

# EXIT PREPARATION

*What Business Owners Need To Know*





# CONTENTS

3	INTRODUCTION
4	ABOUT THE SURVEY RESPONDENTS
5	PREPARATION
8	VALUATION EXPECTATIONS OF BUYERS VS. SELLERS
10	2024 VALUATION EXPECTATIONS
12	SELL-SIDE QUALITY OF EARNINGS
13	TRANSACTION TEAM
14	CLOSING COMMENTS
15	ADVISOR FINDER PROGRAM



# INTRODUCTION

When we surveyed Axial's Investment Banking membership on the topic of exit preparation, we asked a wide range of questions with the hope of distilling the best tips and insights for exit-curious business owners.

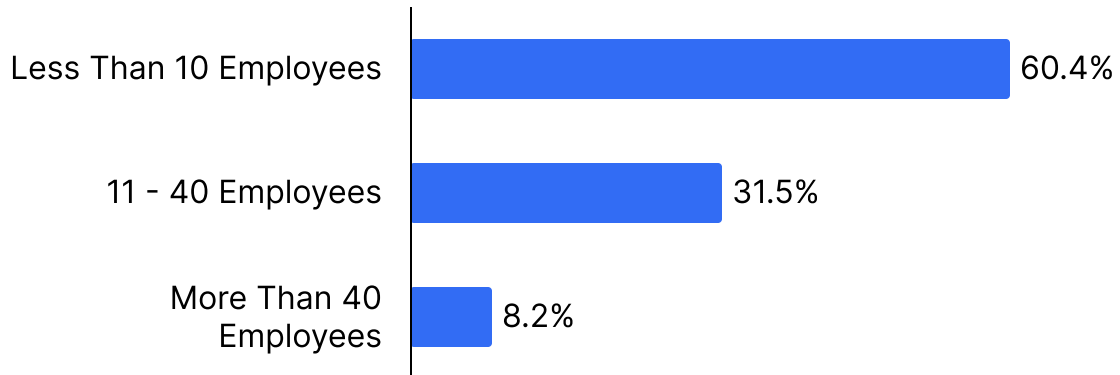
This ebook was assembled using the results of that survey, and we are grateful to all the Investment Bankers who contributed their insights and provided useful color on this topic.



