



Summer 2008

Building Management to Deliver Value

“It’s better to back a bad business with good management than a good business with bad management.” This is a widely held belief among those who invest in middle market businesses. Although there are different degrees of “good” and “bad” that create exceptions to this rule, there is no question a quality management team can do great things for your business. Putting a team in place that can drive sales, improve operations, control costs and identify opportunities in the market will create immediate value to the owner by way of improvements to the bottom line. While bottom line improvements are good, *the greatest economic benefit of building a solid management team will come when an owner decides to sell the business.*

The reason for this is a strong management team is key to achieving a premium valuation. More importantly, a weak or non-existent management team turns off so many potential buyers that it becomes difficult to sell the business at all. The idea is analogous to selling a car that is missing its transmission. The pool of prospective buyers for that car is



minuscule compared to the pool of buyers for the same car with a transmission. Most people don’t want to spend the time, money and effort to buy a car that needs a lot of work. This doesn’t mean it’s impossible to sell, but it will be more difficult to find a buyer and the price will be heavily discounted. The same

holds true for a good business with sub-par management.

Prospective buyers of a business (i.e. those people ultimately valuing the business) look for specific attributes when evaluating a management team.

Successful Track Record – Buyers love to see talented management with a long successful track record with the company or within the industry. A team that has worked through industry cycles, economic downturns, and significant industry change will be able to identify and navigate similar cycles and changes successfully in the future.

Gas left in the Tank – The need for experience must be balanced with management’s desire to continue working going forward. If the entire



We are pleased to present the first edition of Transaction Insights, a quarterly newsletter offering news, tips and solutions for middle market business owners.

The information in the newsletter is intended to address the common questions and issues that business owners raise throughout the process of selling their companies.

We hope you find the content useful and invite you to contact us anytime to learn more about the business sale process, receive a free informal valuation of your company or to explore the sale of your middle market business.

Let us hear from you,

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PRESIDENT

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team is at retirement age or intending to leave the company for other reasons, they won't be much use to a new owner. A team that is excited about and has a need to continue working for an extended period of time is the ideal team to have in place when it comes time to sell the business.

Depth – A management team of one person might be great for running the business under current ownership, but it is sure to raise concerns with someone spending millions of dollars to purchase the company. Having all customer, vendor and employee relationships reside with one person is cause for concern. If that one person gets hit by a bus or walks away, the new owner is left with a company that has no one to run it. A cross-functional team of 3 to 5 competent people is ideal for a middle market business.

Team Players – A transition of ownership should be seamless from the perspective of day-to-day operations. In order to achieve this, management must be willing to work enthusiastically with new ownership and rally around their objectives for the company going forward. It's no secret that building a management team with these characteristics is a complicated task. Good talent is hard to find, recruit and retain. But the challenge of building the team is why the finished product is so valuable. Owners who plan for their business sale with this in mind, will be handsomely rewarded with more numerous and attractive options when it comes time to sell the business.

Making Sense of Multiples

For many years investors have used multiples to compare the value of similar companies. Whether applying Price/Earnings (P/E) ratios to compare publicly traded companies or EBITDA (Earnings Before Interest, Taxes, Depreciation, Amortization) multiples to compare privately held middle market businesses, the idea is that similar companies should trade at similar multiples. For instance, if a staffing company in Illinois produces \$2M of annual EBITDA and sells for \$10M (implying a 5x multiple), a similar staffing company in Indiana with EBITDA of \$2.5M should be valued in the \$12.5M ballpark.

Multiples are a valuable tool when used appropriately. They provide investors and business owners a sanity check when assessing the value of a business. However, people enter dangerous territory when they use multiples for anything more than determining whether or not they are "in the same ballpark". For a number of reasons including those outlined below, multiples should neither be the sole valuation metric nor the tool used to pinpoint a valuation. Here are just a few reasons why:

Available Information – Particularly in the middle market, quality information on comparable companies is not readily available. In most cases, not much more than the sale price and annual revenues of the company are released. In instances where more information is available, it is rarely a case of full disclosure. The lack of quality information makes it difficult to place a great deal of stock in a multiple.

Similar Companies – No two businesses are identical. Some are more similar to one another than others. But even with two companies making the same product for the same industry, they likely have significant differences that impact value. Different sizes, market shares, growth prospects, customer concentration, capital structures, management teams, etc. can mean the difference between a 4x multiple and a 7x multiple.

