



De-risking Your Business to Create Value

Seth Webber

Learning objectives



- ▲ Understand the economic cycle, and where we are
- ▲ Understand impact of borrowing rates on cost of equity
- ▲ Understand relationship between risk and multiples

Agenda

- ▲ **1** Introduction
- ▲ **2** Economic Cycles
- ▲ **3** Inflation and Interest Rates
- ▲ **4** Impact on Cost of Capital
- ▲ **5** Multiples and Risk
- ▲ **6** Q & A





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Leads the Valuation Services Group

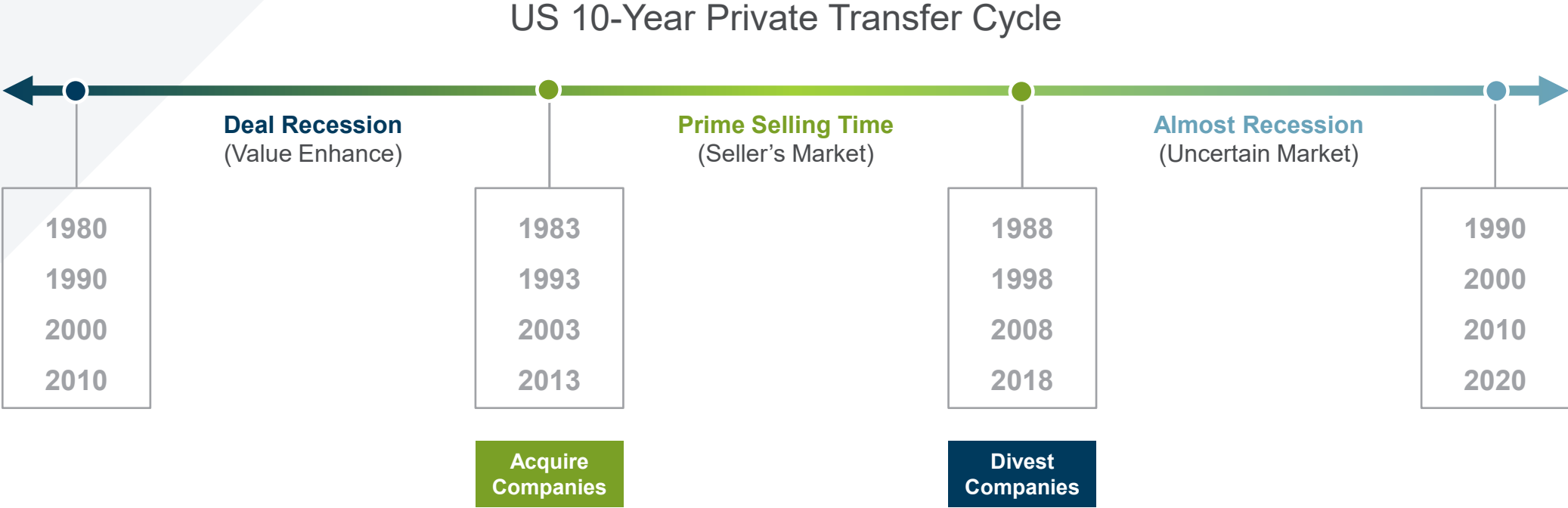
Co-authored “A Field Guide to Business Valuation” with Casey Karlsen.

Focused on helping owners and leaders understand how to drive value in their companies and organizations.

Valuation of closely-held businesses

- Mergers and Acquisitions
- Due Diligence Support
- Succession Planning
- Trust and Estate Planning
- Employee Stock Ownership Plans (ESOPs)

