



Abstract: Many qualities can make a company an attractive acquisition target. Successful companies are likely to attribute their marketability to such qualities as an established and growing customer base, recurring revenue sources and a seasoned, dynamic management team. Knowing how to emphasize and market these features can mean the difference between good offers and those that fall below owners' expectations.

What makes a company worth more?

Identifying key value drivers

Many qualities can make a company an attractive acquisition target. Key value drivers depend, of course, on the company, the industry and potential buyers. But successful companies are likely to attribute their marketability to such qualities as an established and growing customer base, recurring revenue sources and a seasoned, dynamic management team.

Whether you're interested in gauging your own company's financial strength or that of a company you're considering buying, it's important to understand these and other factors that indicate long-term strength and might justify a higher sale price.

Never discount customers

Companies are acquired for a variety of reasons, but far and away the greatest attraction is a desirable customer base. Most buyers understand that, while management team members come and go and equipment eventually wears out, the real value of most acquisition candidates lies with customers and their long-term loyalty. So the ability to increase market share or gain access to deep-pocketed customers draws many buyers to the negotiation table.

Prospective buyers often pore over customer data during the due diligence phase — focusing on buying habits and sales trends over the past several years. Of particular interest are:

- Customer size in terms of revenue,
- The number of new customers gained annually and their percentage of the total base,
- The number of customers who leave annually, and
- Reasons they cite for their departure.

Also of vital concern is the percentage of total sales concentrated in just a few customers. The smaller this number, the greater the acquisition risk, because losing one or two major customers could dramatically harm future profitability.

Recognize recurring revenue

Another, similar value driver is the character of a company's revenue or what percentage of it is recurring. Recurring revenues are those that can be reasonably depended on to occur in the future

based on past trends and existing relationships. Because of its reliability, this type of revenue has an inherently higher value than one-time revenues.

The Gillette Company provides a good example of this revenue model. Early on it realized that it could practically give away razors as long as it held on to the recurring revenue stream of its razor blades. The typical law firm, on the other hand, has only a small percentage of clients requiring recurring services and generally begins each year with few revenue source guarantees, making business development a huge annual priority for law firms.

Uncover value drivers

An old M&A joke claims the perfect acquisition is one in which you keep the clients and lose the employees. But those days are long gone; today, deals often close or collapse based on the buyer's ability to retain key players. While this may vary in importance according to the company or industry, given today's innovation-driven environment and the reality of global competition, people are no longer regarded as interchangeable parts. What makes a company an attractive acquisition candidate may well be a marketing guru, product developer or particularly effective chief technology officer.

Finally, while buyers sometimes overestimate the cost savings that can be achieved through synergies — or the elimination of duplicated positions and processes — this is still a crucial consideration of any acquisition.

Advice for buyers and sellers

For companies considering selling, knowing and emphasizing key value drivers can mean the difference between swift and attractive offers and those that fall below the owner's expectations. Similarly, buyers who perform extensive due diligence to accurately assess value drivers are less likely to overpay for an acquisition, or worse, end up buying a company that doesn't fulfill its promise.