

Advisory Alert: Do you know the true value of your business?

Valuation impacts on all businesses throughout their lifecycle whether buying, selling, financing, restructuring or dealing with disputes. As a finance director, you should be looking at the numbers so that you are in a position to advise your CEO and board effectively.

We are seeing a growth in demand for independent valuations driven by regulation for example, but increasingly there is a need to demonstrate increased shareholder value. So if you think valuation is irrelevant to your business because you're not looking to sell, it may be time to think again.

Learning from private equity

The merger and acquisition market is storming ahead of late with purchase prices heading towards their peak. With finance still relatively cheap and the banks coming back into the marketplace, more money is available to fund transactions, leading to higher valuations.

Private equity (PE) investors tend to be very effective not only at assessing value but also at enhancing it, because the nature of what they do requires a focus on increasing the value of a business quickly and efficiently. Knowing what a business is really worth and what it has the potential to be worth is key to their investment approach. PE therefore tends to

target businesses that are drifting or unloved, but which have untapped value within them.

However, you don't need to be looking at a sale or considering a purchase to benefit from the kind of scrutiny PE might put your business under before making an offer. Being aware of what drives value and how your business measures up to your competitors, judged by the kind of criteria private equity would use for valuation, is a valuable exercise in its own right.

Unlocking the value within your business may not make you more attractive to private equity (in some ways it will make you less attractive), but it is likely to make you more popular with banks, external investors and shareholders.

What drives value?

Although there are some variations by sector in the exact drivers and appropriate benchmarks, the key principles which drive value are common to all cases: how much cash flow does the business generate and what is the rate of return?

Building a financial model is a core element of the valuation process. Technical analysis needs to be supported by clear reasoning and an understanding of the wider context in which you are operating. You need to know not only about your levels of growth now but



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For assistance in this matter, please contact us via ojel.rodriguez@pr.gt.com



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about your prospects for growth in the future. Similarly, your margins may be good, but are there external factors that could threaten your level of profits in the future?

Valuation methods

There are three main methods of valuation that can be used to derive the value of a business: asset, market and income. Usually the valuation process will involve employing one or more of these methods and deriving an estimate of value, or more often a range of value. Whichever method is selected will invariably require establishing how comparable businesses are valued.

You should try to define the characteristics of a good company in your sector and then choose an appropriate competitor to benchmark yourself against. This will aid in highlighting potential barriers to realising value. For example:

- Are there inefficiencies in the way you operate?
- Are you missing out on a key section of the market?
- Do you need to enter new markets or withdraw from unprofitable ones?
- Do you need to develop new products or get rid of old ones?
- Do you need to invest in new systems or equipment?
- Do you lack a strong brand?

A common example in recent years has been a failure to address the digital marketplace. Businesses that engaged early with online selling created a strong engine for growth, which enhanced their value, while those who

lagged behind saw their growth potential falter.

Benchmarking in practice

Effective analysis will reveal how the market distinguishes the valuation of listed companies, which can then be used as a benchmark for valuing private companies.

Factors such as expected growth, profitability, maturity and diversity of similar companies, and the market dynamics are used to develop key valuation benchmarks. These benchmarks are used to derive a reasoned valuation range for our client's business, which supports them in agreeing a price that met their objectives, in the case of a business sale.

The key to pushing value higher

To some extent a company, like anything else, is worth what someone is prepared to pay for it. But knowing the true value of your business will not only put you in a strong position with a potential purchaser or investor, it will illuminate the steps needed to push that value higher.

See more at:

<http://www.grantthornton.co.uk/en/insights/do-you-know-the-true-value-of-your-business/>

Call us to make an appointment with one of our experienced advisors. We will be glad to assist you.

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