10-Year Private Transfer Cycle

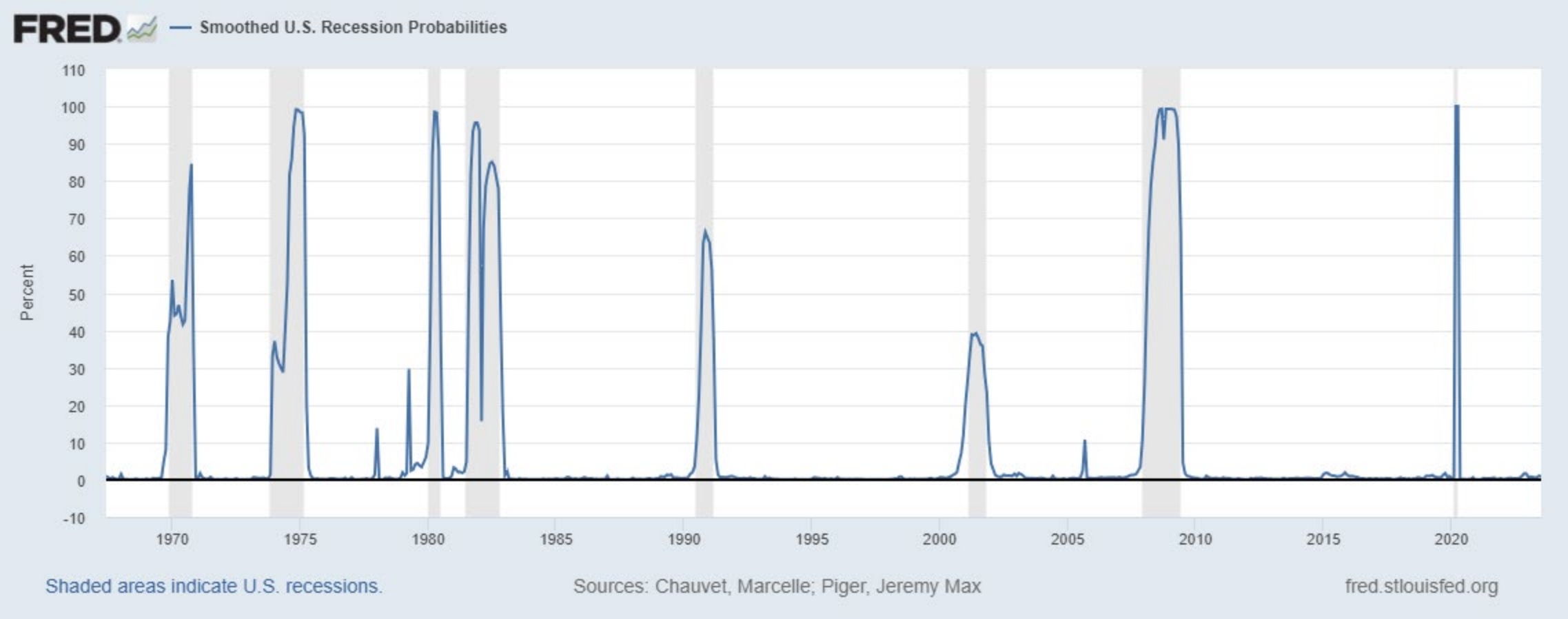


Rob Slee, Private Capital Markets, 2004



Recession Cycles

Smoothed US Recession Probabilities



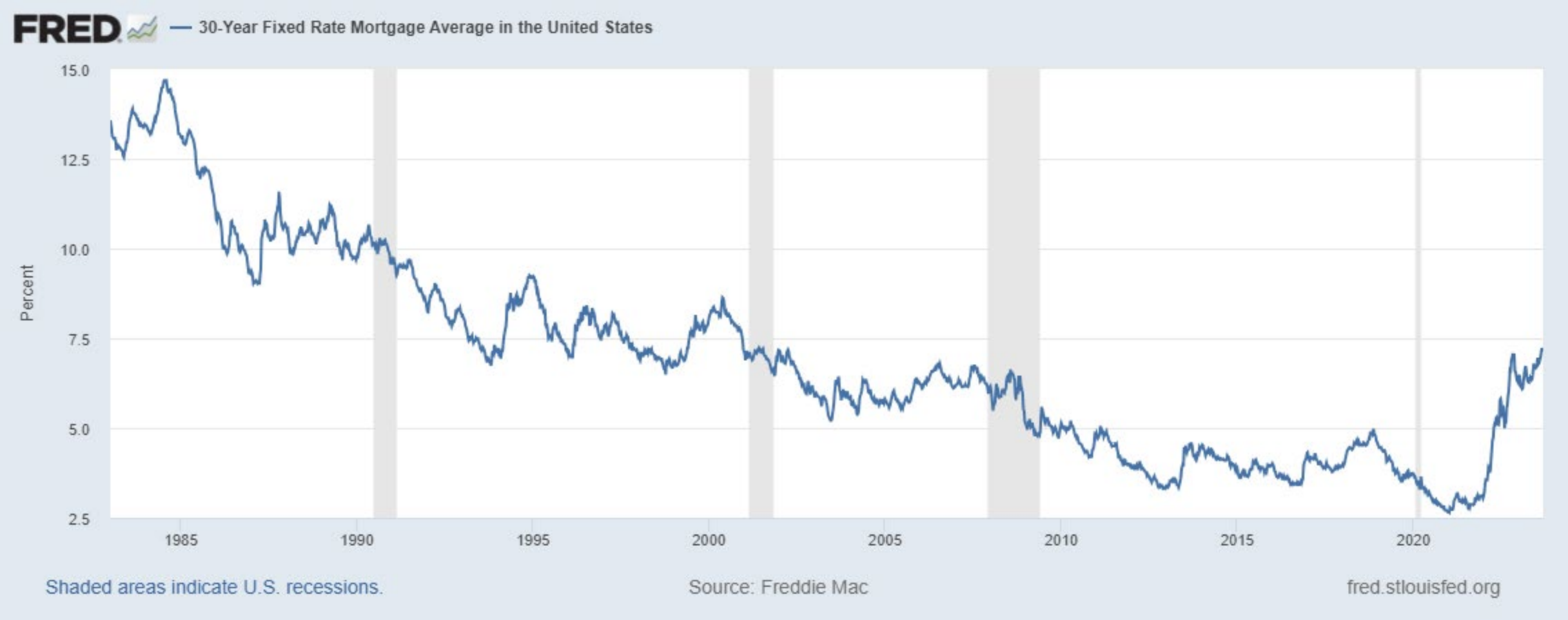
