

## What is Your Business Worth?

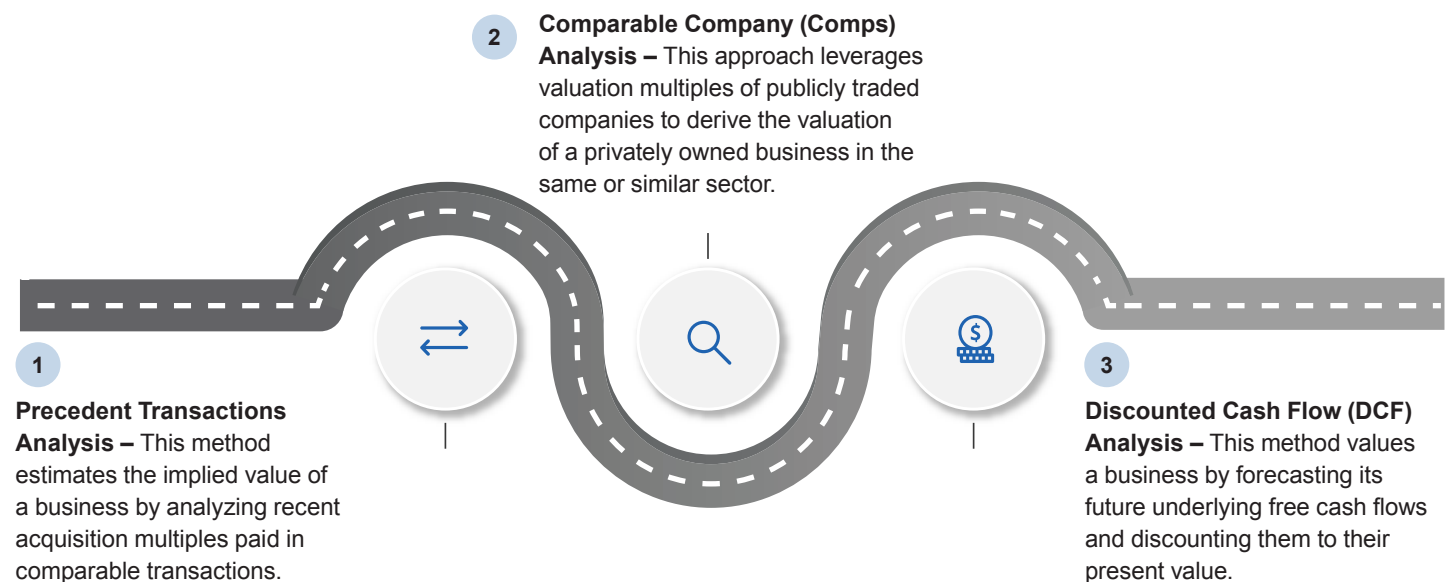
### Roadmap to Help Determine the Value of a Privately Owned Business

By Alberto Sinesi, Director and Robert Murphy, Senior Managing Director

The sale of a business is an emotional, life-changing event and determining its true value is a crucial first step in any sale process. Also, business owners may have a preconceived idea of what their business is worth and their value expectations may vastly differ from those of prospective acquirers. So, business owners need to be prepared and know their next move if approached by a potential buyer or have a plan if they are contemplating exiting their business in the near future. The bottom line is that the notion of “value” is fluid in nature and demands an understanding of **what the business is worth to a potential acquirer as opposed to what it is worth to the owner**. Let’s proceed with the steps to determine value.

### Three Generally Accepted Methodologies for Valuing a Company

When working with a trusted investment banking partner, the deal team will utilize a subset – or all – of the following valuation methodologies to determine company value, all having benefits and challenges:



### Factors Impacting Valuation and Key Considerations

While theoretical valuation methods, as presented above, set the basis for estimating the potential purchase price of a business, various other factors – **external and internal** – will impact the ultimate transaction value.

**External factors** encompass overall economic outlook, geopolitical circumstances, specific market/industry conditions, general M&A activity as well as the availability and terms of financing, among others.

**Internal or company-related factors** include attributes, such as revenue/profit size, stickiness of revenue, margin profile, growth history, depth of management, nature and dependency from customer and supplier base and competitive advantages. A synopsis outlining critical business aspects and associated buyer considerations is presented in the table on the next page.

