

THE EXIT

4 Keys to Maximizing Valuation

EXECUTIVE SUMMARY: *Scaling to sell, using the Scaling Up tools/techniques, maximizes the value of your business whether you plan to exit or not. The first half of this chapter highlights four keys to driving a significant increase in valuation: Become redundant, gain control of an industry constraint, achieve a 10x internal advantage, and generate consistent growth. The second half details the pitfalls to avoid in selling your business. Buyers' calculated (devious?) moves can cost you tens of millions in cash if you're not careful.*

Stephen Adele and his four co-founders at QuickBox Fulfillment, a Denver-based firm that does e-commerce fulfillment, grew the company to 500 employees and \$57.3 million in annual revenue in two years. They sold an 80% controlling interest in the firm, founded in 2017, to Pike Street Capital in 2019 in an eight-figure deal.

How did they pull off this quick exit? The Scaling Up platform helped them achieve their goal of building the company to sell. "I wasn't even sure some of the practices would work but found them to not only work but be incredibly powerful in scaling the business," says Adele, who led the company as CEO and is now a member of the board of directors.

If you are planning to exit in the next six to 36 months, using the Scaling Up platform can help you to do what Adele and countless other founders and CEOs have done: maximize the valuation you receive, often to two to three times an industry standard multiple. This puts tens of millions of dollars more into your pockets as business owner(s). In the meantime, the platform makes it easier to scale while driving industry-leading topline and bottom-line results

Additional \$100 Million

Greg Slamowitz's journey was a bit longer than Adele's. As he describes it, his life was exhausting as he launched and ran Ambrose Employer Group, a professional employer organization (PEO). After eight tough years he managed to get to 35 employees and \$2.5 million in earnings — and was stuck.

He then discovered Scaling Up, hired a Scaling Up coach who facilitated quarterly planning sessions for eight years, and attended our annual Scaling Up Summits with 12 of his leaders without fail. He figures he spent roughly \$300,000 on coaching and learning. The result? He was able to scale to \$20 million in earnings "with ease and loving life." After exiting to General Atlantic, he credits Scaling Up with generating a \$100 million of the \$200 million all cash offer he received — more than a 3,000% return on his investment. Here's a link to a video where he explains the process and results.

<https://vimeo.com/689465085>

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Billion-Dollar Promise Kept

Four of the five companies from the first London cohort of our 20,000 Scaleups initiative launched in 2018, have already seen exits, with a combined value near \$920 million:

- Exponea, a leading customer experience and data platform, was acquired in 2021 by Bloomreach, a leader in the ecommerce experience, and received a \$150 million investment by Sixth Street Growth.
- LegalX, which was the UK division of the Australian tech firm GlobalX, was acquired by Dye & Durham for AUD 170 million in 2021.
- Carousel Logistics, after merging with another European logistics carrier, DANX, was acquired by the private equity firm Axcel in March 2022.
- Point A Hotels, with 1,520 rooms across 10 hotels, was acquired by Tristan Fund and Queensway, for £420m in April 2022

With plans to launch in 150 cities around the globe, one of our promises to supporting cities is that the 20,000 Scaleups initiative will help several of their local firms exit for a combined \$1 billion. We delivered on this promise within 48 months of our launch in London. This matters because these companies and their owners tend to reinvest a portion of their exit funds back into their cities (charities, angel funds, etc.).

Additional case studies of firms crediting the Scaling Up tools/techniques for driving eight, nine, and 10 figure exits can be found on our media site www.scaleups.com.

Following are the four competitive advantages, which many owners credit with driving up the valuations of their businesses. These four align with our Scaling Up Performance Platform framework: People, Strategy, Execution and Cash, which are covered throughout the book. How many of these valuation-enhancing attributes does your company possess? It's worth a final review as this book comes to a close.

People: The CEO Is Redundant

When the owner is critical to a company's success, it is much riskier for someone to purchase the business. It's best for future business owners, and you, if the business can both survive and thrive without you.

Think Apple. Many people thought Steve Jobs' baby would never survive after his passing in 2011. Yet a decade later, the company achieved a valuation almost 10x what it was when he passed. Just like in parenting, the measure of your success is how your "children" behave when you're not around!

