BEAN PARTNERS

The 7 Biggest Levers to a Higher Valuation

Maximising Valuation
Essential Guide

Many founders and CEOs have a very clear understanding of what their business can achieve financially from a P&L perspective; how revenue will grow and how profits will be generated. What is less often known and understood, is how that financial information translates into Enterprise Value at exit. To calculate Enterprise Value, we can use this simple formula:

Valuation = Earnings x Multiple

Earnings is usually a measure of either revenue or profit (for a mature business, a measure of profit is more common). Revenue is typically used when a business is investing heavily in growth and therefore has a negative or artificially low profit figure).

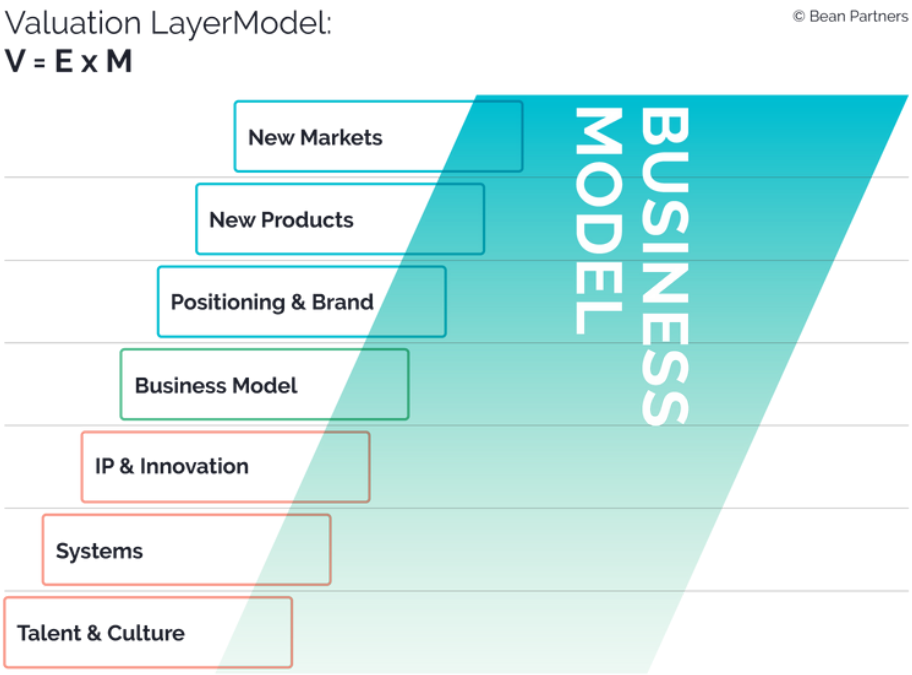
Whilst many business owners focus their growth strategy on Earnings, there is also real potential for driving up valuation by increasing the Multiple. Fundamentally the Multiple is a measure of a businesses' "Future Earnings" potential.

The Multiple that a buyer applies to a potential acquisition depends on a number of factors including:

- Scalability of the business model
- The risk that sits in the business
- Assets created by the business which the buyer can exploit

Many believe the Multiple to be a benchmark set according to industry. The truth is that firstly, the Multiple has a range, and secondly the range in which your business sits will depend on how you categorise the business model.

This Essential Guide gives insight into the 7 levers you can pull to maximise your business valuation by driving the multiple. These levers can be seen using our Valuation Layer Framework below:



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First - Understand and Communicate Your Business Model Dynamics

Your business model is fundamental in setting the context by which a buyer will view the Multiple of your business. To articulate your business model dynamics consider factors such as:

- Target market size
- Target market growth
- Level of competition
- Nature and scalability of your revenue streams

For example, our research indicates that software businesses addressing a large and difficult problem using a business model that drives high recurring revenue, achieves a significantly higher valuation multiple than many other sectors including services and manufacturing.

To calculate your expected Multiple based on business model dynamics, deeper research is required. Too often the mistake is made by comparing to a high profile transaction in the media, where these events are usually outliers and not the norm.

Your business model and exit vision are essential to determine your Enterprise Value. Once determined, the first three points below represent the asset areas you can focus on to achieve the highest multiple possible.

1

Attract and Retain Talent and Build a Strong Culture

Your capability is determined by the talent you're able to attract, develop and retain in the business. This starts with your leadership team, who will be expected to have differing and complementary capabilities. A strong leadership team who are committed to the vision of the business give a buyer confidence in the ability of the business to follow-through on goals and meet its market potential. Beyond this, when your business is known for having top talent, and inspiring them to perform at at the highest level, you are deemed to have achieved something your peers and competitors will struggle to replicate.

2

Build the Infrastructure and Systemise Operations

he more you can systemise the 'way' in which you deliver your business, the less reliant the business appears to be an any one individual or team. A buyer wants to have confidence that not only can the business operate independently of key people, but that it can consistently replicate a high level of output and therefore comfortably scale its operations with ease.

Close consideration of software and systems that can support consistency, efficiency and scale is key, as is their integration into business processes, with evidence that culturally, the team are leveraging those systems with ease.

If you have developed systems that solve unique problems and deepen the assets created within the business, this will further drive your perceived value.

