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Preparing a Business for Sale—Part III: Plotting the Course

Specific actions need to be taken to achieve a competitive process.

by Mark Working

Investment bankers provide a variety of services, but a banker's primary mission is to create a competitive market for an illiquid asset – the privately held business. Competition invariably brings out the best, and a competitive market is created when each relevant and capable buyer simultaneously has a complete understanding of the opportunity. But for a decision on price, there are no unknowns. This article is the third in a series of three essays, each delving into a critical area in which advance preparation can make a meaningful impact on the ability to create a market for a business.

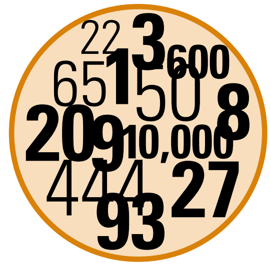
The banker's ideal outcome is conversion of a complex business entity into a virtual commodity. While this is rarely achieved, one can come close. It requires specific actions on the part of owners and managers to prepare the business for a competitive process. Three areas that stick out in our minds are the subjects of our series:

- **Data matters; its absence leaves only a story.** The existence of and accessibility of data on the detailed operational and financial mechanics of the business are necessary to quantify the company's business model and how it employs its capital and earns its return.
- **Understand the problem your company solves.** The size and growth curves for the market, the number and nature of the competitors, and how customers make buying decisions need to be understood and quantified in a manner that defines the environment in which the company competes; understanding precisely which problem the company solves thereby creates the framework for defining each of these items.
- **The future course must be plotted.** There is a specific value proposition that underlies every business and customer buying decision. What is it? The roadmap for future success has to be specific such that the equation for return on capital employed is clear to the potential next owner.

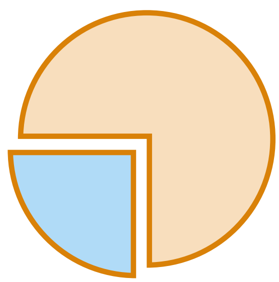
PART 3: PLOT THE COURSE

Part I of this series outlined the necessity of developing robust data systems inside the business being brought to market. Part II addressed the need to define the position of the business within its ecosystem by asking, "what problem does it solve?" Part II also pointed to the need to quantify the expected future growth in the market, thereby defining the size of the pie for all competitors to pursue.

Part I: Data Matters



Part II: Understand the Problem



Part III: Plot the Course

Plotting the course for the future requires several steps:

1. What strategy or strategies will be most successful in the future to solve the market's problems? Features, price, service?

2. What changes can be made by the business, and by when, to best position it to compete to solve future problems?

3. What are the financial implications of those actions over time?

Every market is dynamic, so it is not enough to suggest that overall market demand will grow by X% per year, therefore your business will follow suit. Competitors will adjust their offerings to try to garner a larger share. Some will compete on price; others will emphasize utility, ease of use, assistance, or some other service tied to the product. Fully understanding the nature of the problem to be solved and the possible approaches to offering a solution provide a basis for determining the best future course. Not all businesses will choose the same strategy, or are able to do so, because of differences in capabilities, resources, or market position. For example, the largest company in the market might be able to invest in infrastructure that will decrease its unit costs, thereby enhancing its price competitiveness. This would be harder for a small company as it would be much more difficult to realize the same scale. The course for each business should be the one that is optimal for its specific situation and is achievable within the constraints placed on it. The critical thing is to demonstrate an understanding of the issues and tradeoffs, and to articulate the rationale for the choice of direction.

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The future profile and characteristics of the

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business might be quite different than they are now. A path of activities needs to be defined that show all steps in the transition of the business from its current to desired state. Will the "go-to-market" approach be different? If so, does that mean changes in the sales and marketing effort, the number and attributes of the employees, or the use of external parties in different aspects of the strategy? Will products be produced differently from how they are today? Will there be expansion in physical capacity, outsourcing of services or production, different production processes, or integration of supplier or immediate customer functions? What actions will occur and when? They will need to be mapped out.

Numbers follow activities. A financial plan is the final step in the process. In essence, the financial plan is simply the future story of the business translated into another language – numbers. The backbone of the plan is the activity that is planned to occur – labor and infrastructure configuration, supplier arrangements, and revenue streams. Thinking about revenue as the product of units and price tells a lot about the specific positioning in the market and the expectations for results. If the activity is not projected and revenues and costs are not connected to that activity, expect to have to answer these questions from a buyer. If the logic doesn't tie together, it can change the negotiating dynamics.

The theme of this three part series is that planning is complicated and complex; it takes time and can result in conclusions that imply the need for change. The best strategic plan has as its core, good judgment and insight into the dynamics of the market, and is based on a solid foundation of data. This all takes work, but it pays off. Even if there is no transaction in the future, this effort will result in a better business. If a transaction is contemplated, besides being a more attractive business, due diligence efforts will be much smoother. Once an organization commits to regularly collecting and analyzing data along its value chain and translates those insights into tangible well-conceived plans, it will find benefits in management decisions, as well as being prepared when a sale process begins. **ZS**

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ABOUT ZACHARY SCOTT

Zachary Scott is an investment banking and financial advisory firm founded in 1991 to serve the needs of privately held, middle-market companies. The firm offers a unique combination of in-depth knowledge of the capital markets and industry competitive dynamics, sophisticated analytical capabilities, and proven expertise in structuring and negotiating complex transactions. For more information on Zachary Scott, go to **ZacharyScott.com.**

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