The Scaling Up Performance Platform helps you do just this. It reduces by 80% the time it takes for an owner to manage the business. And after 36 months, with the support of a coach, most CEOs are able to spend as little as a few days a quarter primarily driving strategy. And this gives owners time to be actively involved in the process of exiting their business. Warning: Keep it a secret that you're spending almost no time "in" the business.

Working 100-hour weeks? Put more of the business on autopilot with a well-functioning senior team implementing Scaling Up and see your valuation (and life!) soar.

Strategy: Control an Industry Constraint

Giving CEOs more time to focus on strategy, the Scaling Up Performance Platform next provides the tools and techniques they need to identify the key constraint in an industry. Gain control of this and you'll be better able to control your destiny.

In my second book, *The Greatest Business Decisions of All Time*, I detail how the late Robert Taylor “blackmailed” Colgate-Palmolive into purchasing his firm for a gazillion dollars (\$75 million, a lot of money in the Eighties). He recognized that the key component of his Softsoap liquid soap offering was the spring pump. Given there was only one manufacturer of those pumps at the time, he purchased the entire annual production of the manufacturing firm (100 million units at a price of \$.12 per unit), guaranteeing Colgate, P&G, and others couldn't compete with him — and forcing Colgate's hand in eventually purchasing the company.

Virtual Technology Corp (VTC) did the same, locking up all the unique talent in its military simulation niche. Raytheon later came along and purchased VTC for a gazillion dollars (we can't divulge the amount) to keep the competition from having access to this critical source of talent.

Is there a key constraint in your industry? Gain control and your valuation will soar.

Execution: Insider 10x Advantage

After you've won control of a key external constraint, the Scaling Up Performance Platform will help you identify the equivalent in your business model. Labeled an X Factor, it's an internal 10x advantage over the competition. This advantage helps strengthen the moat around your business and signals to a strategic buyer what they could achieve, given their much larger resources.

The late Wayne Huizenga was able to negotiate a price for the videos Blockbuster rented that was 1/11th the price competitors paid. John Ratliff's Appletree Answers call-center firm had 10x better employee retention than the industry average (18% vs. 200%). Barrett Ersek's firm Happy Lawns landed customers in 5 minutes vs. an industry average of 5 weeks. Steven Adele's firm figured out how to generate 5x the revenue per delivered package than many of the company's rivals. And all four exited for outsized valuations.

This internal advantage is like a buyer knowing there is a “Rembrandt in the attic” of a home they're buying. Buyers are going to be much more willing to offer considerably above asking price to secure this outsized internal advantage.

Is there an aspect of the business where you outperform the competition by a factor of 5 - 10? Nail this and your valuation will soar.

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Cash: Steady Growth

Achieving a 10x advantage that addresses a widespread internal issue in the industry is also key to bringing stability to growth. Your valuation will be much greater if you've had consistent growth in revenue, profitability and, especially, gross margin dollars, than if your growth has been erratic. Disciplined and steady performance, which the tools/techniques of Scaling Up help to provide, proves the company can create and deliver consistent results in a chaotic environment.

Greg Alexander achieved a \$162 million exit from his management consulting firm, Sales Benchmark Index, which specialized in sales effectiveness in the B2B space, by using the Scaling Up Performance Platform to deliver consistent results in that industry — compounding an annual and steady growth rate of 30% for a decade.

Is your growth rate consistent and lacking drama? Demonstrate you have control of your business, even in periods of economic chaos, and your valuation soars.

Conclusion: Master All Four

Become redundant in your business, gain control of an industry constraint, achieve a 10x internal advantage, and generate consistent growth — and scaling your firm will be easier and more fun. And if you exit, you'll receive an outsized valuation.

The Scaling Up Performance Platform has helped thousands of founders and owners master each of these advantages. Again, our media site www.scaleups.com details many success stories, including those that eventually exited.

The most exciting two days in many founders' lives are the day they start their business and the day they sell it. Putting the right systems in place can help you ensure that you enjoy the journey in-between and that your exit is as rewarding as it can be. This will pave the way to new opportunities to achieve an impact in the next chapter of your life.

The challenge, if you decide to sell the business, is navigating the exiting process to assure you get top dollar for all the years of blood, sweat, and tears.

The Games Buyers Play

Business owners work years building up the value in their company, only to give a big chunk of it away when it comes time to sell. Why? Savvy corporate acquisition and private equity teams wear down the most seasoned and savvy owners using a well-practiced method, backing them into a corner where they have to sell for a steep discount.