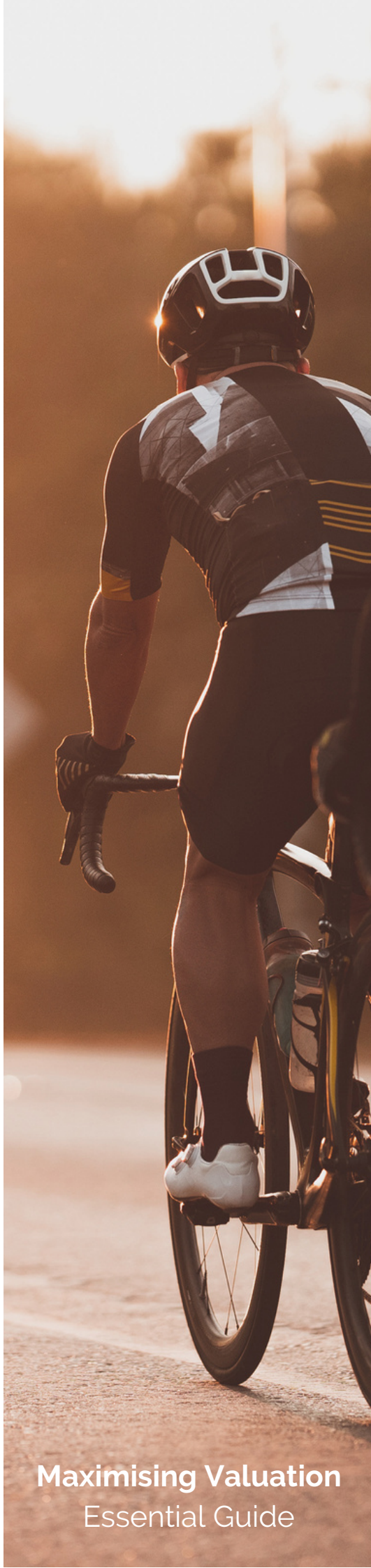
3

Become an innovation machine

One area of the business to systemise is innovation. Having a 'way' your business achieves innovation demonstrates its potential for 'future earnings'. A buyer will have more confidence in a business that is able to flex and respond to changing market conditions and external factors by leveraging its innovation system. It reduces the concern around competitive pressure.

An innovation system should account for the strategic thinking and viability assessment process for any innovation, as well as the process for developing the innovation itself.

Having IP, especially protected IP can support a higher valuation. Having a strong system and process behind developing new IP can have even more worth.



4

Present strong business model metrics

The metrics you are delivering will underpin your valuation. Whilst financial metrics themselves may be represented in the 'Earnings' part of the valuation formula, metrics which sit above 'benchmark' will give you better bargaining power when determining value.

Key metrics to consider include gross margin, revenue growth rate, average contract length and EBITDA margin.

The quality of your metrics are a mirror of the 'scalability' of your business. The following three points are considered the premium layers of the Valuation Layer Model which also demonstrate scalability.

5

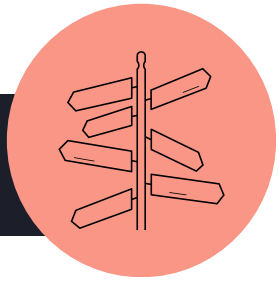
Demonstrate your unique position in the market

To be convinced of the scalability of your business, a buyer would expect to see evidence that you have a very clear position in the market. Your positioning informs your brand, and the stronger your brand in the marketplace, the stronger your position in the mind of your target audience.

Evidence of your positioning comes from research and data demonstrating the 'gap' that you fill. When your position is defined, your business is able to achieve deeper market penetration, customer loyalty and product expansion. This is the potential scale that a buyer will want to feel they have access to, and can leverage once they have acquired your business.

6

Roadmap your future products



The availability of product extensions, both to existing and new markets, gives a buyer insight into your potential future earnings. If you are able to develop the roadmap for these product extensions; demonstrating their technical and market viability, the impact on your valuation could be significant.

7

Demonstrate the potential for market expansion

Being able to demonstrate your businesses capability to open up new markets is a powerful tool to demonstrate potential future earnings. The more systemised your business, the simpler market extensions are perceived to be. Should a buyer consider your business to have the potential to seamlessly open up new markets, it is considered very scalable.

If your buyer were to have a 'foot print' in markets where your business has the potential to expand its product offerings, this would be considered a very complementary opportunity for the buyer. This should result in a higher multiple and valuation, especially when combined with the potential for product extensions.

Building your business using the Valuation Layer Framework is, in effect, creating a blueprint for your business that a buyer can pick up and run with. This is a very attractive proposition and as such should demand a higher than benchmark valuation.

You don't need to deliver every asset within the valuation layers to drive the multiple; you should demonstrate the potential within each layer with evidence in order to give a buyer confidence in the future of your business.

To take your valuation strategy to the next level, you would build your Buyer Universe according to assets and capabilities. By mapping in this way, you can identify active buyers with complementary assets and capabilities who could best leverage and integrate your business. This step allows you to yield the valuation and outcome that is a fair representation of the business you have built.

To find out more about how to pull the valuation levers and build your Buyer Universe, schedule a free 30-minute call with the Bean Partners Team via our website.

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