

Mind Your Own Business

In this issue: Show me The Money



Small Business Owner Exit Plans



- Other:**
- Go Public = 28%
 - To Partners = 23%
 - To Children = 17%
 - To ESOP* = 16%
 - Other = 18%

* Employee Stock Ownership Plan

Data from an Inc. magazine survey

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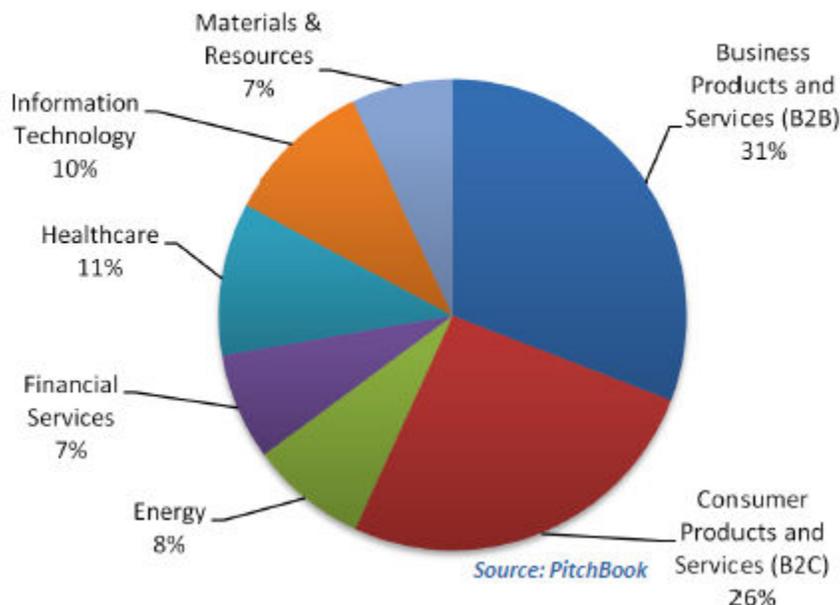
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Family Business Legacy

- 30% of family businesses successfully transition to the second generation (per a study the University of Southern Maine)
- 15% of businesses survive beyond the second generation (per a study by U.S. Trust)

Money Looking for Opportunities. Who Wins?

PE TRANSACTIONS BY INDUSTRY SECTOR IN 2Q 2010



The graphic at the left gives an indication of where the M&A activity had been to mid-year 2010. This chart is only for reported private equity deals because private strategic deals are harder to track. Nonetheless this is a useful high altitude view of where some of the action is.

To put this into perspective there is about \$650 billion dollars in U.S. private equity money looking for deals to invest in before they have to give the money back to the limited partners. There is also about \$975 billion in investment capital sitting in U.S. corporations.

This situation can favor sellers in well-managed auction.

You Can Only Measure It By Looking Out the Rear Window

It's Over!

On September 21st, 2010 it was announced by the National Bureau of Economic Research that the recession had ended in June of 2009. That was 15 months before!

Why did it take so long to discover that nadir had passed long ago? Measurements rely on hard quantitative data (as opposed to guesses or forecasts). "Hard data" results from measurements of things that have already happened, not on guesses about what may happen. Therefore, you can only measure an economic event in context by looking at the past.

Business Retrospective

What is true of the economy

is also true of every sector within the economy. You don't know when a business sector has peaked or when it has troughed until you have enough objective historical data.

In the present context this has important implications for deciding when it is time to exit your business. You will never know the right time until you see it in the rear view mirror

Seller's remorse vs. Non-Seller's Remorse

Accepting that you can never buy or sell a business (or a stock) at the ideal time is the important first step to avoiding remorse about the timing

decision. You will be late or early. Which is best?

Hedging the Bet

If you're later to market than competitors there's little you can do to hedge your bet. If you're earlier to the market than competitors it may be possible to hedge your bet.

In this context the "hedge" is created with a deal structure that allows you to exit yet share in the benefit of the business's post-sale momentum. This is done through performance based deal components in an "earnout". An earnout is not right in every case and requires careful drafting but it can take the edge off the exit timing decision.

Fibonacci Retracement

Even very experienced technical stock market traders understand they can't recognize a peak or trough when its happening. To make decision-making easier they use models. A popular one is based on the Fibonacci number sequence (identified by the eponymous 13th century mathematician).

In technical analysis a "Fibonacci Retracement" is created by looking at past markets and using the ratios between Fibonacci numbers to estimate when the current market is within a certain percentage of its estimated peak (e.g. 23.6%). This is seen as a trigger point at which to exit rather than to wait longer as the peak could occur sooner and you could miss it badly (e.g. at 20% less than the current trigger point).