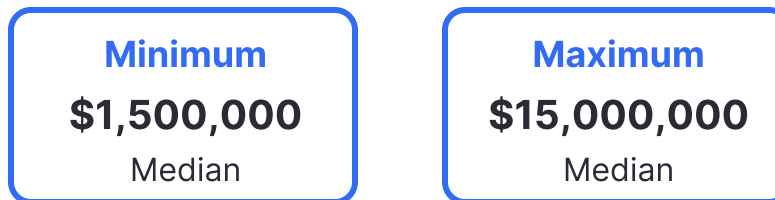


# SURVEY RESPONDENTS

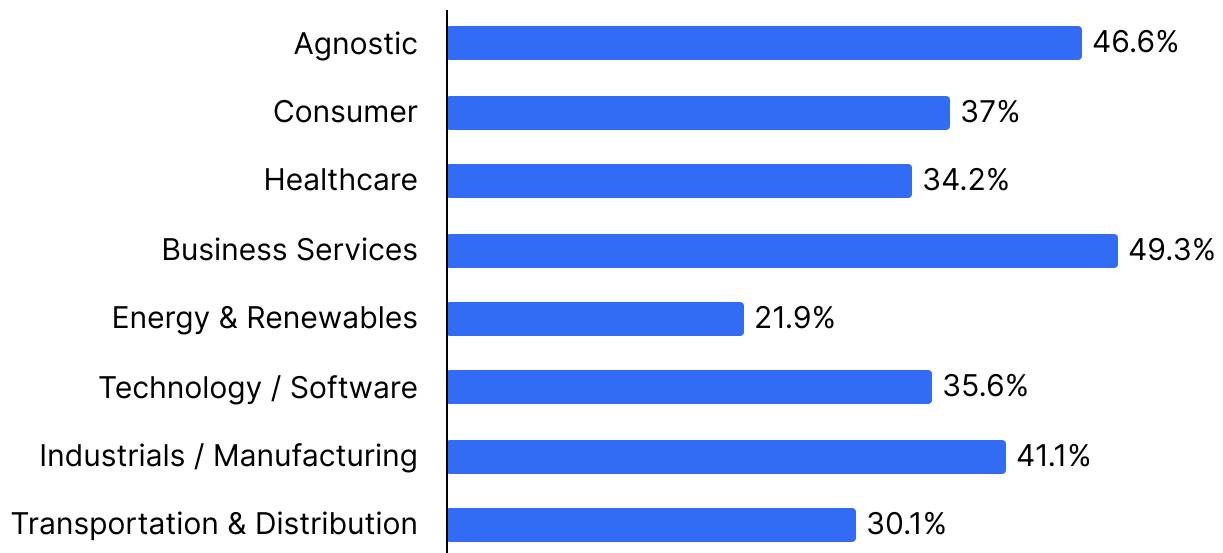
## Firm Size



## Typical EBITDA Minimum & Maximum of Clients



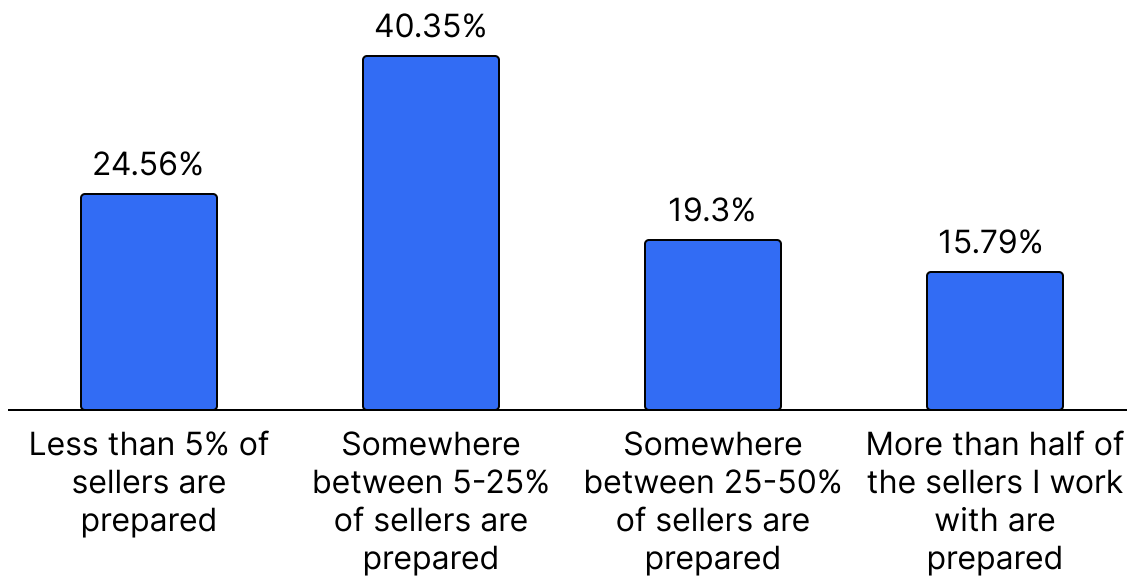
## Industry Focus (Multi-Select)



# PREPARATION

**66% of Investment Bankers say that less than 1/4 of the sellers are prepared to sell before hiring them.**

What percentage of sellers are “prepared” for a transaction prior to an engagement?



## What causes deals to die?

Before diving into how sellers can prepare, we pulled the most common factors that cause a deal to fall apart from the survey data.

### THE BIG EIGHT Avoidable Mistakes That Derail Deals



# PREPARATION

## What is the most important thing a seller can do to prepare for a transaction?

The responses to this question produced a breadth of advice, with a few investment bankers even commenting on the challenge of pinpointing one specific thing. However, there were four consistent themes among the answers.