Inflation

Median Consumer Price Index – January '83 to July '23



30-Year Fixed Rate Mortgages

January '83 to September '23



Bank Loan Prime Rate

Past 10 Years

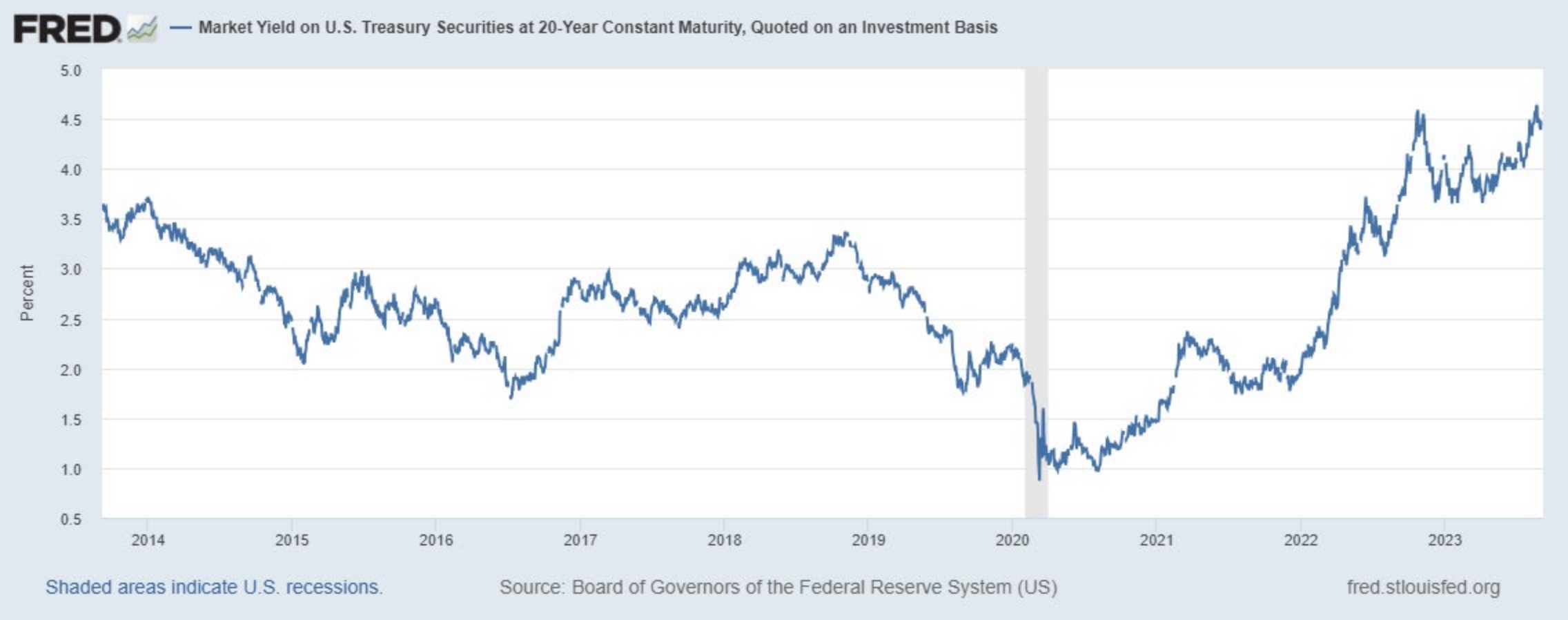


