

Maximizing Business Value

by Darrell V. Arne, CPA, ASA, CBA, CBI

John Brown, author of “How to Run Your Business So You Can Leave it in Style”, says ...

“At some point, every owner leaves his or her business voluntarily or otherwise. At that time, every owner wants to receive the *maximum amount of money* in order to accomplish personal, financial and estate planning goals.”

It has been estimated that \$8 to \$10 trillion will be passed to next generations in the next 20 to 30 years. This is the largest block of wealth to be transferred in this time frame in U.S. history. Ownership in privately held companies will either be transferred outright to next generations, or sold to third parties.

The truth is - business owners are not prepared to make transfers in order to maximize their exit proceeds. Statistics published in *M&A Today*, August 1999, prove this out:

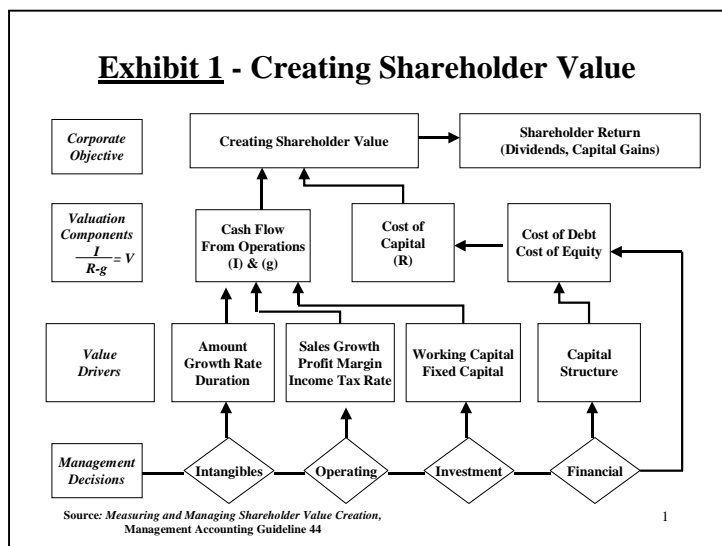
- 65% of business owners do not know what their company is worth
- 85% have no exit strategy
- 75% of their net worth is tied up in their business

This presents a *huge market opportunity* for financial advisors to create value for privately held business owners by : 1) helping them grow and *maximize the value* of their companies, and 2) helping them *maximize the price* when ownership is transferred.

Knowing how to maximize business value begins with the basic valuation components of the *capitalization of earnings method*. Determining enterprise value, following the “IRV” formula, is simply: $I / R-g = V$.

Increasing business value is accomplished by:

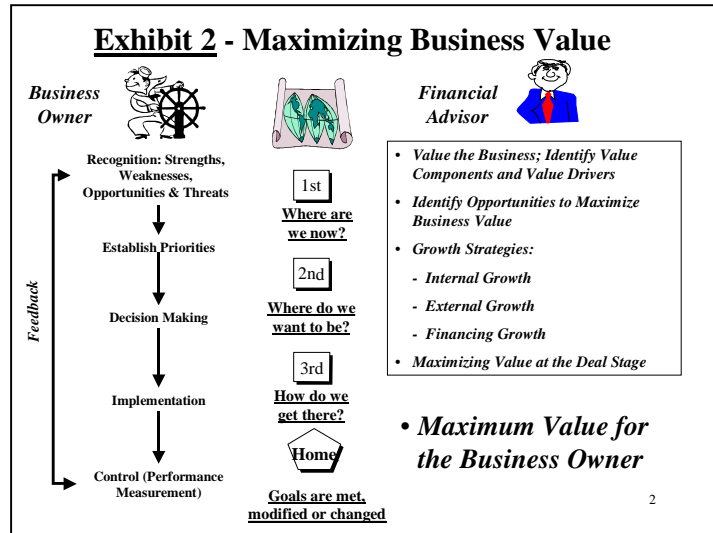
- I – Increasing operating cash flows
- R – Reducing business risks
- g – Increasing growth



The Exhibit 1 schematic shows that the *corporate objective* of “creating shareholder value” begins with *management decisions*.