**Hire M&A Advisor/  
Transaction Team**



**Clean & Organize  
Financials**



**Understand  
Valuation**



**Have Management  
Team in Place**

<p>Have a real team of people underneath them that can operate the business in their absence. Ensure financials are GAAP-compliant and ready for scrutiny; if they aren't, have a Quality of Earnings done pre-marketing process and be ready for due diligence.</p> <p>- <b>Bo Stump</b>, Stump &amp; Company</p>	<p>Engage Professional Advisors, seek guidance from professionals, such as accountants, lawyers, and business brokers, who specialize in transactions. They can help navigate legal and financial complexities and assist in finding the right buyers.</p> <p>- <b>Ilian Obregon</b>, Astor Walker &amp; Co.</p>
<p>Understand how companies are valued and how transactions are structured.</p> <p>- <b>Akash Taneja</b>, Momentum Advisory Partners</p>	<p>Know your true valuation ahead of time and be transparent and prepared to answer tough questions.</p> <p>- <b>Warren Rose</b>, Groce, Rose &amp; Moore, LLC</p>
<p>Have a solid runway ahead of them for revenue growth. Any hiccup in revenues that occurs during negotiations or diligence often undermines the process since it adds to the buyers' anxiety.</p> <p>- <b>William McDonald</b>, McDonald Dalton Capital Partners</p>	<p>Engage an advisor in advance to implement the best plan and practices for the best results for the future. Audit financials and/or conduct a sell-side quality of earnings analysis.</p> <p>- <b>Philip Rodriguez</b>, Statesman Corporate Finance</p>
<p>The best thing that a seller can do is to make themselves redundant in the day-to-day operation of the business.</p> <p>- <b>Chris Perfect</b>, Concept and Perspective</p>	<p>Build a full management team that renders the ownership redundant and get that management team to commit to remaining post-transaction.</p> <p>- <b>Jeffrey Rich</b>, Touchstone Advisors</p>

# PREPARATION

For most business owners, exiting their business is a once-in-a-lifetime event, and even with thorough preparation, it is an inherently complex process. Below is a selection of challenges Axial investment bankers have witnessed their clients experience.

## What are the most unexpected hurdles for sellers in a transaction?

Valuation expectations and the potential need for seller financing to get the deal done.  - <b>Jim Myers</b> , Hanna Business Advisors, Ltd
Sellers frequently underestimate the significant time investment necessary to successfully navigate the sale  - <b>Patrick O'Connell</b> , O'Connell Advisory Group
Understanding working capital and how that is "sold" with the business.  - <b>Keith Wegen</b> , Flatirons Capital Advisors
How physically and emotionally draining it is.  - <b>Drew Langford</b> , Trailhead Partners
Maintaining strong growth during the exit process, while working with a banker and buyers.  - <b>Sally Anne Hughes</b> , Hughes Klaiber
Understanding their fully-loaded adjusted EBITDA and negotiating all of the non-valuation deal points at the time of LOI.  - <b>Jay Jung</b> , Embarc Advisors LLC
Developing a strong outside-in perspective of their business from an investor perspective.  - <b>Patricia Stensrud</b> , Avalon Securities Ltd.
Structured offers. They tend to think offers will be all cash at closing.  - <b>Mark Mroczkowski</b> , Chapman Associates

# VALUATION EXPECTATIONS OF BUYERS VS. SELLERS

## Valuation

Valuation is the analytical process of determining the current (or projected) worth of an asset or a company.

