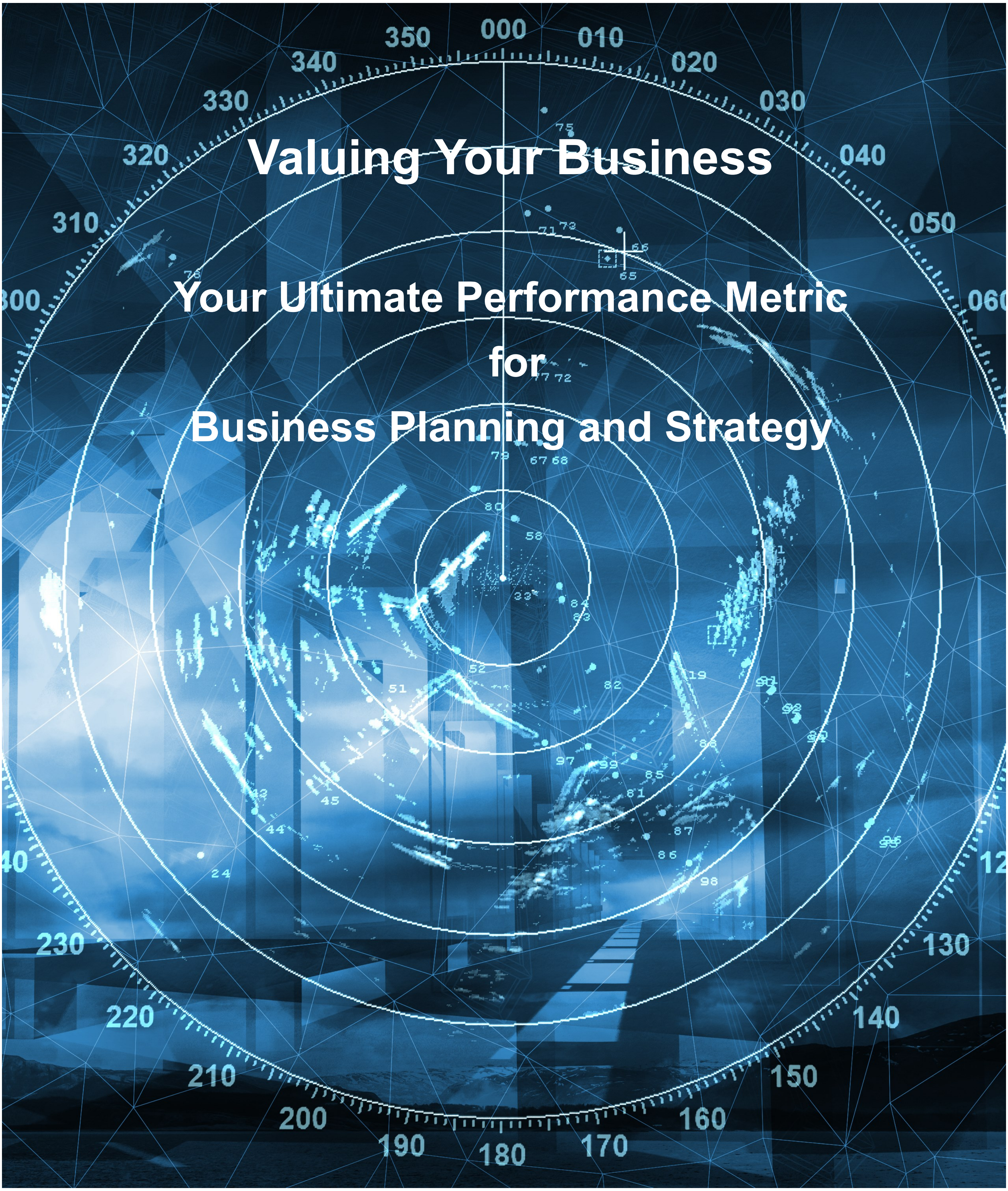
Mari Magno *Navigating Business Performance*

Mari Magno: delivering business performance, business valuations, new market development and business exit strategies, internationally and across all industries.

