

## INSIDE THIS ISSUE

<b>Feature Article:</b> Which Buyer is Best for Your Company?	1 & 3
<b>Expert Tips:</b> How to Create a Marketable Business	1 & 4
<b>Trends To Act On:</b> A Review of 2007 M&A Activity	2
<b>Exit Planning:</b> Is Your Business Ready to Be Sold?	2

## FEATURE ARTICLE

### *Which Buyer is Best for Your Company?*

**By Scott T. Wait, CPA**

Business buyers come in different shapes, sizes and motives. Having a good exit plan can provide you peace of mind and future financial security. I recently spoke with Tom Gledhill, founder of Boston-based Delta Capital, who has built and sold four different businesses in his career. Two mistakes he made with his businesses: lack of planning for his exit and poor strategy to attract a preferred buyer who would pay a premium price for his companies.

Initial steps to a solid exit plan start with understanding the types of buyers and their goals as buyers. There are three general types of buyers: the strategic buyer, the financial buyer and the individual buyer.

The strategic buyer can be any of the following — a competitor, a major supplier or a major customer. An example of a strategic buyer in the news was FedEx buying Kinko's copy center franchises.

*(article continued on page 3)*

## EXPERT TIPS

### *How to Create a Marketable Business*

**By Enrique Brito, CFA, AVA, CM&A**

Most business ventures get started by entrepreneurs who are capitalizing on their experience, skills and contacts. Typically for the first few years the owner is the main engine behind the business' growth with delegation being exercised grudgingly and sporadically. Consequently, as the business grows and succeeds in the marketplace, it becomes more and more difficult to separate the business from the owner.

The synonymous merging of business and owner is fairly common in the service industry. However, while the business may be successful in its own right, it may not be worth much in terms of market value. This is because the knowledge, processes and skills are the owner's and as a result, it is nearly impossible to transfer them without a management transition period that is likely to take several years.

Many people start consulting practices as solo practitioners, and while many remain that way, others bring in additional resources as the business grows. If the entrepreneur's objective is to create a personally satisfying job that makes use of his or her talents, experience and skills, then developing a solo practice may enable him or her to fulfill that goal; however, if the objective is to build a marketable



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## TRENDS TO ACT ON

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### *A Review of 2007 M&A Activity*

By **Zubin A. Patel**

In 2007, deal activity declined slightly in deal count and deal size versus 2006. In the US, there were approximately 2,660 M&A transactions valued from \$5 million to \$500 million. Deals valued at in excess of \$250 million actually posted increased activity. However, Flashwire reported that both strategic and private equity buyers experienced slow-downs in deal flow versus 2006.

For 2007, the monthly deal count ranged from 700 to 1,000. Over the course of 2007, the average aggregate monthly deal value was \$105 billion. However, much of the deal flow was generated in 2007's first two quarters and M&A activity peaked in May when 944 deals were closed with an aggregate value exceeding \$215 billion. Deal volume and aggregate deal value have slowly declined since June 2007. The average EBITDA multiple paid in 2007 was between 10x and 12x. Mergerstat, LLC reported that 2007's leading industry in M&A transactions was Computer Software, Supplies and Services.

## EXIT PLANNING

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### *Is Your Business Ready to Be Sold?*

By **Enrique Brito, CFA, AVA, CM&A**

If you are running a successful business, it is highly probable that you will eventually be approached by a potential buyer. But are you ready?

Given that your business most likely represents the largest portion of your net worth, you should prepare in advance for the day that you will sell your business. If you can do that, chances are good that you will maximize the opportunity to get full market value for your business. At the very minimum, your preparation should include the following elements:

- Determine your business' worth and the factors that enhance and impair its value,
- Clean and update your financial statements so they reflect the true operating assets of the business, as well as its true profitability and discretionary cash flow,
- Secure your key employees with employment contracts and establish a bonus program that rewards them for staying with the company for some period,
- Determine the tax implications of a potential sale to establish the most advantageous method to structure the sale for tax purposes,
- Take care of potential "deal killers," such as expiring leases, obsolete inventory, equipment that needs to be maintained/replaced, customer concentration issues, pending litigation and so forth, and
- Organize a professional team that will help you obtain the highest value for your business. This team should include an accountant, a transaction attorney, a wealth manager, a business valuation expert and an investment banker.