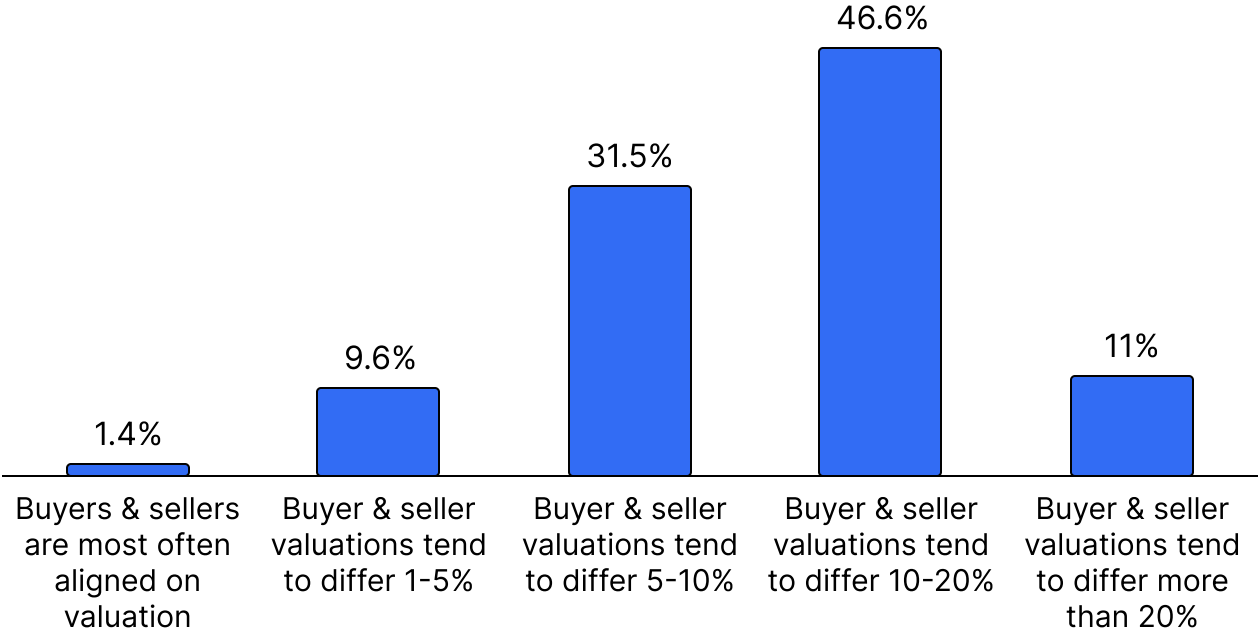
Valuation is important because it provides prospective buyers with an idea of how much they should pay for an asset or company and for prospective sellers, how much they should sell for.



Source: Investopedia

When it comes to valuation expectations, buyer and seller misalignment can arise from a number of various factors, often stemming from differences in perspectives, goals, information, or external circumstances. Since sell-side intermediaries work with both sides of the transaction, they are in a unique position to provide insight on this topic in today's market.

### On average, how large is the valuation gap between buyers and sellers in today's market?





# VALUATION EXPECTATIONS OF BUYERS VS. SELLERS

Only 1.4% of those surveyed indicated a frequent alignment between buyers and sellers on valuation and more than 56% expressed the belief that valuations commonly deviate by 10% or more. We delved further into the factors contributing to this misalignment and have include select responses below.

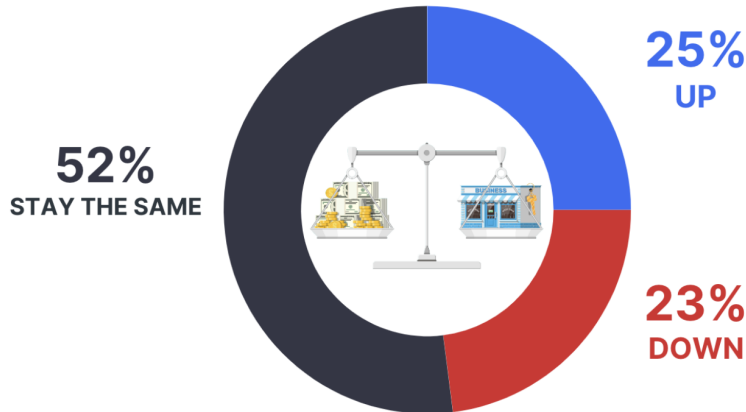
## What are the biggest contributors to valuation misalignment?