The lesson is that you must have the discipline to lower your risk by realizing your gains ahead of the hoped for peak price and by hedging when possible.

Bargain Hunters and Bottom Feeders

Challenging economic times and the cusp of a recovery tend to bring out the bargain hunters and bottom feeders. They trawl for weakened businesses that they can acquire for depressed values from disheartened owners. How do you recognize them and how do you deal with them?

This class of buyer can initially look just like any other interested party but they usually begin by making a direct and unsolicited approach to a target business rather than responding to an offer for sale (this is not to say that all such approaches are by this type of buyer). They get attention by floating a possible price that falls within a reasonable range.

Thereafter the bottom feeder will quickly try to lock in a no-

shop period (an exclusive negotiation period) that is relatively short (30-60 days).

Having gotten some level of commitment from the seller the bottom feeder will begin to slow down the pace of the process. They believe that the longer they draw out the process the more opportunity they will have to drag the seller down on price and terms.

Amongst their tactics:

- repeatedly bringing up minor issues to justify lower offers
- submitting written offers that are inconsistent with verbally agreed terms
- inserting undefined "material adverse change" contingencies allowing them to justify a price reduction later on

If a bottom feeder is interested in your business then it's likely that full value buyers will also be interested. The best way to screen out bottom feeders and to get full value is to have several offers to consider at once.

To attract multiple competing offers (while protecting your business) you'll need to conduct a confidential "auction". In the context of that auction the bottom feeders will be easy to weed out.

If the business is in decline and/or in a challenging market a lower price might be justified but competition for the business provides the context for informed decision-making. It also give you the leverage to negotiate favorable deal terms and structures.

The Magic Multiples

The most common rule of thumb for measuring the relative prices paid for businesses is X times EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) but what does it tell you?

This rule of thumb is most useful when looking at large volumes of sale transactions to get a general feel for trends in the market, per the table at the right. The table uses "Total Enterprise Value" rather than price because not all investments were total buyouts. In cases where less than 100% was purchased TEV shows the pro rata value of the whole business.

The most obvious pattern is that the larger the TEV the

TOTAL ENTERPRISE VALUE (TEV)/EBITDA—ALL INDUSTRIES

TEV	2003–					1H		N =
	2005	2006	2007	2008	2009	2010	Total	
10-25	5.5	5.7	5.4	5.3	5.1	4.8	5.4	392
25-50	6.0	6.0	6.2	5.9	6.1	6.3	6.0	295
50-100	6.1	6.5	6.6	6.4	6.1	6.2	6.3	186
100-250	6.9	6.8	7.5	6.6	6.5	6.9	7.0	69
Total	5.9	6.0	6.0	5.8	5.7	5.5	5.9	
N =	337	171	189	131	72	42	942	

Please note that N for 2003-05 encompasses three years of activity.

SOURCE: GF DATA RESOURCES LLC

larger the multiple of TEV. So large deals and small deals have different rules.

Aside from TEV what is hiding inside this data that you would need to know to make sense of it? Here are a few:

- Is the price paid in a single payment based solely on historical EBITDA or are their

future contingencies that can change the multiple?

- Is it a business with a high or low future Capex requirement?
- Which sector is it in?
- The average is shown for a volume of deals but what the EBITDA range?

The lesson is to be cautious with rules of thumb.

Sector Trend Review: Diagnostic Imaging Centers

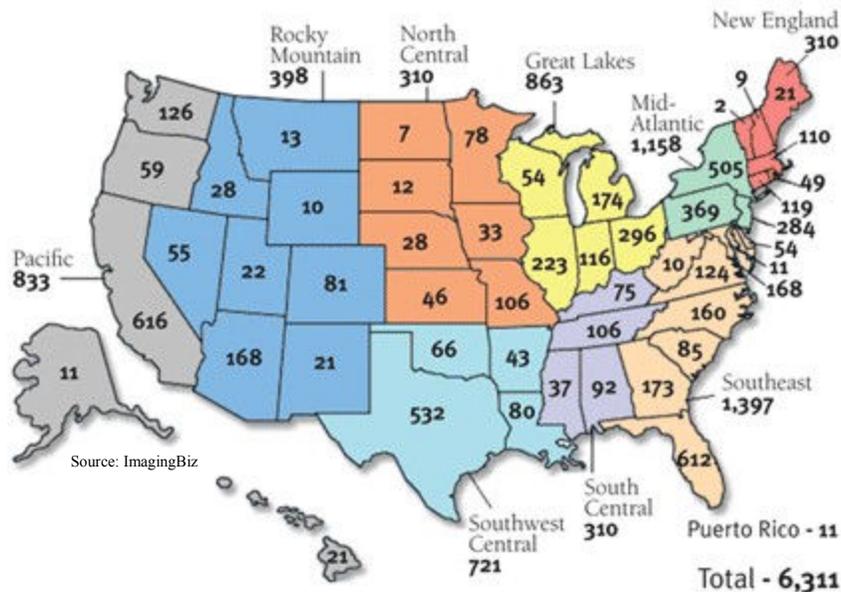
Given all the pending changes in healthcare it is timely see a snapshot of one medical service sector that boomed in the 1990's with physician-owned diagnostic imaging centers.

