

**THE MERIDIAN GROUP**

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**THE SELLING PROCESS**

**A Guide for Market**

**Divestitures**



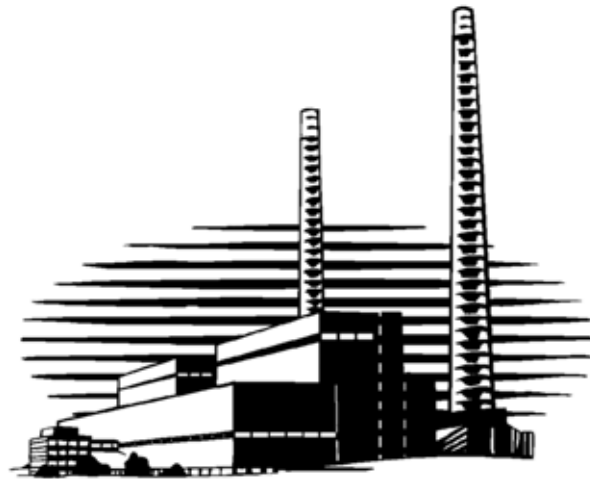
***FORMULATE  
YOUR PLAN***



## FORMULATE YOUR PLAN

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# DETERMINE WHAT IS FOR SALE



- *Assets?*
- *Stock?*
- *Intangibles?*
- *Earnings Potential?*



## FORMULATE YOUR PLAN

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- Assemble Your Team
  - ❖ Investment Banker
  - ❖ Legal Counsel
  - ❖ Accountant
  
- Establish Pricing Strategy and Alternatives
  
- Develop Marketing Plan
  
- Identify Preferred Deal Structure



## FORMULATE YOUR PLAN

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### GLOBAL PLAN STRATEGIES

- Control the Process
- Clearly Define Goals and Objectives
- Take Time to Make Informed Decisions
- Keep in Perspective that a High Portion of Personal Net Worth is at Stake



***ESTABLISH  
REASONABLE VALUE***



## ESTABLISH REASONABLE VALUE

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# ECONOMIC REALITY - WHAT IS FOR SALE?



- Why Does It Make Money
- What are the Risks
- What are the Strengths and Weaknesses
- How Strong are the People and the People Relationships
- What is the Profit Making Potential



## ESTABLISH REASONABLE VALUE

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### VALUE - DETERMINANTS

- The Value the Seller gets at Closing depends on:
  - ❖ The Effectiveness of the Marketing Plan
  - ❖ The Buyer's Perception of the Inherent Value of the Business
  - ❖ The Skills of the Negotiator



## ESTABLISH REASONABLE VALUE

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### **BUYER'S VALUE DEPENDS ON PURPOSE**

- Liquidation
- Eliminate Competition
- Avoid Start-up Risk
- Acquire Key Management/Employees
- Enhance Portfolio Return
- Extend Distribution Network
- Increase Sales
- Acquire Manufacturing Capability/Capacity
- Extend Product Lines
- Capture Synergies and Cost Savings if a Combined Entity



## ESTABLISH REASONABLE VALUE

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# BUSINESS VALUATION

- Is It Necessary?
  - ❖ Most Companies Sell Within Standard Multiple Ranges of EBITDA and Net Book Value
  - ❖ Ranges Vary With the Lending Environment and the Supply of Capital
- Seller Needs to Have a Realistic Understanding of the Company's Value Prior to Offering It for Sale



## ESTABLISH REASONABLE VALUE

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# QUANTITATIVE PRICING ELEMENTS

- Trends in Financial Performance
- Industry Performance
- Earnings Volatility
- Asset Base
- Leveragability
- Expected Cost Efficiencies
- Anticipated Financial/Tax Benefits
- Price/Earnings Ratio



## ESTABLISH REASONABLE VALUE

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# QUALITATIVE PRICING ELEMENTS

- Seller's Timing Objectives
- Glamour of the Industry
- Numbers of Buyers in the Market
- Deal Structure Acceptable to Seller
- Quality of Earnings
- Market Synergies
- Private Equity and Lending Market Environments



## ESTABLISH REASONABLE VALUE

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# VALUATION TECHNIQUES

- Discounted Cash Flow  
("Going Concern")
- Market Multiple
- Transaction Multiple
- Orderly Disposition Value
- Forced Liquidation Value

