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Selling your company

EFFECTIVELY MAXIMIZING THE VALUE OF A BUSINESS BEGINS LONG BEFORE THE SALE PROCESS KICKS OFF

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BOOM AND BUST in the oil patch have given way to boom and boom in the shale era. Technology may not have created permanent prosperity in the oil and gas industry, but it may be a very long time before the old bumper stickers reappear with the words, "Lord, if you will send us one more boom, we promise not to (mess) it up."

As they continue to see years of steady growth in revenues and profits, the owners of small- to mid-size companies in oil and gas manufacturing and services inevitably wonder whether the time is right to sell all or a part of their businesses.

Owners should realize that a favorable marketplace is just one of several factors to ponder in the decision to sell. Effectively maximizing the value of a business begins long before the sale process kicks off. Some mid-range planning and an honest examination of a number of key factors, like the owner's role after the transaction, can go a long way toward formulating an effective exit strategy that yields a win-win transaction. Here are some real-world illustrations of action steps that should find their way into an exit planning program.

STEP 1: PROVIDE RELIABLE, CREDIBLE FINANCIAL REPORTING

Three years ago the owners of a pipeline services company wanted to know what they could do to better position their firm for the future. The company was based in Arkansas and provided oilfield construction services in the midcontinent and southeast. At the time, it had $4 million in annual revenues.

After examining its business practices, we advised that the company begin annual audits to enhance the credibility of its financial information and to give the owners the ability to better explain its financial positioning at any point in the business cycle. The reliable and trustworthy financial data that came out of these audits by a reputable accounting firm has subsequently put the company in the running for larger contracts with several significant exploration and production companies.

Certifiably sound financial data got the attention of the large E&P firms. It also gave the company's representatives a solid basis upon which they could negotiate more favorable contracts. Since regular audits became routine three years ago, the company's revenue has increased from $4 million to $30 million. Now, if the owners decide it's time to sell the company, they can command a much more favorable selling price and a faster, less difficult sales process should they decide to monetize their business.

STEP 2: DIVERSIFY YOUR CUSTOMER BASE

The case just cited also illustrates how a diverse customer base will enhance the financial strength of a company as well as its potential selling price. Many small entrepreneurial concerns go through an incubation period when their revenues depend on one or a few major customers. Continued reliance on a narrow customer base can eventually betray a weakness. Difficult times at one of its few major customers will drag down the performance of the entrepreneurial concern.

We recently advised a pipeline services company, which was able to diversify its customer base by providing audited financial results. With audited results, the company qualified for larger contracts from oil and gas majors that previously would not do business with it because it was perceived as too small and possibly unstable.

Another company we've dealt with recently had a similar experience, but this particular firm was an electrical engineering service provider to the oilfield. By adopting a regular schedule of audits, the firm established its financial stability and, as a result, was able to qualify for master service agreements (MSA) with a wider range of drilling companies than it qualified for previously. The outcome was a steadier and more diverse revenue stream, which made the firm a more valuable acquisition target.

STEP 3: CONSIDER WHERE YOU ARE IN THE BUSINESS CYCLE AND ON YOUR COMPANY'S GROWTH CURVE

Most small but growing concerns are tightly focused on ongoing operations. Analyzing their context in terms of the business cycle and their growth curve is usually a luxury they can't afford. To do this, executives would have to take a conscious step back from the daily demands of running the business, demands that always seem so very urgent and unavoidable.

Recently, we were approached by a diversified pipeline construction company specializing in pipeline construction support services, such as clearing and pipeline integrity. The firm believed it was not yet ready to be acquired, but it wasn't sure. First, we analyzed the company's operations and made certain recommendations, but we also conducted a confidential outreach to potential buyers so the company would have an objective and unbiased evaluation of its prospects in the merger and acquisition (M&A) marketplace, given the business cycle and the firm's corporate performance to date.

The results of this confidential outreach were very positive. Following the adoption of our operational recommendations, the firm was eventually sold at an above market evaluation. This particular pipeline service company needed more than raw data on market conditions. It needed objective and confidential feedback from the market that would either reinforce its current beliefs or reveal a more accurate assessment of its corporate performance within the context of the business cycle. Frequently, only outside third parties are able to provide this kind of insight.

STEP 4: EVALUATE THE STRENGTH OF YOUR MANAGEMENT TEAM

Qualified buyers who complete transactions in the oil and gas services space are keen on assessing risk. Specifically, they want to know the likelihood that a company's favorable performance will continue into the foreseeable future.

A critical part of a firm's continued success will be the strength of management after an acquisition has taken place. Unless the entrepreneur or group of founders has taken steps to groom the firm's second tier of executives, the founders will usually have to stay on with the firm during a transitional period while a new management team absorbs the nuances of running the business successfully. The alternative is to prepare the firm's second tier managers to take over for the top executives following the sale of the company.

The founder of a pipeline construction company recently came to us in just such a situation. He was ready to step away from day-to-day management of the company and diversify his wealth by selling his holdings in the firm. We analyzed the company's operations and realized that its second tier managers were quite talented and capable executives.

In preparation for a corporate sale, our advice was to give these second-tier managers greater responsibilities so they could seamlessly move into senior management positions after the sale. The company followed our advice, but the buyer still required that the founder remain onboard as a consultant for a brief period of time. Nevertheless, the buyer was impressed with the management team to the point that the sales price for the company was significantly higher than expected.

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STEP 5: BE PREPARED TO EXPLAIN THE WORTH OF YOUR COMPANY

It's a logical question for every corporate buyer to ask of a business owner: Why are you selling your company now? And sometimes, it's the question business owners are least prepared to answer because they have not been able to step back from daily operations in order to do the due diligence research that the buyer will. In many cases, the owner is just too busy running the company to worry much about what the company would be worth to a buyer, but without this knowledge, the seller is at a disadvantage to the buyer.

Doing this sort of due diligence research on one's own company involves a healthy dose of brutal honesty. All of the strengths and shortcomings must be exposed. Then, strengths can be highlighted and shortcomings corrected before the sales process begins.

WE NEVER DO THE SAME DEAL TWICE

Every M&A deal is as different and as diverse as the parties to the deal. We all have our own set of emotions, our own analytical skills and our own judgmental perspectives. We look at the same thing and see something very different. Taking these action steps will put business owners in a favorable position for selling their companies, but that's just the first step toward getting a deal done. OGFJ

ABOUT THE AUTHOR

Bryan K. Livingston is Managing Director and Chief Executive Officer of Dallas-based Capital Alliance Corp. He provides M&A advisory services to shareholders of middle-market companies, with an emphasis on construction and engineering services providers throughout North America. Livingston has completed transactions for clients in oil and gas pipeline construction, oil and gas pipeline support services, and minerals mining and processing, among other industries.