Here are some of their questionable, (and sometimes dirty) tricks.

Promises, Promises

The first step is counterintuitive, which is why it's so effective. The buyer — typically a significantly larger corporation — offers the owner an insanely high price for the business and suggests the deal can close in weeks.

The price, almost always expressed indirectly as some multiple of earnings before interest, taxes, depreciation and amortization (EBITDA), will be a price that is 25% to 100% more than what the business owner even thinks the business is worth. At this point the owners think they've landed the deal of the century — while the reference to earnings sensitizes the seller to reduce expenses (more on this later).

Why would the buyer do this? To get sellers to drop their guard. Nothing builds a temporary relationship faster (look, the CEO is not likely to stick around after the sale) than offering a premium price for the business.

It also gets the owners and their spouses dreaming about the life they will lead after the sale — the houses, boats, and vacations — once they have a boatload of money. The potential buyer will often take them to dinner and discuss these precise topics to help them imagine their future. But when buyers casually ask about vacation homes and boats the seller might buy, it is never casual. It is a big red flag!

The buyers are also offering a price they don't plan to pay to entice sellers to sign an exclusivity agreement that prevents the owners from talking with other potential buyers for a few months (there goes the competition for your firm), while the buyers do their due diligence — which they promise will go quickly.

The sellers will usually sign on the exclusivity dotted line, relieved that they are going to get a great price and not have to deal with other buyers, which is extremely time consuming. The trap has been set.

Psychological Warfare

Once the document is signed, the buyer now drags out due diligence for months, while promising all along the way that everything will be wrapped up shortly. If I had a nickel for every time a seller heard "It's just a couple weeks more," we could all retire.

Because the buyer implies all along the selling price is tied to some multiple of EBITDA, the sellers start putting off key expenditures they would otherwise make to keep the business humming — a key hire, marketing spend or training/planning session.

To make matters worse, the buyer, early on, asks about anniversary dates, planned vacations, industry tradeshows and other key plans and then starts disrupting the seller's rhythms and life through the infamous "emergency meeting." The evening before the seller departs for a family vacation or major trade show, the M&A team will call to say that there's been a problem with the deal and demand that he or she show up for a meeting the next day to straighten things out.

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Afraid to derail the deal, the frazzled seller will cancel the departure. Now the family and business team start pushing to get the deal done. The pressure continues to mount.

Diminished Performance

With the owner mentally checked out of the business, cutting back on critical expenditures to pump up EBITDA and worn out from missing vacations and the grind of due diligence, the business typically suffers a temporary slump. It's all part of the buyers' game plan. The buyers want the company's performance to suffer a little so they can use it as a giant sledgehammer to drive down the price at the 59th minute of the eleventh hour.

They might seize upon something they have deliberately left open to negotiation in the Letter of Intent (LOI). One classic example is the "working capital peg." Companies are often sold "cash free, debt free" which means the seller takes out the net cash to pay off debt, with some reasonable working capital left in to operate the firm. In one classic late renegotiating tactic, buyers will pressure the seller to leave a more "reasonable" amount of working capital in the business than expected.

Beat up by the entire process, the seller begrudgingly gives in to this or other kinds of last-minute demands and concessions, and ultimately lowers the price — to a fraction of what was originally offered. The buyer wins big, and the seller leaves millions on the table.

Bidding Wars

How do you avoid this scenario—and still sell your business? Always enlist an outstanding sell-side advisor experienced in M&A work (this is no time for amateur hour). All professional athletes and entertainers have agents for a reason. It's impossible to represent yourself without getting dirty. You need a "bad cop" in the deal when things get dicey, and they always do.

The primary job of the sell-side advisor is to seek out strategic vs. financial buyers — and to help uncover/discover the "Rembrandts in the attic" (described earlier in the chapter) that will drive your strategic value in the marketplace. Then they'll set up an auction for you. Don't let a single potential buyer call the shots. One friend's sell-side advisor identified 23 strategic buyers of which seven came to the table to bid for the business.

If a serious prospect wants an exclusivity agreement, only after your sell-side advisor has run a soft-auction (never before), limit it to 30 days. This puts pressure on the buyer to complete due diligence quickly. And have "the box" of materials prepared in advance so you are bulletproof during due diligence. In fact, the best practice is to run a full "reverse due diligence" on your company long before a buyer does. It can help identify key issues before hand. Surprises in diligence have killed many deals.