Valuing Your Business

Your Ultimate Performance Metric for Business Planning and Strategy



For a free consultation regarding your business requirements, please contact Emma Heathcote

info@marimagno.co.uk * +44 77 390 72717 (UK) * www.marimagno.co.uk

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Mari Magno is Latin for **Big Sea**. For many hundreds of years merchant mariners have sailed the globe, opening up new trade routes, supply chains and international markets: www.marimagno.co.uk

These merchant mariners were passionate about navigating new and exciting business environments.

They were strategic thinkers, with the diplomacy to develop strong business relationships, the skill and tenacity to drive their ships forward through challenging environments, the calculation and tactics to out-perform their competitors, and a commitment to exploration, innovation and watch-keeping, to identify and capitalise on new business opportunities.

Navigating Business Performance

Mari Magno is a business consultancy delivering business performance, business valuations, new market development and business exit strategies, internationally and across all industries

Mari Magno Business Valuations

Our business valuations are the ultimate performance metric for any business, large or small. They are based on strong business analytics and market research and are used by business owners to navigate their market and chart their business direction. Our unique valuation tools may be used year-on-year, enabling business owners to consider the best time for either new market development or business exit.

Our Business Clients

Our client base is extensive and features large and small business clients from a diversity of sectors including international education, maritime services, engineering, events management, travel and tourism.

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Business Consultancy
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Mari Magno Services

Our first port-of-call for your business is the development of a unique and comprehensive business valuation report. Working together with the business owners, we then use the results of the business valuation to deliver consultancy services, for either business development or business exit:

Business Development:

- New and existing market development
- Brand development and management
- Business analytics, performance and KPIs
- Market research, competitor analysis and market positioning
- Business acquisitions
- Franchising arrangements

Business Exit:

- Succession planning
- Business brokerage and sales
- Franchises sales

Value Drivers in Your Business

The development of a valuation for your business offers consideration of all the value drivers within your business, and the unique aspects of your business that differentiate it from competitor businesses. It involves a great deal of analysis of your business assets, both tangible and intangible, and how these are orchestrated to interact with the external market environment, to impact on your business financials.

Tangible & Intangible Assets

A business valuation is far more than simply a consideration of your business financials, added to your tangible assets. In fact, that would be very easy to do.

A business valuation should also involve analysis of your intangible assets such as product design, IP, customer ‘good-will’, autonomous systems and infrastructure, location, supply chain and brand, all of which contribute significantly to the value to the business. These intangible assets may be considered as ‘value-drivers’ because they drive your financials and the value of your business.

Business Valuation as a Performance Metric

It is not the case that a business owner who seeks to derive a business valuation, is necessarily considering selling the business. Understanding the changing value of your business and the different drivers that create value, will enable you to regularly use business valuation reporting as a single and comprehensive performance metric for your business. It will also enable you to identify and accelerate specific value drivers, which will impact on the financial performance of your business.

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Single-Point Business Valuation

Since business valuation reporting involves analysis and calculation using wide variety of performance metrics, such as financial, operational and marketing, then the combination of these sub-metrics on an annual basis, may be used to calculate the ultimate performance metric for your business, the value of your business.

Annual Tracking of Business Valuation

By calculating and tracking the value of your business from one year to the next, you will develop an understanding of how variations in the performance of your intangible assets, impact on the value of your business. More importantly, you will be able to make informed decisions about how to increase the value of your business, by 'turning up the volume' on certain intangible assets.

Furthermore, by using the principles of calculating and tracking the value of your business, you will reach a point where you will be able to anticipate how under-performance or over-performance of intangible assets will impact on the future value of your business, over a number of years.

This opens the opportunity of developing robust and comprehensive business planning and strategy, to future-proof your business, and protect and grow the value of your business.

Return on Investment

Certainly, if you are considering selling your business, then you will also need to consider the 'best time' to sell your business. Again, tracking the value of your business on an annual basis and anticipating the impact of the variable performance of each of your intangibles assets, will be important. This will enable you to consider the best time to release equity or sell the business, in order to realise a return on investment, your investment.