In its most recent review *Imaging Business* found that imaging center consolidation in the US continues but at a different pace in different regions. Among their findings in comparing 2008 to 2010 was that there was about an additional 2% net reduction in the number of imaging centers (-120). The current state count is shown in the map at the right.

- The Southeast lost 56 imaging centers.
- The Southwest gained 8 centers.

- Great Lakes, South Central, North Central and Northeast have about the same net number.
- Mid-Atlantic, Pacific and Rocky Mountain regions together saw a decline of 55 centers.

The average number of imaging centers per 100k of U.S. population is 1.6 but some states have a much higher concentration (DE=6.1, RI=4.65, CT=3.38, FL=3.3, NJ=3.2) and we're likely to see consolidation continue.





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Blackbridge Partners LLC is a Boston-headquartered investment bank. We specialize in merger and acquisition and capital raising advisory services for owners of privately-held lower middle market companies seeking to harvest maximum value upon exit and companies seeking to acquire the same.

We are a boutique firm delivering a level of professional service not usually available to the lower middle market.

Our experience ranges from medical services to manufacturing, software, IT services, technology and professional services.

Specializing in the Middle Market – Businesses with revenue of \$5 - \$150 million.

What's the Business Sale Process Like?

Harvesting the maximum value from your business takes time and requires a considered process. Even before seeking outside advice there are some things that you should do:

Preparation

1. The initial step is to consider what your personal timelines and goals are and to begin tax planning.
2. The second step is to make sure that all of your records (leases, employment, financial, corporate, etc.) are accurate and up to date.
3. Next look at outside factors such as the economic environment and the prospects in your business sector (see also Looking Out The Rear Window on page 2), assess their impact and document how they may present opportunities to an acquirer.
4. Consider what you can do to enhance the value of your business (reducing customer concentration, clearing up regulatory issues, reducing verbal agreements to written contracts, etc.).
5. Consider all your liquidity options including selling to employees, selling to an ESOP, sale to another business, an asset sale, transfer to family, a staged exit through sale to a financial buyer etc.
6. Once you begin to consider the sale options you should also establish a relationship with an M&A attorney. They can help you with the legal aspects of getting ready and will be vital once you go to market. You need an experienced M&A specialist.

Valuation & Evaluation

But what is the business worth and

how do you find that out? Many business owners consult with accountants or talk to a valuation firm to get a feel for what their business might be worth. That can be valuable for estate, tax and divorce purposes but this doesn't necessarily advance the sale process. They will give you a Fair Market Value but this doesn't always correlate with the Real Market Value in an actual sale.

The best step is to consult with an experienced investment bank. They will have access to statistical data (see Magic Multiples on page 3) but will also be able to weigh your specific variable to give you a range of value. They should do this evaluation at no charge because it's part of their own evaluation process. If they want to charge you to determine if they want to represent you then they're more interested in this fee than in selling your business. Find someone else.

For example, Blackbridge can decide if we wish to propose to represent a business, we need to do our own analysis at our own cost. We need to fully understand the business's operations, the financial details (P&L and Balance Sheet), the competitive context, the customer network, the growth potential, reasons for sale, corporate structure, IP assets and many other factors. This process can take up to 60 days.

Only when we've completed this process, supplemented by some Q&A, can we present the owners with a useful indication of a value range for the business and what can be done to enhance it as well as possible deal structures and target buyers.

This report and value range is only for the seller's internal use in evaluating their options. We never go to market with an advertised price target because:

- This sets a ceiling price and all offers will come in below the advertised price.
- The value in buyers' hands can vary greatly from one buyer to the next depending on their needs, strategies, synergies, etc. Wait for buyers to make an offer and negotiate from there.

All of this is done confidentially and with no obligation between the parties. If the sellers and Blackbridge decide that we wish to work together then Blackbridge will submit a proposal.

Fees

Blackbridge aligns its interests with those of the seller. We do not charge open-ended monthly retainers, which can encourage delay. Blackbridge charges a fixed fee at engagement and charges no other fees until the sale is successfully completed and the seller is paid. If the sale never happens the fixed engagement fee is all for researching and preparing of documents and target lists and representing the seller.

Length of Time

We typically get to market within 60 days of engagement. Thereafter we are not in total control and a sale could take as little as 90 days or as long as 18 months or more.