<p>Sellers do not understand fully how bank financing affects valuation.</p> <p>- <b>Ken Miller</b>, BlackRose Group</p>	<p>Success in the past vs. perception of the future and investments needed to grow.</p> <p>- <b>Ramsey Goodrich</b>, Carter Morse &amp; Goodrich</p>
<p>Sellers riding the COVID wave in some cases have an inflated perspective of their market value. Buyers are less willing to stretch on valuation due to perceived risk regarding company stability going froward. This along with the increased rates on debt are yielding lower valuations in some cases.</p> <p>- <b>Brandon Maddox</b>, CRI Capital Advisors</p>	<p>Buyer anxiety about macro-economic expectations. Reliability of future earnings is often questioned by buyers even when sellers are confident. Buyers typically want to base value only on historical performance while sellers naturally want credit for what has been built and will be fulfilled in the near future.</p> <p>- <b>William McDonald</b>, McDonald Dalton Capital</p>
<p>Access to financing from the credit markets is very soft, not just in terms of interest rates, but in terms of the amount of debt that lenders are willing to underwrite.</p> <p>- <b>Scott Mitchell</b>, SDR Ventures</p>	<p>Sellers relying on "word of mouth" valuations from 2021 and 2022, and expecting them to remain the same into 2023.</p> <p>- <b>Greg DeSimone</b>, Beacon Equity Advisors</p>
<p>We have coined the term "slope of hope" to describe the gap in which today, sellers are hoping that valuations return to the level their expectations are sitting while the buyers are a notch lower, primarily due to interest rate increasing and sellers not seeing the impact on real estate or the stock market valuations.</p> <p><b>Michael Gravel</b>, iMerge Advisors Inc.</p>	<p>I believe much of the gap is driven by higher multiples in prior years and misinformation to prospective sellers. Unfortunately many sellers only know rumors of valuation multiples and what they hear from peers (i.e. "big fish stories"). Most don't understand the underlying factors that drive multiples.</p> <p>- <b>Aaron McCambridge</b>, Citadel Advisory Group</p>
<p>Interest rates and Medicare/Medicaid reform</p> <p>- <b>Bradley Smith</b>, VERTESS Healthcare</p>	<p>Sellers misinformed on market multiples.</p> <p>- <b>Jay Jung</b>, Embarc Advisors</p>

# 2024 VALUATION EXPECTATIONS

Which factors do you think will impact 2024 valuations the most?

Do you think valuations will go up or down in 2024?



## Valuations Will Stay The Same

Cost of capital. But seller expectations continue to fall so volume will pick up.

- **Ramsey Goodrich**, Carter Morse & Goodrich

Interest rates and political environment (presidential race). Valuations will continue to remain lower than they were in 2021 and 2022.

- **Erik Endler**, Three Twenty-One Capital Partners

US interest rates, consumer spending, dry powder from strategics and PE, and overseas geopolitical environment.

- **Sally Anne Hughes**, Hughes Klaiber

Resurgence of IPO market; rebound in the stock market; tapering off of interest rate hikes.

- **Patricia Stensrud**, Avalon Securities Ltd.

Many factors, including creative capital investment to avoid expensive debt, a 'meet in the middle' on valuations, and what else are we gonna do with all this dry powder?

- **Rouzheen Myrick**, Palm Tree

Federal reserves desire to reduce inflation with quantitative tightening and longer term high rates causing banks to reduce lending.

- **Ronald D Torretti**, Turriss Group Inc.

# 2024 VALUATION EXPECTATIONS

Which factors do you think will impact 2024 valuations the most?

## Valuations Will Go Up

The unique story of the company, management, how the financial performance has come out of COVID, and the sustainability of those results.

- **Keith Yonkers**, 41 North

Return to steady growth and margin improvement after the volatility experienced in 2022-2023, Comparatively small portion of available assets being of high quality.

- **Nicholas Somos**, Left Lane Associates

More certainty in interest levels and more certainty around the economy will lead to more credit availability. Also, a number of PE firms getting very few deals done in 2023 will cause a surge of activity.

- **Scott Mitchell**, SDR Ventures

2024 is poised for increased M&A activity which could spark a rebound in valuation levels. Prospective buyers have cash and ample liquidity. Credit markets are improving. C-Suite confidence is rising as management teams and boards adjust to the "new normal".

- **Brian Egwele**, Egwele & Company

Interest rates, available capital, consolidation.

- **April Mason**, Paragon Ventures

Lower inflation and more stable economic environment.

- **Ray Johnson**, Exit Experts

## Valuations Will Go Down

Political uncertainty, rising risk of larger military conflicts.

- **Robert Latham**, IBG Business

Availability of debt / leverage and interest rates, followed modestly by slower growth rates.

- **Craig Dickens**, Merit Investment Bank

Higher interest rates. This will increase debt service loads, which will lessen the available cash flow for buyers. This will also reduce the valuation ceiling of a particular company. In the end, a business' asking price must take into consideration debt service.

- **Shep Campbell**, Merger & Acquisition Specialists

Interest Rates, Uncertainty, normalization of EBITDA as we continue to pull away from the Covid era.

- **Michael Schuster**, Cross Keys Capital

More than anything, out of control inflation and reckless monetary policy, creates the biggest risk to the economy. We continue to "ease" funds through the Fed and the result is primary and regional banks have billions of unrealized losses.