Intangible Assets and Market Share

When asked to value a business for a business owner, my first consideration is always 'how unique is this business?' That is the same as considering 'does this business have intangible assets?' And for a new business owner, that is the same as considering the difference in value between starting up a new business from scratch, or purchasing an 'oven ready' business. What would motivate a buyer to pay more money to purchase an already established business, when the cheaper option may well be to start up a competitor business from scratch? The answer of course lies in the value of the intangible assets.

For an already established business, intangible assets such as product design, goodwill, supply chain and brand are already realised in terms of market share and sales volume. It often takes many years of hard work and financial investment to growth the value of intangible assets and to realise their value in terms of market share. Therefore, the initial start-up costs in both time and money to launch a new business to market, are really just the tip of the iceberg.

It is likely that unless there is excessive demand in the market that existing businesses are unable to meet, a new business launched to market with no intangible assets, will struggle to establish and grow market share within its first years of trading.

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Buyer Considerations

By using a range of performance metrics to derive the value of your business, you will understand very quickly the value you have created in your business, compared to the initial start-up costs of the business. The value of a well-established business is defined by the value of its intangible assets, which are difficult for a new competitor in the market to replicate.

In a potential sale situation for your business, it is the value of these intangible assets that will be of interest to a prospect buyer, and which the prospect buyer will challenge you on, in an attempt to cut your price. This is because the value of intangible assets is difficult for you to 'prove' but represent a significant opportunity for a prospect buyer. Therefore, in a potential sale situation, it is super important that you understand how value is derived, so that you are able defend and justify the value of your business when negotiating with a prospect buyer.

In contrast, the value of an existing business with few intangible assets is likely to be consider exclusively in relation to the depreciated value of its tangible assets. From a prospect buyer's perspective, the difference will be in the decision to purchase second-hand equipment and fittings from your business, as opposed to new.

Business Growth through Acquisition

Once you have understood how your intangible assets drive the value of your business, it also follows that with the right level of disclosure, you will also be able to calculate the value of competitor businesses, or businesses offering a portfolio of products and services complimentary to your own. This creates an opportunity for you to use business valuation to grow your own business through the acquisition of other businesses, and to disable your competitors by acquiring their intangible assets.

Business Growth through Franchising

Having analysed the variable performance metrics of your business, you may identify that your business brand is a strong value driver for your business. Your brand value is a measure of the relationship between your marketing performance, market share, premium pricing and the impact of your brand converted into sales, as compared to competitors. A strong brand can create business growth opportunity through franchising, which essentially packages your business brand into a replicable business format. This format may then be sold again and again through licencing arrangements, to new business start-up owners. It is the business version of a DIY 'flat-pack'.

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Seeking a Business Valuation

If you can successfully operate your own business then you can successfully value your own business. But what you do need is time. Developing a robust business valuation is time consuming and for many business owners, time is an elusive resource. That's why so many business owners choose Mari Magno, for expertise in developing a valuation for their business.

Generic Online Business Valuations

You may have already tried using one of the many business valuation tools available online. You simply throw your business financials into a generic system, toggle your industry from the drop -down menu, and click the green 'GO' button. And out pops the valuation for your business, complete with caveats, non-liability tick-boxes and a confidential helpline to an 'expert consultant' who will charge you a fee, simply to explain what you have just received for free.

And then the online consultant will start to modify your business valuation based on any further information you may wish to disclose, deriving a completely different business valuation to the one you received for free.

This is because the online valuation tools do not normally have the complexity to acknowledge or consider the value of your intangible assets. So really, tempting though it may be to go for a cheap option, free online business valuation tools are rarely free, and they inevitably fail to value the most valuable assets of your business, the intangible ones.

Using EBITDA and Industry Multiples

You may also have tried calculating your business EBITDA (earnings before interest, tax, depreciation and amortisation are deducted) and using the EBITDA to derive the value of your business by multiplying your EBITDA by an 'industry multiple'. If you have selected your 'industry multiple' from one of the many 'industry multiple' listings available online, you will probably feel tremendously proud and satisfied that the value of your business has exceeded all your expectations and wildest dreams.