Polling Question #1



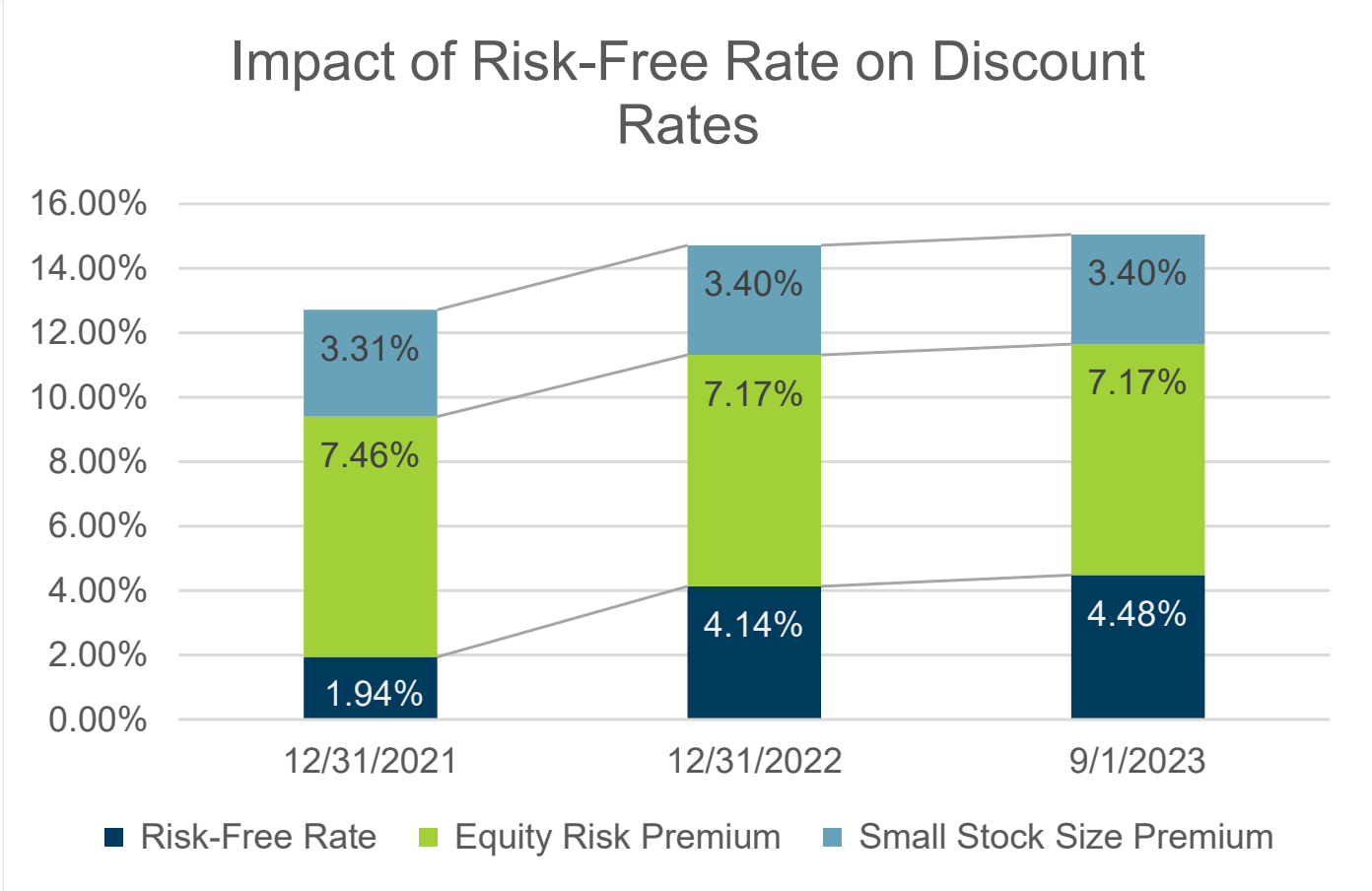
Yield on 20-Year US Treasuries

Past 10 Years



Impact on Cost of Capital

Interest rates alone have driven cost of equity up ~17% year-over-year