**ESTABLISH REASONABLE VALUE****DISCOUNTED CASH FLOW EXAMPLE**

\$ 000's	<u>Year 1</u>	<u>Year 2</u>	<u>Year 3</u>	<u>Year 4</u>	<u>Year 5</u>	<u>Residual Value</u>	<u>Equity Value</u>
Revenue	\$ 25,000	\$ 26,250	\$ 27,563	\$ 28,941	\$ 30,388		
Oper. Exp.	<u>15,000</u>	<u>15,675</u>	<u>16,380</u>	<u>17,117</u>	<u>17,888</u>		
EBIT	\$ 10,000	\$ 10,575	\$ 11,182	\$ 11,823	\$ 12,500		
EAT/BI	\$ 8,000	\$ 8,460	\$ 8,946	\$ 9,459	\$ 10,000		
Add: Depreciation	1,000	1,100	1,210	1,331	1,464		
Inc. in Def. Tax	200	209	218	228	239		
Amortization	<u>600</u>	<u>627</u>	<u>655</u>	<u>685</u>	<u>716</u>		
Funds Provided	\$ 9,800	\$ 10,396	\$ 11,029	\$ 11,702	\$ 12,418		
Less: Cap. Exp.	(2,000)	(2,090)	(2,184)	(2,282)	(2,385)		
Inc. in Work. Cap.	<u>(400)</u>	<u>(418)</u>	<u>(437)</u>	<u>(456)</u>	<u>(477)</u>		
CFBI	\$ 7,400	\$ 7,888	\$ 8,408	\$ 8,964	\$ 9,556	\$ 87,500	
PV of CFBI							\$27,804
PV Resid. Value							<u>43,503</u>
Total Capital Value						\$	71,307
Less: Debt							<u>(15,000)</u>
Total Equity Value						\$	56,307

\*Assumes Multiple of 7 times EBIT of \$12,500



## ESTABLISH REASONABLE VALUE

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# MARKET MULTIPLE ATTRIBUTES

- Attributes of Comparability:
  - ❖ Type of Product
  - ❖ Market Segment
  - ❖ Geographic Area
  - ❖ Market Position
  - ❖ Size
  - ❖ Growth - Historical and Projected
  - ❖ Leverage
  - ❖ Liquidity
  - ❖ Diversification
  - ❖ Perceived Market/Business Risks



## ESTABLISH REASONABLE VALUE

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# TYPICAL MARKET MULTIPLE RATIOS

- Operating Multiples
  - ❖ Price to Earnings, Cash Flow or Revenues
  - ❖ Total Capital to EBITDA, EBIT, Revenue, or “Free Cash Flow”
  
- Balance Sheet Multiples
  - ❖ Price to Book
  
- Other Multiples
  - ❖ Price to Unit (Commodity Comparisons)
  - ❖ Market Capital to Population



***PREPARE FOR  
THE PROCESS***



## PREPARE FOR THE PROCESS

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# LONG RANGE PLANNING FOR THE SALE

- Develop Key Management
- Maintain Good Record Keeping/Accounting Policies
  - ❖ Accounts Receivable and Inventory should be Tightly Controlled
  - ❖ Develop History of Achieving or Exceeding Financial Projections
  - ❖ Resolve Payable and Litigation Issues
- Continue Capital Investment/Maintenance
- Control Owner/Family Deductions
- Transfer Relationships from Exiting Owners to Current Management
- Secure 1st Contracts to Enhance Backlog



## PREPARE FOR THE PROCESS

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# LONG RANGE PLANNING

- Eliminate Poor Performing Product Lines
- Sell Unprofitable Divisions/Subsidiaries
- Restructure Debt and/or Equity
- Review/Revise Labor Agreements
- Keep Current with Industry Practices and Technology
- Reduce Unneeded Overhead



## PREPARE FOR THE PROCESS

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### PREPARING FOR THE PROCESS

- Develop Communications Plan for Informing Key Employees, Customers and Suppliers
- Gather Pertinent Marketing and Operational Data
- Gather/Develop Information
  - ❖ Equipment Lists/Appraisals
  - ❖ Real Estate Appraisals
  - ❖ Union/Employee Contracts
  - ❖ Environmental Audits