However, this formula for calculating the value of a business using 'EBITDA x Industry Multiple', should probably carry a couple of health warnings, levelled primarily at the industry multiple. It may well be considered that the industry multiple is the weak link in the calculation.

Industry Multiples

With such diverse and varying industry multiples available, it is tempting to choose the highest industry multiple for your business valuation, working to your favour. In contrast, a prospect buyer is likely to conduct a similar EBITDA calculation for your business using a far lower industry multiple that works to the buyer's advantage. This is the brokerage version of 'check-mate'.

The problem is that there is no negotiation space in between these business valuations, as neither the seller nor the buyer have understood the authenticity of their industry multiple selected. Furthermore, industry multiples fail to acknowledge and calculate the real market value of your intangible assets, assets with are totally unique to your business.

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Business Valuation Methods

There are lots of ways of valuing your business, here are just a few of the more common methods:

EBITDA: To avoid the irregularities of industry multiples, it is possible to use EBITDA with a derived multiple that is unique to your company, which considers market capitalisation (value of shares + debt – cash).

SDE: Another useful valuation method uses SDE (seller's discretionary earnings) and a return on the business owner's earnings, possibly over a 2-3 year period. This method involves restating the profit and loss account, to demonstrate the true earning capacity of the business, in terms of business owner benefits.

Discounted Cash Flow: Using a discounted cash flow valuation model with a growth rate and discounted rate, can also be useful. Free cash flow (all cash in – all cash-costs out) is unencumbered and can be used to estimate the cash flows over a period of time, years into the future. The discount rate is cumulative and represents the business risk profile.

Considering the Value of Assets

For any of these business valuation methods, there is still the opportunity to identify, (re)value and add onto your business valuation, the value of your tangible and intangible business assets.

The revaluation of your tangible assets, separate to your balance sheet, would normally require an industry specialist which the right industry credentials. Whether you are revaluing land, property or ships, the world is not short of industry specialists, ready to help you value your tangible assets.

In contrast, valuing intangible assets is more tricky. It relies on good market knowledge of your particular industry, and depending on the market position of your business, the market knowledge required may be local, national or international. An understanding of your industry market, and your competitors, will enable you to identify which of your intangible assets are unique in driving value in your business.

Financial Metrics for Intangible Assets

Equating intangible assets with financial values is not an exact science. But there are ways of measuring the value of goodwill, your brand, supplier and client contracts, marketing impact and IP. There are also ways of increasing or depreciating their values, dependent on the performance of other assets.

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Using Ratios

One useful method for allocating value to intangible assets is to use ratios, as related to your key market competitors. Some information may be difficult to obtain, such as the profit and loss account, but more obvious ratios might include price, marketing and the balance sheet (available for all UK registered companies from Companies House).

Intangible Assets & Impact Over Time

Whereas it is true that the value of intangible assets will eventually impact on your business financials, this no reason not to value each of them individually, and include them in your consideration of business value. This is because there will inevitably be a time delay on the impact of your intangible assets on the financial performance of your business. In some cases, this time delay could mean that some intangible assets will take years to impact on your business financials.

Liabilities

The liabilities of a business are shown on the balance sheet of the business accounts. They are an important aspect to consider when developing a business valuation, as they include business debt and any outstanding accounts relievable. Normally on the balance sheet the net asset value is given (Assets – Liabilities). In situations where you have had your tangible assets revalued, it is still important to subtract the business liabilities, to show the new net asset value.

It is also likely that your business will have intangible liabilities, such as a product recall or negative customer feedback, in which case you may decide to progressively discount or depreciate these liabilities over time, and to reduce the value of your intangible assets.

Consistency

If you are using your business valuation as an annual performance metric, then you will need to ensure absolute consistency regarding your choice of metrics, ratios and calculations, year-on-year.

Using an excel spreadsheet is a great idea, as you can develop your chosen formulas and ratios, and simply update the data on an annual basis. Creating an autonomous valuation tool, unique to your business, is really worth the set-up time. You'll be able to run fresh data through your valuation tool, year-on-year.

Understanding Your Business Accounts

Contrary to popular belief, a valuation does not need to be complicated and you do not need a university degree in science or accountancy. What you do need is time, a clear head and a sensible approach. You will also need is an understanding of your business accounts.