Expected Return – Eventually, the person or company with the ultimate say on value is the one that steps up and pays for it. While comparable multiples will provide them some guidance, they will ultimately make a decision based on what kind of return they expect to get on the business purchase.

Although multiples are often referred to in this business, we suggest to our clients that they keep their attention on the goals they wish to accomplish. For most, the key financial goal is to walk away with as much value as possible at the end of the day. In order to do so, we suggest focusing on how to **structure the transaction in a way that maximizes after-tax proceeds** rather than getting distracted by trying to pinpoint a multiple.

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Middle Market Insights

Buyers contact us daily to discuss their current acquisition interests. Below are just a few of the company types that buyers have recently indicated a specific interest in:

- Multi-location ready mixed concrete companies adjacent to or within major metropolitan areas in the Midwest, Southeast, or Great Lakes regions
- Home health, hospice, home infusion, and other healthcare service businesses
- Staffing companies providing quality healthcare professionals
- Agriculture equipment manufacturers
- Truckload carriers with a large percentage of dedicated freight
- Regional processors of ferrous and non-ferrous scrap
- Oil & Gas industry service companies and Utility Infrastructure service companies
- Janitorial service companies catering to industrial, office, retail, or state/municipalities
- Insurance brokers/agencies dealing primarily with commercial lines
- Machine shop catering to a niche industry or product category
- Regional or national providers of routine maintenance, upkeep, or repair of commercial property including lighting, signage, parking lot striping, etc.
- Injection molders of plastics used in packaging, consumer or medical products
- Branded consumer products companies that sell through DIY home centers, mass merchants, lawn & garden centers, farm/agricultural stores, and to professional pest control providers



Should you have a curiosity regarding the current level of interest in your particular business, please call us at 888-808-0202. We would be happy to share our market insights with you.

NOTABLE MIDDLE MARKET TRANSACTIONS Q2 2008

SELLER	LOCATION	INDUSTRY	BUYER	LOCATION
Wade Paper Corp.	Deerfield, IL	Paper Wholesale	Shaughnessy Kniepp Hawe Paper Co.	St. Louis, MO
Time-O-Matic	Danville, IL	Digital Signage	Harbour Group	St. Louis, MO
Pendl Companies	Brookfield, WI	Printing Supplies	American Toner Serv	Santa Rosa, CA
Dayton Progress Corp	Oak Brook, IL	Industrial Tools	Connell Limited Part	Boston, MA
B&B Electronics	Ottawa, IL	Engineering	Graham Partners	Philadelphia, PA
Specialty Risk, Inc.	Liberty, MO	Insurance Broker	Arthur J. Gallagher & Co.	Itasca, IL
Pro-Gard Products, LLC	Indianapolis, IN	Security Products	Castleray Investments	Chicago, IL
Hallmark Data Systems, LLC	Skokie, IL	Magazine Subscription Fulfillment	EBSCO Industries, Inc.	Birmingham, AL
SM&P Utility	Carmel, IN	Utility Service	Laclede Group	St. Louis, MO
Wittman Hydro Planning Associates	Bloomington, IN	Water Resource Consulting	Layne Christenson Company	Mission Woods, KS
Central Power Products	Grandview, MO	Railcar Movers	The Riverside Company	Cleveland, OH
Mid Land Equipment Comp	Des Moines, IA	Ag Equipment Dealer	Titan Machinery	Fargo, ND
Personnel Management Inc	Greenwood, IN	Staffing	TrueBlue, Inc.	Tacoma, WA



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Main Street Values, Wall Street Expertise

Nolan & Associates has been assisting middle market business owners for more than three decades with what is likely the most significant economic event in an owner's lifetime – the sale of his or her business. Our passionate and dedicated team of professionals possesses midwestern Main Street Values and Wall Street Expertise: a combination allowing us to work comfortably and closely with owners in pursuit of the best deal the market has to offer.

We are financial professionals, CPAs and engineers. Our focus is profitable Midwest businesses generating \$10 million or more of annual revenues. We work with companies across many different industries. Regardless of size or industry, our clients consistently choose Nolan & Associates because of our 30 years of success with “the business sale process” and ready access to the marketplace of qualified buyers.

From start to finish, our engagements are conducted in a strictly confidential manner. Prospects are contacted only with our client's approval and we work enthusiastically and diligently to complete each transaction in a timely manner.