## PREPARE FOR THE PROCESS

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# PREPARING FOR THE PROCESS

- Organize Financial Information
  - ❖ Five Year Historical Financial Statements
  - ❖ Three-Year Pro Forma Statements
  - ❖ Historical Tax Returns
  - ❖ Backlog Statistics
  - ❖ Revenue Trends by Customer
  - ❖ Inventory Listing
  - ❖ Aging Reports for Accounts Receivable and Payables
  - ❖ Depreciation Schedules
  - ❖ Product Sales and Cost Information
  - ❖ Detailed SG+A Analysis
  - ❖ Adjustments to EBITDA
    - Non-Recurring Events
    - Excess Owner-Related Expenses
    - Unusual Events
  
- Create Dataroom for all critical Information



## PREPARE FOR THE PROCESS

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# OFFERING MEMORANDUM

- Generate Offering Memorandum
  - ❖ Clearly identify the Seller's Objectives
  - ❖ Give a Comprehensive Description of the Business
  - ❖ Restate Income Statements to Exclude Non-Recurring Costs and Expenses:
    - Excess Salaries
    - Perquisites
    - Personal Expenses
    - Life Insurance and Retirement Plans
  - ❖ Restate Balance Sheet to Exclude Items Not Being Sold



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***MARKET YOUR  
OPPORTUNITY***



## MARKET YOUR OPPORTUNITY

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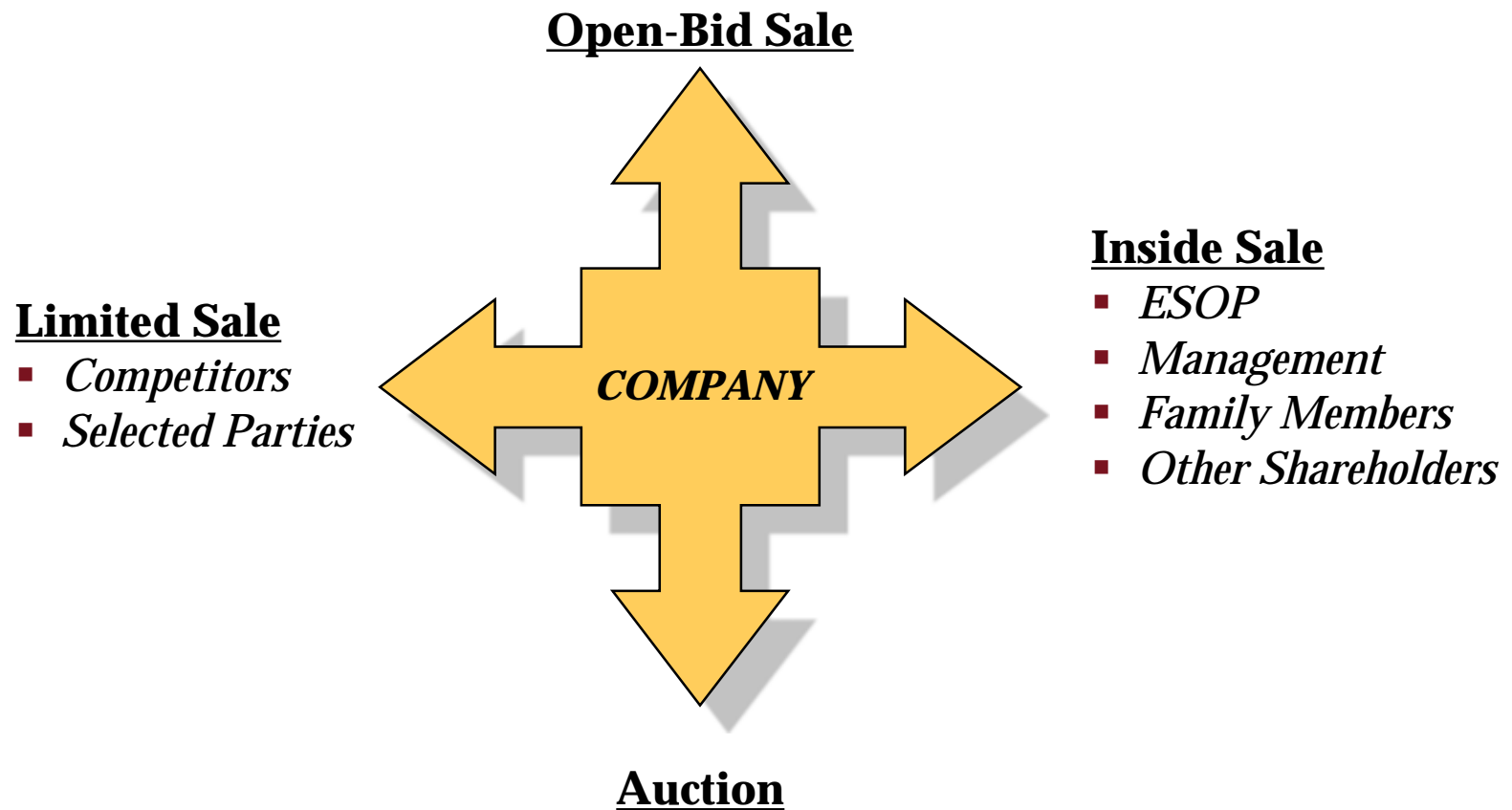
### TYPES OF BUYERS

