

A blue-tinted photograph of a business meeting. Two people in suits are seated at a desk, looking at various documents. One document features a line graph titled 'Business activity of companies and subdivisions' with a y-axis ranging from 15 to 25. Another document shows a pie chart labeled 'Relative' and a world map. A laptop is open in the background. The overall scene conveys a professional and analytical business environment.

FINDING THE REAL VALUE OF A GROWING BUSINESS

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Finding the Real Value of a Growing Business

It is not unusual for buyers to base their valuations of a company using multiples. Multiples are compare one financial metric with another and can then be used to make a comparison with different businesses. In an acquisition and merger situation enterprise value (EV) multiples are the ones to use. There are various multiples that can be used. Some examples are :

- EV/Sales. This can be affected by different accounting techniques.
- EV/EBITDA. Enterprise Value to Earnings Before Interest, Tax, Depreciation, Amortization. This is used to lessen the divergences because of bookkeeping methods and is by far the most used multiple
- EV/Invested Capital. Used for capital heavy industry.



When they are used appropriately multiples are a useful tool, but it has to be remembered that a single figure cannot do justice to the complexities of a business. There will be many other factors that can affect the value of the business. In particular when buying a business this single figure which is a representation of a single period of time, doesn't show the direction in which the company is moving or how much it is growing. Even additional multiples will normally only show short term changes rather than how things are likely to continue in the long term. Many buyers will come up with a low evaluation figure of a growing business, when using a multiple of the past year or even taking a weighted average of several previous years. The following comparison will help to show how these figures do not really show the true worth of a business :

Let's look at two different businesses, one is growing steadily along with a growing market potential and the other has been an ever decreasing cash flow within a shrinking market. Both these businesses have the same value when using a standard multiple, but anyone can see that they do not have the same worth. If using a weighted average then we would find we are even further from the right conclusion. The business in decline would be the one that looked like it had the best value and the business which is growing the least. This turns things completely on their heads.



So, how should these companies be evaluated? Well, one method is to make a prediction about the earnings over the long term. A formula that can help with this is the Gordon growth model formula. This is useful where there is a steady growth rate.

The stable model formula consists of the following parameters :

- Value of the company = $D1 / r - g$
- D1 = the annual expected earnings of the next year
- r = rate of return
- g = the expected earnings growth rate (assumed to be constant) over the long term

A more complicated method would be to consider alternative scenarios according to various projections. The result will no longer be one figure, but a range, but it will be more realistic and take into account the complexities of the company. However, even these figures are only a starting point. Much of the value of any business is the strategic value and its synergetic benefits to a particular buyer.



In summary, the standard method of using a multiple to work out the value of a business can be very misleading and a weighted average even more so, particularly as it does not show the growth of the company and its potential in the future. There are other formulas that can be used to include the growth potential, but even these do not allow for the synergetic benefits. All these things should be taken into consideration and the optimum value can only be found with the right buyer.



Our M&A Process

TARGET APPRAISAL	APPROACH	DUE DILIGENCE	NEGOTIATION & CLOSE	POST MERGER INTEGRATION (PMI)
Key Areas				
<ul style="list-style-type: none"> Target & market analysis; Initial assessment of synergies & value drivers; Indicative valuation; Go or No-Go decision; Preparation of transaction documents (NDA – Non-disclosure Agreement/LOI-Letter of Intent); Select Transaction team; Appoint advisors; Consider funding ability. 	<ul style="list-style-type: none"> Initial approach letter; Signing of NDA; Prepare & share initial information requests; Formulation of LOI (Letter of Intent) & possible negotiations; Initial meeting and Q&A; Circulate information on the Target to the Transaction team. 	<ul style="list-style-type: none"> Set scope of due diligence; Set up VDR (virtual data room); Coordinating of due diligence, further meetings and Q&A sessions; Consider points relevant to the Post-Merger (PMI) phase; 	<ul style="list-style-type: none"> Revisit indicative valuation & prepare detailed valuation based on due diligence findings; SPA negotiations with the seller; Development of final structure (share/asset deal) and final valuation; Approvals; Signing of SPA & Close. 	<ul style="list-style-type: none"> Consider the extent of integration; Development of 100 Day PMI Plan; Consider short & long term objectives; Estimate requirements to capture synergies; Determine resource needs & optimal allocation.
Parties Involved				
<ul style="list-style-type: none"> CFO; Head of M&A; Accountants; Corporate finance advisors; Consultants. 	<ul style="list-style-type: none"> Senior management; CEO, CFO, CTO; Strategy director; Head of M&A; Head of Business Development; Consultants. 		<ul style="list-style-type: none"> Company general counsel; Lawyers; Senior management. 	<ul style="list-style-type: none"> Company general counsel; Lawyers; Senior management/HR.

An overhead view of a business meeting around a wooden table. Several people's hands are stacked in the center, symbolizing agreement or partnership. The table is cluttered with business items: a laptop, a calculator, a coffee cup, a glass of water, a pen, a notepad, and some documents. One document is titled 'INFORMATION'. The background is dark, making the wooden table and the white text stand out.

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