Polling Question #2



Multiples and Risk

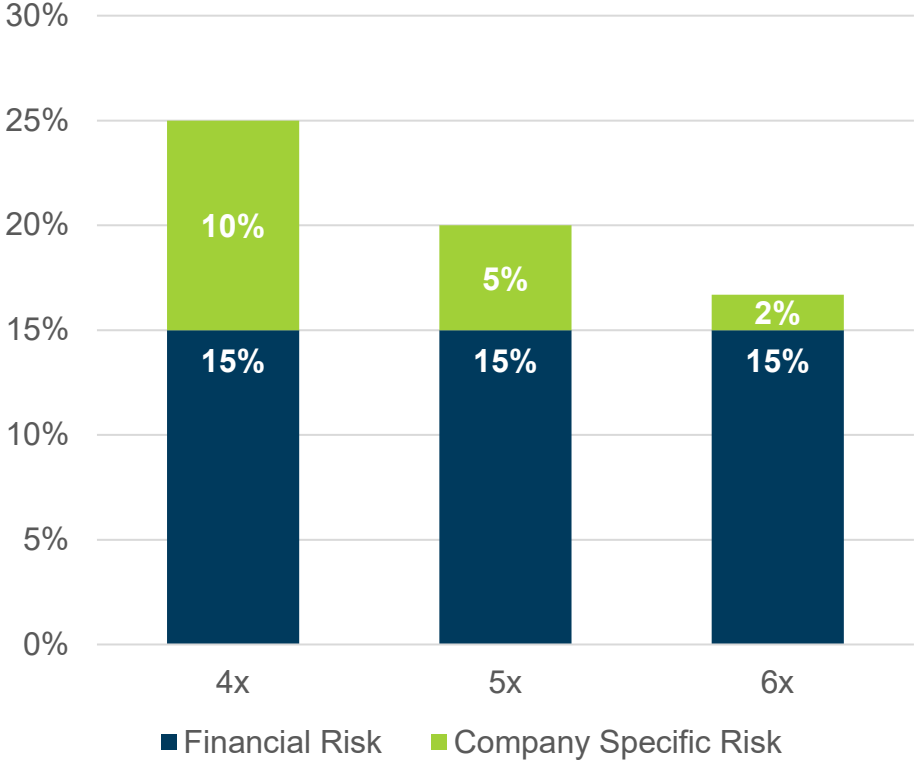
Company specific risk

- Financials
- Depth of management team
- “Key person” risk
- Competition
- Customers
- Suppliers
- Diversification