- Strategic Buyer
- Foreign Entity
- Financial Buyer
- ESOP/Employees
- Management
- Insiders/Family



## MARKET YOUR OPPORTUNITY

# DETERMINING METHOD OF SALE





## MARKET YOUR OPPORTUNITY

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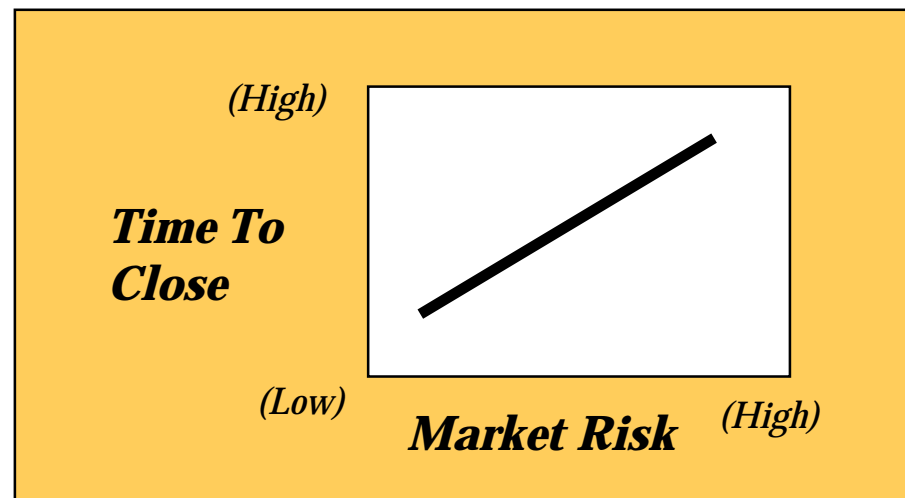
# MARKET YOUR OPPORTUNITY

- Develop Marketing Plan Based on Seller's Sensitivity to Confidentiality
  - ❖ Conduct Direct Mail Campaign
  - ❖ Advertise Opportunity through Trade Journals and Professional Organizations
  - ❖ Utilize Industry Referrals and Professional Community
  - ❖ Source Existing Databases
  - ❖ Search/Advertise on the Internet
  - ❖ Develop Target Buyer List with Management Team - Competitors, Suppliers, Customers



## MARKET YOUR OPPORTUNITY

### RECOGNIZE MARKET RISK



*The longer the time it takes to close, the greater the risk that confidentiality will be breached and employees, customers and suppliers will be lost.*



***DUE***  
***DILIGENCE***



## DUE DILIGENCE

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# THE DUE DILIGENCE PROCESS

- Qualify Interested Buyers
- Obtain Confidentiality Agreements
- Distribute Offering Memorandum
- Conduct Tours and Dataroom Visits
- Address Additional Information Requests



## DUE DILIGENCE

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### QUALIFY THE BUYER

- Financial Capabilities
- Operational Expertise
- Level of Interest
- Competitive Posture
- Employee/Union Philosophy
- Analyze Long-term Objectives for Acquisition
  - ❖ Merger
  - ❖ Expansion
  - ❖ Elimination of Competitor



## DUE DILIGENCE

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### THE DUE DILIGENCE BY BUYER

- Financial Examination
- Union/Employee Contract Review
- Operations Assessment
- Competitive and Marketing Analysis
- Legal Review
- Environmental/Governmental Audit
- Intellectual Resource Review