- **Mark Thomas**, M&A Healthcare Advisors

The presidential cycle can have a paralyzing impact on the market. Again, good companies will still trade, but the smaller tuck-ins will suffer.

- **Aaron Delidow**, Provest Inc

# SELL-SIDE QUALITY OF EARNINGS

## Quality of Earnings

An assessment of a company's earnings that removes distortions introduced by accounting methods to more accurately reflect its operational efficiency.

Tracking activity from the income statement through to the balance sheet and cash flow statement is a good way to gauge quality of earnings.

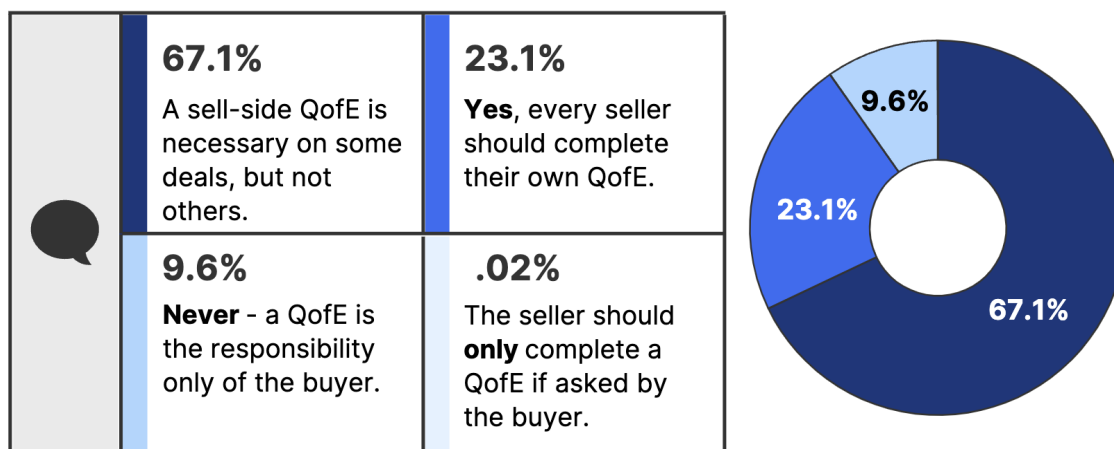


Source: Investopedia

It comes as no surprise that nearly all buyers will complete a Quality of Earning (QofE) analysis prior to a purchase to ensure that the financial information provided is trustworthy and reflective of the company's true financial performance. But should buyers be the only side of the transaction concerned with QofE?

Of these surveyed Investment Banking members, only 9.6% of respondents indicated that Quality of Earnings is strictly the responsibility of the buyer, while 23.1% had the opposite thought, recommending that sellers always complete QofE.

### Do you recommend a seller complete their own sell-side Q of E?



With the majority (67.1%) viewing the need for sell-side QoE on a deal-by-deal basis, we thought it would be valuable to dig deeper into the benefits.

We're pleased to share more information on this topic from FOCUS Investment Banking, an Axial member since 2010 and an [Axial sell-side partner](#) since March of 2021. [➔ Full article](#)

# TRANSACTION TEAM

## Who should be on the seller's deal team?

In lower middle market M&A, a transaction team plays a critical role in facilitating deals efficiently and effectively. Below are the parties that survey respondents believe a seller should have on his or her transaction team.