You can increase your wealth by knowing a few simple ground rules for successfully selling your business. Spending the time and money to discover and fix your company's problems now will pay large dividends in the form of increased company value, which is exactly what you want when it's time to sell.

For further information on exit planning, please visit The McLean Group's Exit Strategies Institute site at [PlanYourExit.org](http://PlanYourExit.org).

## FEATURE ARTICLE

### *Which Buyer is Best for Your Company?*

(CONTINUED FROM PAGE 1)

The strategic buyer is interested in increasing its company-wide earnings and cash flow for the short and long term. Strategic buyers also are interested in economies of scale and strategic fit with its overall profit goals. They prefer to pay for the seller's stock, not its assets, because their desires are to increase earnings to their stockholders. It usually can cash out the seller and has little or no interest in future time commitment from the seller.

Financial buyers will also pay hefty prices and pay for a seller's company stock. A major difference in this buyer's motive vs. strategic buyers' motives is that financial buyers generally will not pay as high of a premium as strategic buyers. Financial buyers mainly are Private Equity Groups (PEGs) that are interested in assembling a portfolio of companies. The PEGs are looking for bargains or companies with tremendous future profit growth.

Many of their prospects are companies that need to improve their internal efficiencies or scale up operations from a regional to national scale. PEGs usually have the ability to cash out the sellers but may require a significant future commitment from the sellers including profit targets in the agreement.

Individual buyers may be sole owners or groups of investors that gather funds to buy various kinds of businesses. They generally have different motives on structuring their deals and many times, wish to buy the seller's assets, not the company stock. Individual buyers also are interested in maximizing the company's depreciation to reduce tax liabilities in the early years following the purchase.

These buyers are usually the weakest buyers financially. Financing is a major issue in negotiating these deals. Individual buyers usually require the sellers to commit two or more years to profit targets and other terms to complete the sales.

Understanding the three types of buyers (strategic, financial and individual) and their respective goals will provide you with the essential knowledge needed to generate the best transaction. This knowledge, combined with the establishment of a solid exit plan, will give you a solid position when the time arrives for your to sell your business.



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**Have A Question?**

**Please submit any topics of interest to [egins@mcleanllc.com](mailto:egins@mcleanllc.com) with the subject: "M&A Market Update Topics" and we will try to address it in the next issue!**

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**EXPERT TIPS*****Creating Value Through M&A Transactions*****(CONTINUED FROM PAGE 1)**

business that can be sold in a few years, a different strategy will be needed.

In essence, the value of a business for a prospective buyer resides on the potential for the business to generate enough cash flow (revenues less operating expenses) to enable the buyer to recuperate the original investment and realize (and probably exceed) a given rate of return. Of course, the business' past performance will provide the buyer with anecdotal evidence about the enterprise's potential to generate the earnings necessary to meet the buyer's objectives. However, the risk for the buyer resides on whether or not past performance can be repeated and even surpassed in the future.

Having a business that is too dependent on its owner is certainly one of the main factors affecting its marketability. But this is not the only factor as there are other issues that will also have an impact on the potential marketability of a business, such as:

- Inexperienced management teams,
- High customer concentration (having just a few large customers),
- Poorly maintained financial records,
- Poorly maintained assets,
- Contingent liabilities, and
- Threats of litigation

In the end, the acid test for an owner who wants to find out how marketable the business is revolves around the answer to a simple question: Can I afford to leave the business for a couple of months without any significant deterioration in its performance? The answer to this question not only can be quite revealing, but also points out the need for a change in his or her leadership strategy.

*"Can I afford to leave the business for a couple of months without any significant deterioration in its performance?"*

**ABOUT THE McLEAN GROUP**

The McLean Group is a national investment bank providing merger and acquisition (M&A), capital formation, business valuation, litigation support and exit planning services. The McLean Group serves middle-market businesses generating up to \$500 million in annual revenues. Headquartered in Washington, DC's technology, communications and government contracting corridor, the firm is among the largest independent middle-market investment banks in the region. The McLean Group is a FINRA Registered Broker Dealer and Member FINRA/SIPC.