THE REALITY OF EXIT STRATEGIES

KEY INSIGHTS FOR BUSINESS OWNERS—WHETHER SELLING TO FUND RETIREMENT OR KEEPING THE BUSINESS IN THE FAMILY.

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WHAT DO EXIT STRATEGIES MEAN TO YOU?

Given the serious consequences of not being able to sell a business or leave it in capable hands, exit strategies and succession planning need to be a primary consideration for business owners as they prepare for the future.

Unless you proactively and carefully plan a strategy for handing the reins of your business over, or making it as attractive as possible to potential buyers, you may be left with an unwanted business on your hands.

Yours may be one of many similar businesses on the market at the same time in the very near future as baby boomers retire. There will be an over-supply compared to demand. Failure to plan now can end up costing time, resources and ultimately sale value further down the line.

The good news is that there is plenty you can do to plan for the future.

TYPES OF EXIT STRATEGIES

Business exit and succession plans are all about preparing your business for sale or handover. In the case of a sale, the business obviously needs to be made as appealing and attractive as possible for any prospective buyers, in order to avoid the problems of lower values or an un-saleable asset.

Business owners require a clear understanding of what will happen to their business when it comes time to exit. There are a number of options to realising a return on your business investment, including:

Trade Sale Exit	A company's shares/assets (or even liabilities) are sold in whole or in part. It is often seen as a "clean exit".
Management Buyout	The existing management of a company acquires part or all of the company from the owners (or the parent company).
Intergenerational Transfer	The business owner passes on control and ownership of the business to family members.
IPO	An Initial Public Offering, where a company is "floated" on the stock exchange and shares are made available for private
Merger and Buyout	Two or more companies join forces to create a single entity; it is a mutual decision for the benefit of both.

Every business is unique, and not all strategies will suit. Which exit strategy is right for your business depends on many factors including whether you wish to keep the business in the family, how soon you wish to retire and how much the sale needs to achieve in order for you to retire.

HOW TO PREPARE FOR A BUSINESS EXIT

To be adequately prepared for a future where you expect your retirement to be partly or wholly funded by the sale of your business, or handed over to others in a fit state, you need to create a functioning, documented and appropriately resourced exit or succession plan.

Once you have decided on your preferred exit strategy option, utilising Shirlaws learning management system which guides you through our frameworks and methodologies will ensure you complete the necessary steps towards making your business ready for sale.

There are several main considerations here: when to start planning, who will be involved, how to manage your business if it's "in the family" and how to value your business.

When to Start Planning?

It is generally recommended that a minimum of 18 to 24 months are needed to successfully plan ahead. Research shows that most businesses leave it too late and don't allow the time to make the necessary adjustments or improvements.

Of course, it is never too early to make your business its most efficient, which is one of the main goals of creating an exit plan, but it also means that you'll be well positioned to receive any unsolicited approaches in the lead up to your planned sale or exit date.

Who Will Be Involved in the Decision?

All stakeholders need to have input into the decision.

Clearly if a management buyout is seen as the best option then the feasibility of this needs to be discussed with all parties and preliminary measures taken to structure any agreements to the acceptance of all.

MANAGING BUSINESS EXIT FOR A FAMILY BUSINESS

Many family businesses hope to keep the business in the family when the current principal exits.

Often this is a parents-to-children arrangement but there are some important considerations here and it is not a decision to rush into without taking into account all relevant factors:

- Does the next generation have the enthusiasm, or the will, to follow in the footsteps of the parents long-term?
- Is the next generation capable of running the business? Do they have the necessary skills and experience?
- Do they have personality and beliefs that fit with the values of the business you have created?
- How will the business maintain employee, supplier and customer loyalty when the boss is gone?
- What is the plan if the intergenerational transfer doesn't work

Effective succession of a family business involves overcoming several important challenges relating to the family and to the business itself.

5 STEPS FOR FAMILY BUSINESS OWNERS

Conflicts can arise when people are not clear on roles, responsibilities and processes. It's easy for confusion to reign. With the following steps you can start to transition the company to one based on clarity of company direction, fairness and preparing for a future based on the good of all concerned:

1. Separate family ownership issues from business issues by setting up distinct forums for resolving disputes and conflicts, for instance a shareholder's assembly and a family council.

2. Create a transparent and accountable system, whereby there is reporting to the Board and adequate communication to all the shareholders. The Board may be made up of family members, or a combination of external directors and family.

3. Design a fair system based on a set of family rules and protocols that address all known ownership issue

4. Implement a system that trains and mentors the next generation of future leaders of the company.

5. Ensure that everyone is clear on their own responsibilities and the decision-making processes regarding important issues like future investments, hiring policies, remuneration levels and strategic direction.

WHAT IS THE VALUE OF YOUR BUSINESS?

Obtaining a realistic valuation of your business is not straightforward as it depends on many things, not least the prevailing market conditions. This is where professional advisors can really make a difference.

When valuing your business, it's important to factor in all of your assets. This is more than the bricks and mortar holdings of the company. It incorporates all aspects that can multiply the business value to a potential buyer (or future earnings potential), such as your:

- Client base
- Employees
- Intellectual property (systems and products)
- Distribution
- Brand positioning, and
- Scalability of your operations

Most deals use an earnings multiple (usually EBIT or Earnings Before Interest and Tax) as an indicator for future cash flows, which lies at the centre of a business' value. The more confident that a prospective buyer is of the potential of the business to grow EBIT, the higher its value.