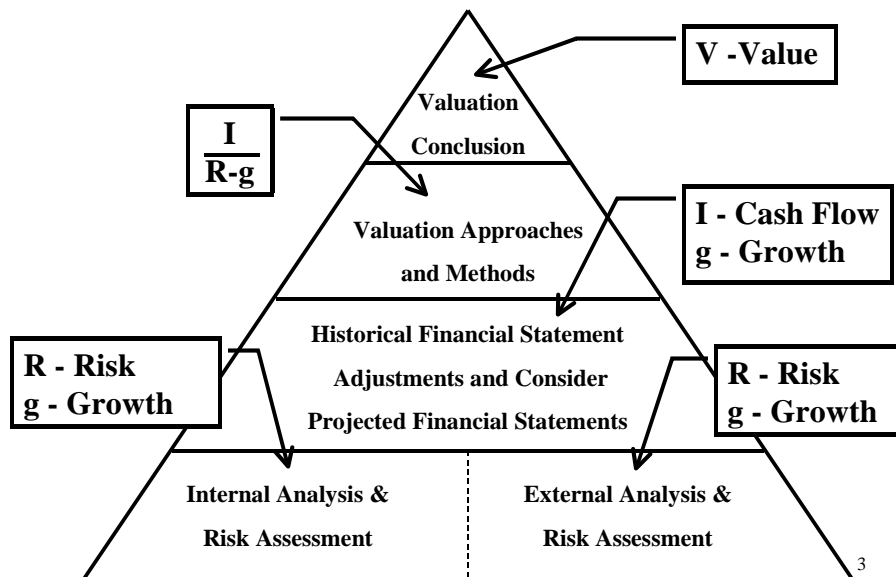
Exhibit 2 shows three important parts to maximizing business value:

- The management decision process business owners follow.
- The steps to a strategic business plan which provides direction to the process.
- The roles financial advisors can play assisting business owners maximizing business value.



Business valuations help answer the question - “Where are we now?”, by identifying a company’s valuation components and value drivers, and uncovering *some* opportunities to maximize business value. Exhibit 3 shows where valuation components are addressed during the business valuation process.

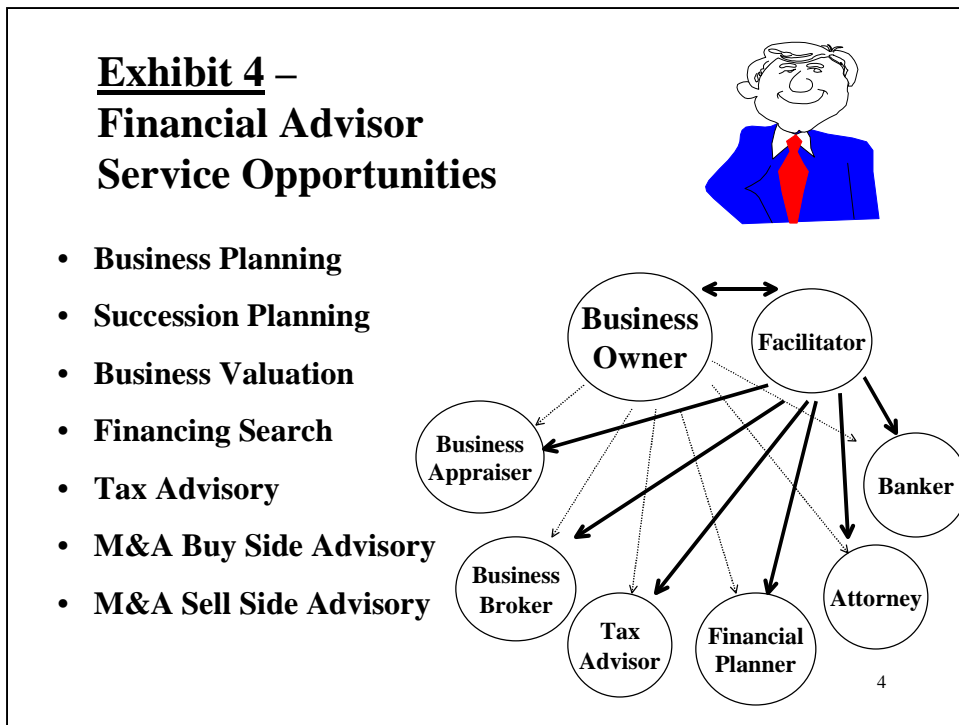
Exhibit 3 - Business Valuation Process



By itself, a business valuation has its limits. Further work is necessary to uncover a company’s strengths, weaknesses, opportunities and threats (SWOT). Financial advisors must dig deeper into the “internal” operational segments of a business to locate *additional* opportunities, and to develop the strategies that increase growth and value. Increasing business growth and value

might be achieved more cheaply and faster through an “external” acquisition of another business. To achieve internal or external growth objectives, financing will be a critical ingredient. Financial advisors can assist business owners with external growth and financing strategies, and during the deal stage to maximizing exit proceeds.

Exhibit 4 lists some financial advisor service opportunities that may come into play when assisting business owners maximize the value of their companies.



To become a “value added” service provider, a financial advisor must: a) learn the tools and techniques to *recognize* where the value of businesses can be maximized, and b) develop the technical and people skills necessary to *implement* strategies that create value for business owners.



Darrell V. Arne is President of Arne & Co., Albuquerque, NM, a financial consulting firm specializing in business valuations and mergers & acquisitions.

He presents an 8-hour course nationally to Business Brokers/Intermediaries and Business Appraisers titled: “Maximizing the Value of the Privately Held Company”. Course dates and locations can be found at www.arne-co.com.

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