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Due Diligence Warning

During due diligence, emphasize that this is NOT a time to renegotiate the deal but to verify what has been negotiated in getting to the LOI. This is where your sell-side advisor is key. Make it clear early that any attempt at an unreasonable re-negotiation is a cause to terminate exclusivity and will not be tolerated.

Last, as best you can, insulate yourself from the transaction. Have your CFO or another trusted executive work with your sell-side advisor to act as a go-between with the buyer, so you don't get distracted from leading your team. Push back against last-minute demands for meetings. You want to be calm and think clearly every time you negotiate—and not fresh out of a fight with your spouse about cancelling the family vacation.

Overall, keep your head in the game and continue running the business as if the deal isn't going to happen up until the moment you cash the final check!! Your willingness to walk away from the deal is the ultimate competing buyer. That mindset will put you in your strongest negotiating position, as will lining up other buyers who understand how they can multiply your strategic value in the marketplace.

By finding the right strategic buyers you can create a group that doesn't just "want" to buy your company, but "needs" to acquire it to further their strategy. This shifts the balance of power entirely to your side. Having two or more bidders on fire to buy you is an entirely different experience than negotiating with a sole-sourced buyer acting like they are doing you a huge favor.

Public Company Multiples

Whenever a business owner has mentioned they want to sell their business, we steer them to certain sell-side only advisors and advocates. The first time was a close friend who had almost signed with a major accounting firm to sell his firm. The allure was its global reach and that it had brokered many firms in a similar space with significant contacts in my friend's industry.

Though purporting to represent the seller, these large accounting and M&A firms have much closer relationships with the buyers, likely helping to facilitate dozens of transactions for them. In turn, they are likely to do only this one transaction with you. To whom are they more loyal?

Worse, if the M&A firm has done a lot of transactions in your industry, they can't afford to get you a much higher valuation as a multiple of earnings than they did the previous dozen transactions, to protect their reputation. You will be stuck in a financially driven formula that ultimately gets you three to seven times earnings, depending on the standard in the industry.

To these larger brokerage firms, you are just another transaction. Additionally, they may do other work for buyers around quality of earnings, valuation, etc., so they can be conflicted. In contrast, the right sell-side advisor focuses on maximizing your return.

Unique Strategic Advantage

You've spent years, if not decades, scaling the business. Most of your net worth is likely tied up in all this effort. Our approach is to discover your unique strategic advantage — one you are so close

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to you don't even see it (it takes a fresh set of eyes to uncover it) — and then to identify a potential pool of up to 200 buyers.

And it's important to bring to the table international buyers who are willing to pay much higher valuations for firms simply to enter the seller's market(s). Ultimately, the right sell side advisor creates a soft auction among a handful of buyers until it gets two or three firms fiercely competing to buy your business.

This is a much lengthier process and usually the fees increase as a percentage of the sale if it gets you considerably more for the business (isn't this how it should be). Luckily, my friend engaged the right sell-side advisor, which sold his firm for 3x the number in his mind (on the high end of multiple of earnings in his industry), and 5x the number in his spouse's mind. The extra tens of millions matter.

Many of Scaling Up's clients have achieved exit multiples of 15, 20, 30, or more of earnings. To be fair, most of these firms have used our Scaling Up tools/techniques to scale their businesses, making them much more attractive to larger companies. Public companies especially appreciate the quarterly discipline and meeting rhythms Rockefeller Habits 2.0 instills within organizations. These larger firms often note that our clients operate better than they do! This is why several of the CEOs we coach have gone on to become CEOs or senior executives inside global 500 firms.

Golf or Tennis Pro

If you're within six to 36 months of wanting to exit your firm, please reach out to me at verne@scalingup.com and we'll arrange for a complimentary consultation on what the valuation would be for your business from strategic international buyers.

Selling (or scaling) a business for the first time is like the first time picking up a golf club or tennis racquet. You can be an outstanding athlete, but you will be no match for a seasoned player. Worse, you are often up against world class players in the market and M&A space.

It is millions you're risking and likely one of the most important transactions you'll make in your life. Make the very best of it so you can keep scaling your impact for generations to come!