# ***NEGOTIATIONS***



## NEGOTIATIONS

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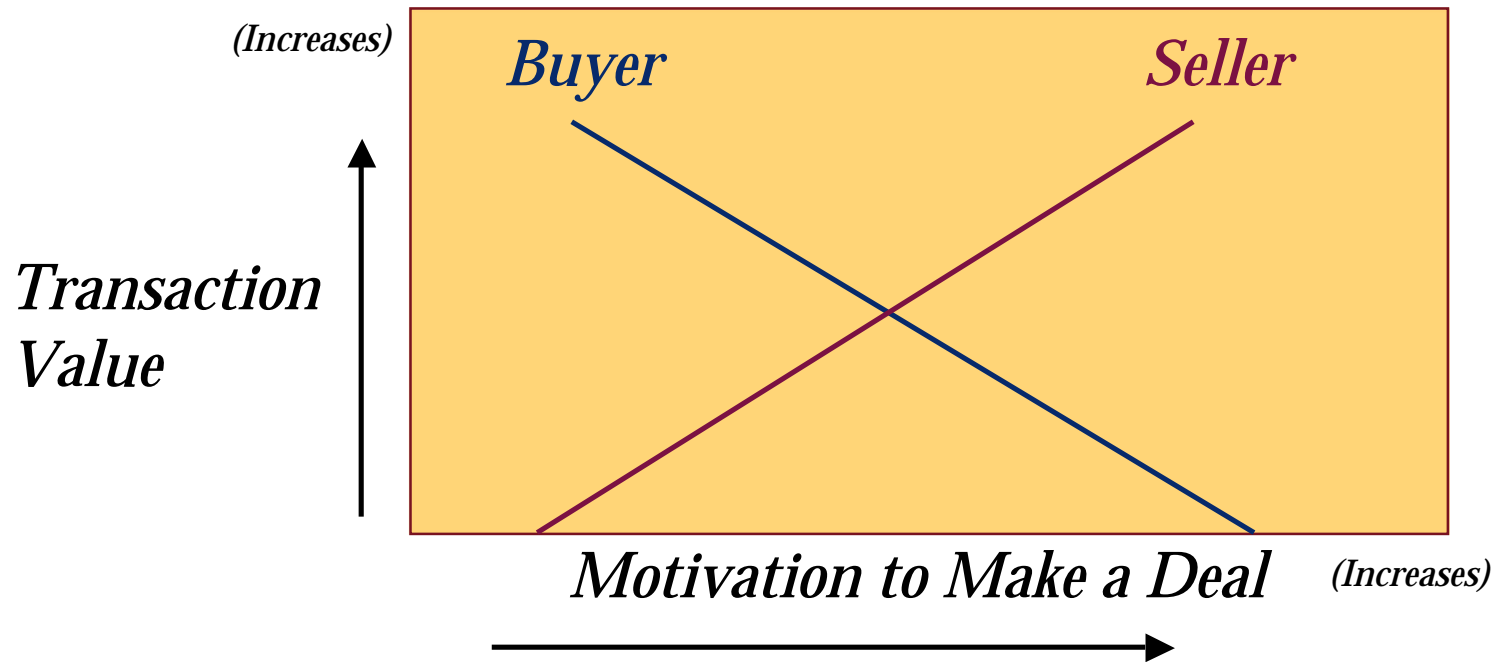
# NEGOTIATIONS

- Reassess Objectives of the Sale
- Understand Legal and Financial Implications of Negotiations
- Be Creative to Avoid Deal Collapsing
- Control Emotions
- Keep the Target in Sight
- Be Flexible
- Negotiate a Detailed Letter of Intent



