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EXIT PLANNING SUMMIT

CREATING WINNING M&A OUTCOMES

Fair Market Value vs Strategic Value:
Don't Leave Money on the Table

PRESENTER:

SCOTT MASHUDA

Founding Partner, REAG

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Scott Mashuda

Founding Partner, REAG

- Lead the firm's growth and strategic vision with 20+ years in M&A and business valuation.
- Faculty at The Exit Planning Institute, teaching M&A processes since 2020.
- Chair of M&A Source in 2023. Board of Governors member since 2017.
- Recognized as a top M&A service provider in "40 Under 40" by The M&A Advisor (2013).
- Active in Cleveland's Association for Corporate Growth; former adjunct professor at Duquesne University.
- Co-founded REAG in 2004; previously a senior valuation analyst at Ernst & Young.

AGENDA

- Price vs. Value
- Fair Market Value
- Strategic Value
- Play a Game

Price vs. Value

Price:

- Fact
- Sum of money (or its equivalent) for which anything is bought, sold, or offered for sale

Value:

- Opinion
- Relative worth, merit, or importance
- Industry-specific trends

Understanding Value

Value:

- Risk vs. Return

In an M&A Transaction:

- The applied multiple captures the perceived risk of achieving the expected return
- Projected EBITDA represents the expected financial return generated by the selling company

Potential Risk Factors

- Quantity and magnitude of normalized adjustments
- Lack of contractual based revenue
- Customer concentration vs. diversification
- End market concentration vs. diversification
- Lack of consistent and repeatable contracts, processes, and business practices
- Weakness vs. strength of management team
- Reliance on owner (seller)

Fair Market vs. Strategic Value

Fair Market Value:

- Willing Buyer
- Willing Seller
- No Compulsion
- Both have reasonable knowledge of all relevant facts

Strategic Value:

- Seller's projected cash flow on a standalone basis plus the value of the synergies from combining with the acquirer
- Greater than the value that can be extracted from the profit generating resources of the company being acquired.

Fair Market Value Calculation (7x)

Accounting FMV EBITDA	$ 5,000,000
+Normalizing Adjustments	+ 300,000
Normalized FMV EBITDA	5,300,000
x Multiple	x 7.0
Enterprise Value	**$ 37,100,000**

Strategic Value Calculation (7x)

Normalized FMV EBITDA	**$ 5,300,000**
+Better vendor pricing of 2%	+ 106,000
+Overhead reduction	+ 500,000
Strategic EBITDA	5,906,000
x Multiple	x 7.0
Strategic Value	**$ 41,342,000**

Valuation = Risk vs. Return Analysis

- Prior example focused solely on the financial return side (EBITDA) of the equation
- The multiple did not change
- The multiple an acquirer pays depends on their assessment of risk
- Lower risk = higher multiple
- Higher risk = lower multiple

With New Ownership: Acquirer Providing

- Customer diversification
- End market diversification
- Depth of management team

- **Result is a multiple of 7.5x vs. 7x**

Fair Market Value Calculation (7.5x)

Accounting FMV EBITDA	$ 5,000,000
+Normalizing Adjustments	+ 300,000
Normalized FMV EBITDA	5,300,000
x Multiple	x 7.5
Enterprise Value	**$ 39,750,000**

Strategic Value Calculation (7.5x)

Normalized FMV EBITDA	**$ 5,300,000**
+Better vendor pricing of 2%	+ 106,000
+Overhead reduction	+ 500,000
Strategic EBITDA	5,906,000
x Multiple	x 7.5
Strategic Value	**$ 44,295,000**

Value of a GREAT Investment Banker

Starting Value ($)	Ending Value ($)	+Value ($)	+%
Normalized FMV EBITDA (7x) 37,100,000	Normalized FMV EBITDA (7.5x) 39,750,000	2,650,000	7.1
	Strategic EBITDA (7x) 41,342,000	4,242,000	11.4
	Strategic EBITDA (7.5x) **44,295,000**	**7,195,000**	**19.4**

Value to the Seller

- Strategic value is unlocked by identifying the “right fit”
- Key to unlocking it is a great investment banking team that can run a robust, clean, professional process (REAG)

Gametime

The Game

Rules:

- Only bet in $1 increments
- Cannot have consecutive bids
- $20 goes to the highest bidder
- Second highest bidder pays their bid but does not win the $20

The Game vs. M&A

- Created a market that didn't previously exist
- The investment banker set the rules of engagement and ran the process
- Asset was valued based on FMV principles
- Market gained efficiency as the game progressed
- Value was set based on risk versus return analyses
- Risk was introduced in not doing the deal
- Strategic value was ultimately paid

Takeaways

- Investment Bankers create competition for the seller’s business
- Competition is the key to unlocking maximum value for the seller
- Make sure you’re working with a GREAT investment banking team!

REAG

M&A Brokers | Lower Middle Market Investment Bank

Questions?

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THANK YOU

Questions?

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