Most business owners sell based on a traditional formula where the key factor is the profit, however sometimes profits are not the most accurate measure which can put some businesses at a disadvantage.

10 KEY EXIT STEPS TO START TAKING - NOW

Whichever exit plan you select, there are a set of steps that can be taken to increase efficiency which potential buyers will value when looking at acquiring your business.

The respective importance of these steps will vary, but the following ten ideas are a good start to increasing the value of your business:

1. Up to Date Financial Records

Get financial records in order. It's important to be able to demonstrate to prospective buyers the current and projected future cash flows.

2. Audit Your Business

If you haven't already done so, this should be completed well before you intend to sell and include at least two years of audited accounts to demonstrate the health of your business to prospective buyers.

3. Separate Personal and Business Tax

This will greatly affect the prospective net gains. The structure of the company should be clean and simple, making due diligence easier. Discuss the tax implications, to the company and personally, of selling assets with a professional advisor.

4. Cut Unprofitable Lines

Make sure you understand what's profitable and what's not in your business. It may be necessary to close sections that are costing the business. Consider the publicly-available benchmarks for profitability of your business type and compare how yours is doing against those benchmarks.

5. Implement Productivity Improvement

In the two years prior to sale, control discretionary spending and look for where you can make improvements and economise without affecting quality. You should also attempt to control capital investments and maintenance expenses.

6. Identify Your Intellectual Property

If you have a business where most of the value derives from what you carry around in your head, you need to start considering ways of passing this Intellectual Property (IP) on. Ensure that you actually do own your IP. If necessary, register trademarks and patents and any other registrable form of IP.

7. Shore up Key Assets

Ensure that leased premises have a lengthy tenure remaining and that all key employees have signed appropriate employment contracts that lock them in. These agreements must be professionally drawn up to protect the intellectual property, client base and trade secrets, as well as having appropriate restraints of trade included.

8. Systemise

Document the business know-how of all key employees and convert this into operations and procedure manuals. Start insisting that that the business operates in accordance with those manuals from now on.

9. Make Yourself Redundant

Ensure that your business can succeed without you running it and you make your business more attractive and less of a risk to prospective buyers. Utilise the right people and implement systems and processes that help to make the business independent of you being there.

10. Optimise Timing

In the two years prior to sale, control discretionary spending and look for where you can make improvements and economise without affecting quality. You should also attempt to control capital investments and maintenance expenses.

At the time of sale, get to know your buyer and customise your offering to what you know they need. This will help them make the decision you want them to take. This little bit of extra reflection and homework about prospective buyers can make a big difference to standing out in the crowd.

THE GROWING ROLE OF TECHNOLOGY

Wherever there is change, there is opportunity. It is interesting to briefly consider the role of technology in exit planning, as it can be a major factor in increasing the value of your business.

Technology is an excellent way to differentiate your business from other similar ones in a competitive market. If there are five businesses essentially doing the same thing, but one of them has invested more in the latest technology and developed an established digital footprint it may be more attractive to a potentialbuyer.

REVIEW AND ADJUST YOUR PLANS

Exit plans must be 'made in pencil' and be ready for you to adjust as required. Making a plan and never reviewing it can be almost as dangerous as having no plan at all.

Market conditions change; unforeseen technological change or a change in your circumstance may affect your business one way or another; you may have a re-think or be forced to exit earlier or later than originally planned.

Whatever the reason, it pays to re-visit your plan and see if all the details still apply. Keep the thinking and information current. Consider it as an ever-evolving process until you do actually exit.

WHAT CAN GOOD EXIT AND SUCCESSION PLANS ACHIEVE?

In any market, let alone a highly competitive one, a business needs to be 'exit-ready' to ensure a good price. Even a steadily performing business will fail to attract bidders if it isn't prepared in some of the basic areas such as tax, financial records and management structure.

A regularly reviewed exit plan will help demonstrate to a bidder that the company is healthy and represents a good investment with growth potential. It prepares the company for audit, gets key financial records in order, and addresses the question of tax and staffing/management concerns of any prospective buyer.

A well-drafted succession plan that has addressed the concerns of all stakeholders in a family business ensures a smooth intergenerational transfer, with the minimum of conflict. In this way a small business that has been painstakingly built up over decades can survive into the next generation.

As baby boomers look to sell to fund their retirement, we can expect an oversupply of businesses for sale on the market.

Business owners with unrealistic expectations or who keep working in their business instead of on it, without any forethought for succession, may be disappointed when they are unable to attract the price they hope for. Some businesses may be forced to simply close down when they don't find a buyer or may just fade out of existence. Considering the contribution of the SME sector to the economy, this is likely to have a significant effect on employees of the businesses and the community at large.

The good news is that businesses have time to start planning for their future. Whether it's a family transfer or a trade sale exit, business owners carrying out simple exit steps such as cutting unprofitable lines, protecting their IP and key employees, and getting their accounts audited can expect to negotiate a better price.

START PLANNING YOUR BUSINESS EXIT

Shirlaws develops people and improves bottom-line performance using unique, tried and tested methodology.

SMEs are supported to learn vital skills and gain knowledge which improves profits and builds long-term sustainable growth, creating more money, more time and less stress for business owners.

For more information on how Powered by Shirlaws frameworks and methodologies can help you prepare your business for exit, contact:

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