## Business-Specific Attributes Affecting Buyer Appetite and Valuation

Business Attributes	Key Considerations
Size	<ul style="list-style-type: none"> <li>Larger companies typically trade at higher valuation multiples.</li> <li>Their operations are more established and easier to finance – thus seen as less risky.</li> </ul>
Revenue Nature	<ul style="list-style-type: none"> <li>Revenue stickiness indicates the likelihood of a customer making a repeat purchase.</li> <li>Contract-based revenue models provide strong visibility into purchasing patterns.</li> </ul>
Margin Profile	<ul style="list-style-type: none"> <li>Gross and EBITDA margins provide insights into the financial health of a business.</li> <li>Margin analyses are used to assess the profitability of a product, service or business.</li> </ul>
Growth	<ul style="list-style-type: none"> <li>A track record of sustainable, profitable growth indicates how well the company is positioned in its market and the overall prospects of such industry.</li> <li>Opportunities for future revenue and/or margin expansion heavily influence valuation.</li> </ul>
Capital Expenditures (CapEx)	<ul style="list-style-type: none"> <li>This metric measures the level of capital to be reinvested into the business to acquire, upgrade and maintain physical assets, such as plants, technology or equipment.</li> <li>The CapEx profile provides a reasonable proxy for how capital intensive a business is.</li> </ul>
Barriers to Entry	<ul style="list-style-type: none"> <li>These are obstacles that hinder competitors from easily entering a business sector.</li> <li>May include elevated start-up or fixed costs, capital requirements, degree of innovation, IP/regulatory hurdles, customer stickiness, sector fragmentation, etc.</li> </ul>
Leadership Team	<ul style="list-style-type: none"> <li>Depth and strength of the leadership team affect value and overall deal attractiveness.</li> <li>Areas to assess include identifying any roles to be filled, key man risk, etc.</li> </ul>
Intellectual Property (IP)	<ul style="list-style-type: none"> <li>IP encompasses patents, trademarks, copyrights on technology, products, licenses, etc.</li> <li>Having legal protection reveals whether the company has adequately secured its IP.</li> </ul>
Diversification	<ul style="list-style-type: none"> <li>Diversification reflects the reliance on customers, suppliers, products, services, etc.</li> <li>Would the loss of a key customer or vital vendor lead to a significant revenue decline?</li> </ul>
Systems	<ul style="list-style-type: none"> <li>Systems include internal workflows, processes, reporting, technical resources, etc.</li> <li>Acquirers may perceive weak systems as an area requiring large capital deployment.</li> </ul>

## Historical Evolution of EBITDA Valuation Multiples by Deal Size

TEV (in \$M) (*)	2003 – 2019	2020	2021	2022	2023
\$10 – 25M	5.8x	6.0x	6.1x	6.3x	6.1x
\$25 – 50M	6.5x	6.7x	7.1x	7.1x	6.9x
\$50 – 100M	7.5x	8.0x	8.4x	8.4x	8.0x

Source: GF Data, M&A Report

Note: (\*) Private company buyouts only across all industries. TEV stands for Total Enterprise Value.

## Industry Sectors in Demand

The table below provides an illustrative list of sectors that have witnessed resilient M&A activity and healthy valuation multiples over the past few quarters. Sectors in favor include companies with strong end markets, tangible growth opportunities, visibility of earnings, ongoing consolidation strategy and attractive free cash flow and margin profile.

Select Sectors Observing Resilient Activity	Favorable Business/Sector Characteristics
Tech-enabled health care and business services	Recurring purchasing pattern/revenue visibility
Financial services/fintech/insurance	Solid cash flow profile vs. growth at all costs
SaaS	Sticky customer/vendor relationships
Value-added distribution	Functional nature of products/services
Automotive aftermarket/services	Premium brand positioning
HVAC/landscaping/roofing services	Efficient operations mitigating supply chain issues
Pet services/foods	Defensible segments even during a downturn
Better-for-you foods/health and wellness products	Fragmented spaces ripe for consolidation
Frozen foods/ethnic foods	Underlying secular trends with strong tailwinds

## Premium Valuation for High-Performing Businesses

A strong financial profile is one aspect which will positively affect the value of a business. Specifically, the “**quality premium**” is the reward in valuation for above-average financial performance which in the analysis herein is defined as companies with revenue growth rates and EBITDA margins above 10 percent for the trailing 12-month period (or one above 12 percent and the other metric at least eight percent). In 2023, above-average performing companies received a **28 percent greater EBITDA multiple** compared to those that did not meet these criteria.

## Historical Quality Premium for Private Company Buyouts

	2003 – 2018	2019	2020	2021	2022	2023	Total
<b>Avg. EBITDA Multiple</b> Above Average Perf.	6.7x	7.6x	7.7x	8.2x	7.9x	8.2x	7.2x
<b>Avg. EBITDA Multiples</b> All Other Buyouts	6.2x	6.3x	6.2x	6.4x	6.5x	6.5x	6.2x
<b>Premium/(Discount)</b>	109%	121%	124%	127%	122%	128%	115%
<b>Incidence</b>	56%	51%	55%	63%	66%	48%	57%

Source: GF Data, M&A Report

Note: Private company buyouts only across all industries.

## One Final Consideration – Selecting the Right Investment Banking Advisor

No matter what valuation approach is used, or attributes a company possesses, the main takeaway remains: **a business is only worth as much as someone is willing to pay for it.** A healthy pool of potential acquirers ensures competitive tension in a deal process – often driving up the valuation of the target company. An experienced investment banking advisor should define the appropriate type of process for the business, obtain a higher value and significantly increase the odds of closing a successful transaction than any business owner could accomplish on his or her own.

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