Trusting your accountant is great but signing off your accounts means that you are ultimately responsible for their financial integrity and credibility. As a business owner, you owe it to yourself to understand in basic terms, exactly what you are signing.

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Some Easy Considerations

As an expert Business Consultant, business owners often ask me which valuation method I use. The simple answer 'is all of them'. And every valuation I develop is then subjected to a market valuation check. But I do have a couple of old favourites in terms of business valuation formulae.

The most important point when using any valuation formula is to make sensible decisions about what to include. In certain circumstances, where I know that the source data is unreliable, I may decide to discount it or omit it altogether. After all, if I can't justify the valuation to myself, then I can't justify it to either the business owner or a prospect buyer.

This formula is a favourite of mine:

(EBITDA x EBITDA Multiple*) + (Tangible Assets – Liabilities) + (Intangible Assets –Liabilities)

Which is the same as:

(EBITDA x EBITDA Multiple*) + (Net Tangible Assets) + (Net Intangible Assets)

* where the EBITDA Multiple is calculated from the financial data in the business accounts

Another favourite of mine is this formula:

(SDE x Multiple) + (Net Tangible Assets) + (Net Intangible Assets)

* I have a tendency to use a multiple between 2.0 and 3.5 as the multiple with SDE, based on the understanding that the cost of purchasing the business owner's benefits, net of the assets, should be recoverable over a 2-3 year period.

Market Valuation Check

Whichever method you use to value your business, it is always a good idea to double check the value of your business against the sale price of other similar businesses in your industry and market.

You can use a wide variety of ratios to do this, comparing financials such as turnover, gross profit, net profit and EBITDA, depending on the financial data available from the business sale. These ratios are quick, simple and fun to play with, and will enable you to gage the market position of your own business, moderating your sale price, if necessary.

At worst, it will enable you to consider your 'bottom line' in the potential sale of your business, the point at which you turn your back on a prospect buyer.

Working Backwards

Personally, having developed a valuation for a business, I always like to do a sneaky back-check to calculate the ultimate industry multiple for this business, and compare it to the with the hugely variable array of industry multiples available online. It's just for fun really but it does offer me a cumulative understanding of which listings are consistently comparable to my own calculations, and vice versa. And I would never rely on any of them, without working through the entire business valuation process myself, first.

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Future Proofing Your Business

Since an annual business valuation is the ultimate measure of business performance, the process of valuing your business will offer you new insight and perspective regarding your market position. This enables you to develop a more focussed to approach business planning, contingency and strategy, impacting on the future performance of your business.

Your Business Response to Crisis

In such circumstances, it is likely that weathering the storm with both short-term contingency plans and long-term recovery plans, will be critical to your business survival. Short-term contingency responses may be characterised as by the immediate availability of cash-flow and cash reserves, and your operational capability to respond quickly and flexibly to changing situations.

In contrast however, your long-term recovery response will be heavily dependent on how you utilise your intangible assets to adapt to new market conditions. By driving forward their implementation, you will be able to drive the value of your business and grow market share in the immediate aftermath of crisis. In any situation where your business trading has been disrupted, the performance of your value drivers will be critical to the recovery of your business. Businesses with the strongest brands, the best customer feedback and the strongest supply chains will be the strongest to recover, and those with relatively low value intangible assets may never recover.

Valuing a Business in a Crisis Economy

There are many reasons why a business may be subjected to a disrupted trading environment, impacting on the future performance of the business. Normally such circumstances start as industry specific, and then ripple through the value chain, impacting on a range of interdependent industries. Sometimes disrupted trading may also the result of specific insecure links within your business' own unique supply chain.

Shape of the Crisis

Your business response during crisis will make or break your business. As an enabler, it is useful to consider the shape of the crisis, and your response. A 'V' shaped crisis would suggest a fast collapse and a rapid power-back response. A 'W' shaped crisis would suggest several successive collapses and power-back responses, a truly rocky road. A 'U' shaped crisis would suggest a longer period of time spent in crisis and a slower more strategic recovery.

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