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Want to Build Business Value In A Recession?

Michael Wildeveld, CEPA, M&AMI, CM&AP, CM&AA, CBI, CBB
michaelw@veldma.com

Veld Mergers & Acquisitions
www.veldma.com
1 Park Plaza, 600
Irvine, CA 92614
310-652-8066

In an economy when many of us are tempted to bury our heads until the shooting is over, smart business owners are realizing that this may be the perfect time to acquire smaller, less adaptable, less capitalized or less well-managed competitors.

As the *sellers* of goods or services, owners sometimes forget that they, too, can be buyers. And in this buyer's market, you can expect to find not only lower purchase prices, but also much more attractive seller-based financing and earn-outs.

Consider for a moment that many of your smaller competitors are experiencing a fall in revenue that portends the end of their company's viability. While their overhead is not large by your standards, it represents such a substantial percentage of their revenue that, as revenue sinks, they simply cannot correspondingly reduce overhead. The hypothetical business owner, Bob Eustice's company, All-City Printing, is a good example.

For a good many years, All-City enjoyed a solid business based upon servicing many of the area's top companies. When this economic downturn began, Bob prudently pruned expenses and actually increased the company's gross margins. But he didn't stop there.

Bob began acquiring less fortunate competitors who were unable to weather the downturn. These businesses were much smaller and undercapitalized. Less profitable in the good times they quickly became unprofitable when business declined. Their owners had two options: liquidate and receive very little (if any money) or sell to All-City.

Bob contacted the owners of several smaller print shops whom he thought would consider selling. Within 12 months he acquired three such businesses, or, more accurately, parts of three businesses. Here's how he structured the purchases:

- All-City acquired only those assets it could immediately use, such as equipment directly used in printing operations. Usually this simply meant assuming existing equipment leases. If Bob purchased other equipment, he paid cash.

- All-City bought the customer lists. As All-City received payment from customers, it paid the sellers for their lists. For two years, All-City paid each seller 10 percent of the future gross revenues received by All-City from that seller's customers. Payment in this form of "earn-out" was likely more money than the sellers would have received from those customers had they not sold. With its greater efficiencies and economies of scale, All-City was easily able to generate enough cash flow from these new customers to make the payments.

The net result for All-City was a very low risk acquisition financed by future cash flows of that acquisition with the promise of increased future revenues.

All-City's acquisition methods are far from unusual in times like ours. In many situations, owners are able to acquire businesses — or the parts of businesses they want — with little up-front cash and no bank financing. While you would not sell your company on these terms, they may be the best — and only terms — offered to a less well-positioned competitor.

This is just one acquisition technique you can use to build the value of your company during a recession. If you have questions about other techniques or how to evaluate potential acquisition candidates, contact us.