Groups (PEGs), large pools of capital collected in a Fund and used to invest in Private companies. A PEG may have been a good option for me. However, PEGs were not as numerous or visible then as they are today and, consequently, they were not considered an option in the acquisition of my company.

Strategic buyers are usually companies operating in the same industry: competitors, suppliers, or even customers. These buyers are looking for cost or revenue synergies – areas in which the combined company can increase its cash flows to a greater level than the two companies could achieve separately. For this reason, strategic buyers are most likely to pay a premium over what you may think your company is worth. Ultimately, a large, public competitor acquired my company and it was a pure strategic acquisition.

Had I kept this potential exit in mind at the *beginning* of the process, I would have positioned my company so I could have maximized value to the potential acquirer – thereby maximizing the proceeds from the sale. Always begin with the end in mind, and weigh carefully the impact those large strategic decisions may have on your company's value.