## NEGOTIATIONS

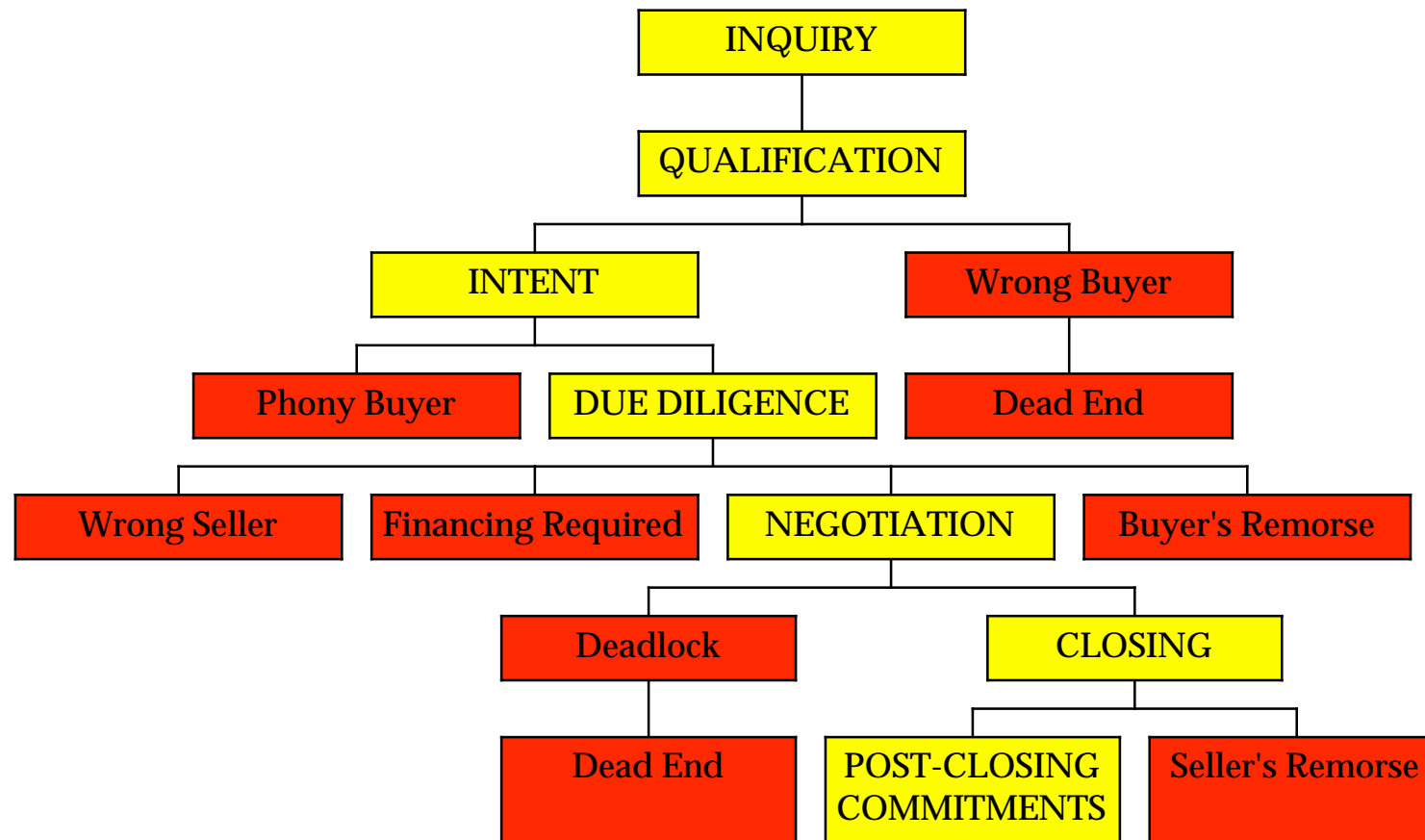
# NEGOTIATION - THE RANGE OF SETTLEMENT





## NEGOTIATIONS

# THE NEGOTIATION PROCESS





## NEGOTIATIONS

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### DEAL POINTS

- Price
- Structure
- Payment Terms
- Taxes
- Future Commitments
- Legal Issues
  - ❖ Degree Of
- Representations and Warranties
- Level of Escrow, Holdbacks , and Setoffs



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***CLOSING***



## CLOSING

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- Complete Definitive Agreements
- Prepare Schedules Supporting Legal Documents
- If Not Already Done, Inform Employees, Customers and Suppliers
- Keep the Pace Moving Forward
- Be In Control of the Deal



***FULFILL  
POST-CLOSING  
COMMITMENTS***



## **FULFILL POST-CLOSING COMMITMENTS**

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# **FULFILL POST-CLOSING COMMITMENTS**

- Adjustments
- Earn Outs
- Consulting Agreements
- Set-Off Provisions
- Non-Compete Agreements
- Severance Issues for Employees
- Final Preparation of Schedules and Document Transfers