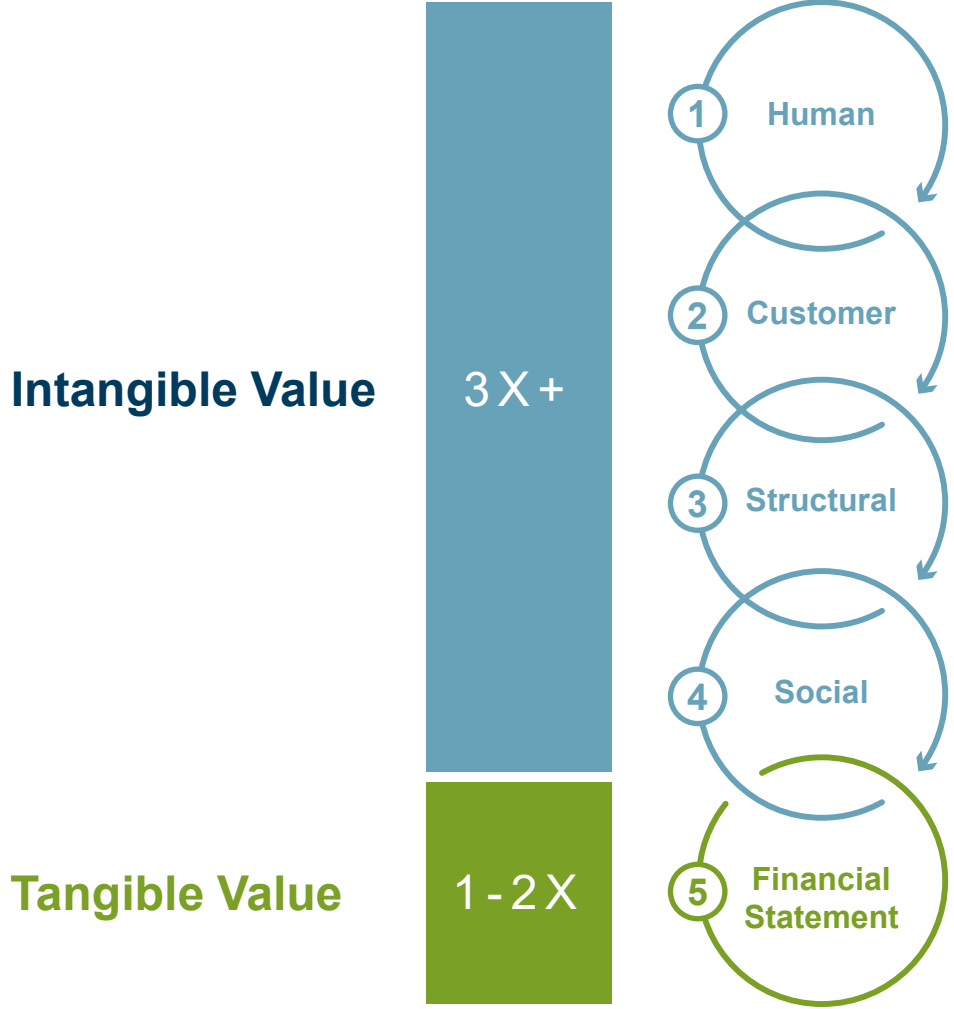
Financial risk

- Treasury Rates
- Equity risk premium
- Size
- Debt/equity ratios
- Industry performance

EBITDA and Rates of Return



What Impacts Multiple?



Human Impact on Multiples

< 4x	4x – 6x	6x
One-person operation (chief cook and bottle washer)	One- or two-person senior management team (two humans and a shaggy dog)	Well-rounded management team
No professional accounting staff	Controller on staff	Full-time CPA/CFO on staff
Owner takes all phone calls from customers	Dedicated salesperson on team	Full sales team that manages customers



Customer(s) Impact on Multiples

< 4x	4x – 6x	6x
Top 3 customers over 90% of revenue	Top 10 customers are less than 50% of revenue	No customer is more than 5% of revenue
Master service agreement with purchase orders	Annual contracts	Multiyear contracts
Local mom / pops are only customers	Middle market / regional businesses	Blue chip multinationals
Lumpy / project revenue	Mix of one-time / recurring revenue	Small, recurring purchases



Customer(s) Impact on Multiples - Continued

< 4x	4x – 6x	6x
High commodity product with low margins	Limited alternatives to your product with average margins	Proprietary product with high margins
No differentiation	Balanced market share across industry	Market leader with few competitors
No contracts	Annual contracts	Multiyear supply agreements with exclusivity
Core operations outsourced to supplier	Painful to switch suppliers, but not crippling	Easy to swap out non-performing suppliers
Top 3 suppliers are over 90% of material expense	Top 10 suppliers are over 50% of material expense	No supplier more than 5% of material expense
Small market size that is shrinking	Low market growth	Large market, growing rapidly



Structural Impact on Multiples

< 4x	4x – 6x	6x
No CPA / Compiled Financials	Reviewed Financials	Audited Financials
Little to no accounting systems	Limited information systems	Sophisticated information systems
No formal training or operating guidelines	Informal processes and reporting structure	Well-documented systems and processes
No explicit sales process	Sales process with uneven execution	Sales process with coordinated incentive programs
Heavy government pressures / regulation that constrains business	Heavy government pressures / regulation that promotes the business	Little government involvement



Social Impact on Multiples

< 4x	4x – 6x	6x
Completely discretionary (unimportant)	Should / need to have your solution (can pick from many like companies)	Product / service is “required” (best in breed or sought out for work)
No / low employee engagement	Divide between management team engagement and hourly employees	Collaborative culture
Reactionary culture, no driving vision	Vision / strategic plan created as an exercise, not widely shared or updated	Well articulated vision of “to-be” state with engagement by key stakeholders
Suppliers can sell directly to your customer base (bypass)	Occasional / hybrid competition	Exclusivity / non-compete as part of the contract
Completely discretionary (unimportant)	Should / need to have your solution (can pick from many like companies)	Product / service is “required” (best in breed or sought out for work)



Questions?

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