### Investment Banker / M&A Advisor



### Wealth Manager



### Attorney / Legal Counsel



### Industry Consultant



### Accounting Firm



### Executive Coach

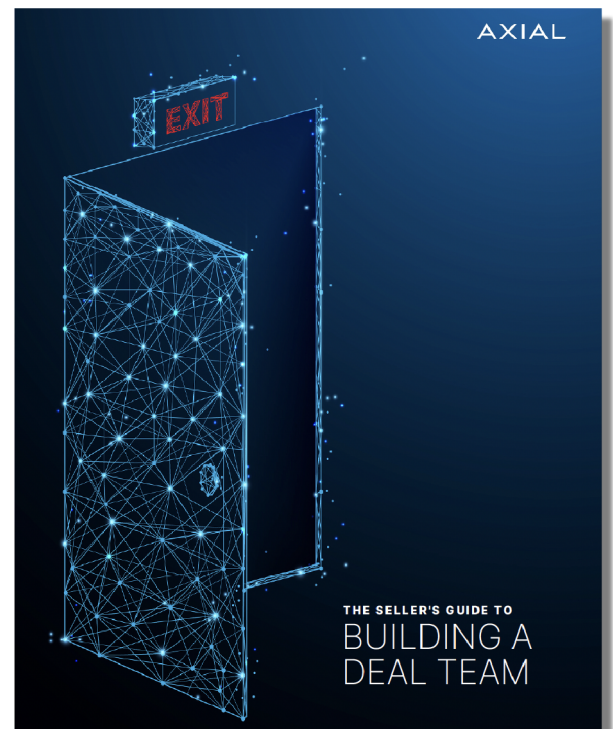


## The Seller's Guide To Building A Deal Team

Interested in learning more about what goes into building a deal team? Check out [The Seller's Guide to Building a Deal Team eBook](#).

This ebook covers building a deal team with both external and internal resources.

- What roles the C-suite plays in the deal process
- The external roles needed on the deal team
- The value and role of hiring an M&A advisor



# CLOSING COMMENTS

To close out the survey, we asked for any additional comments or advice for sellers on how to prepare for a transaction. Select responses below.

An unsolicited tap on the shoulder does not mean you are ready and attractive to a buyer.

- **Michael Schuster**, Cross Keys Capital

Start early, get a transactional calculation of value (not a formal valuation), consult with an advisor who can identify areas of weakness and strength beyond the mere "numbers" but on the factors that affect the reliability of those numbers moving forward.

- **Jamison Rounds**, Valuevisor

Make sure it's the right fit for you and rely on more than one expert to guide you through the process.

- **Warren Rose**, Groce, Rose & Moore, LLC

Being able to articulate effectively about the business is critical. Owner and important management team members often require much coaching re messaging, staying on point and succinct with communications.

- **Ron Hodge**, Westbury Group

First look internally (update monthly financials, align with GAAP, etc.). Then look externally - sellers should be conducting their own due diligence (e.g. ask to speak to other operating partners, research other portfolios, know the market multiples, etc.)

- **Rouzheen Myrick**, Palm Tree

Read industry newsletter to get information on trends in the specific sector.

- **Ken Miller**, BlackRose Group, LLC

Hire a competent M&A person to go over keep vs sell processes a few months before making a decision to sell to an outsider. The preparation for selling to an outsider is quite different than the prep for keeping a family business or selling to employees, family or partners.

- **Ronald D Torretti**, Turriss Group inc

Exit Ready is a bi-weekly newsletter from Axial that distills the best content, tips, and guides designed to inform, educate (and entertain) exit-minded business owners running \$5-\$100M businesses. Subscribe below.

**EXIT** READY

# Advisor Finder Program

## Find An M&A Advisor You Can Trust

The Advisor Finder program guides business owners through the M&A Advisor identification, interview, and hiring process. Leveraging 10 years of behavioral data and relationships on the Axial platform, we help you choose the right advisor for your business.

[Get Started →](#)

## Why Choose Axial's Advisor Finder Program?



### Comprehensiveness

There are 3,000+ advisors on Axial, and 10+ years worth of data on each of these advisors. This data includes the deals they've worked on, their reputation in the market, their process effectiveness, and their historical success.



### Trust

Axial has a well-staffed relationship management team that works directly with every advisor using the platform. This allows for a nuanced understanding of the integrity and personalities of the advisors participating in the program.



### Confidentiality

Business owners and executives can keep their identity confidential until it makes sense to disclose. Axial's team sets up the calls and exchanges relevant information between parties in order to facilitate a productive, fully anonymous experience.



### Efficiency

We do the research. We manage the process and necessary correspondence. We coach you on how to prepare for each call. We make it as easy as possible for you to run a comprehensive, competitive process to find the right advisor in a timely manner.



### Competition

Advisors that participate in the program know that they are competing with other advisors to win your business. This means advisors are more willing to answer pointed questions and divulge important information earlier on the process – most prominently about their experience, fees and terms.

## SELECT ADVISOR FINDER BUSINESSES

