



Evaluating opportunity for business valuations and transactions during COVID-19

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Webinar starts at 11 a.m. CT



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Presented by
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Cathy Mitchell

Vice President

Business Valuation Services

- ✓ Cathy specializes in valuation.
- ✓ Cathy primarily works with closely held and family-owned organizations.
- ✓ She has earned the Accreditation in Business Valuation (ABV) credential.



Todd Richardson

Vice President
Corporate Finance Services

- ✓ Todd leads AGH's M&A and corporate finance services team.
- ✓ He works with family-owned and closely held entrepreneurial businesses.
- ✓ Todd also provides buy-side advice to those who are actively acquiring businesses or seeking financing for organic growth.



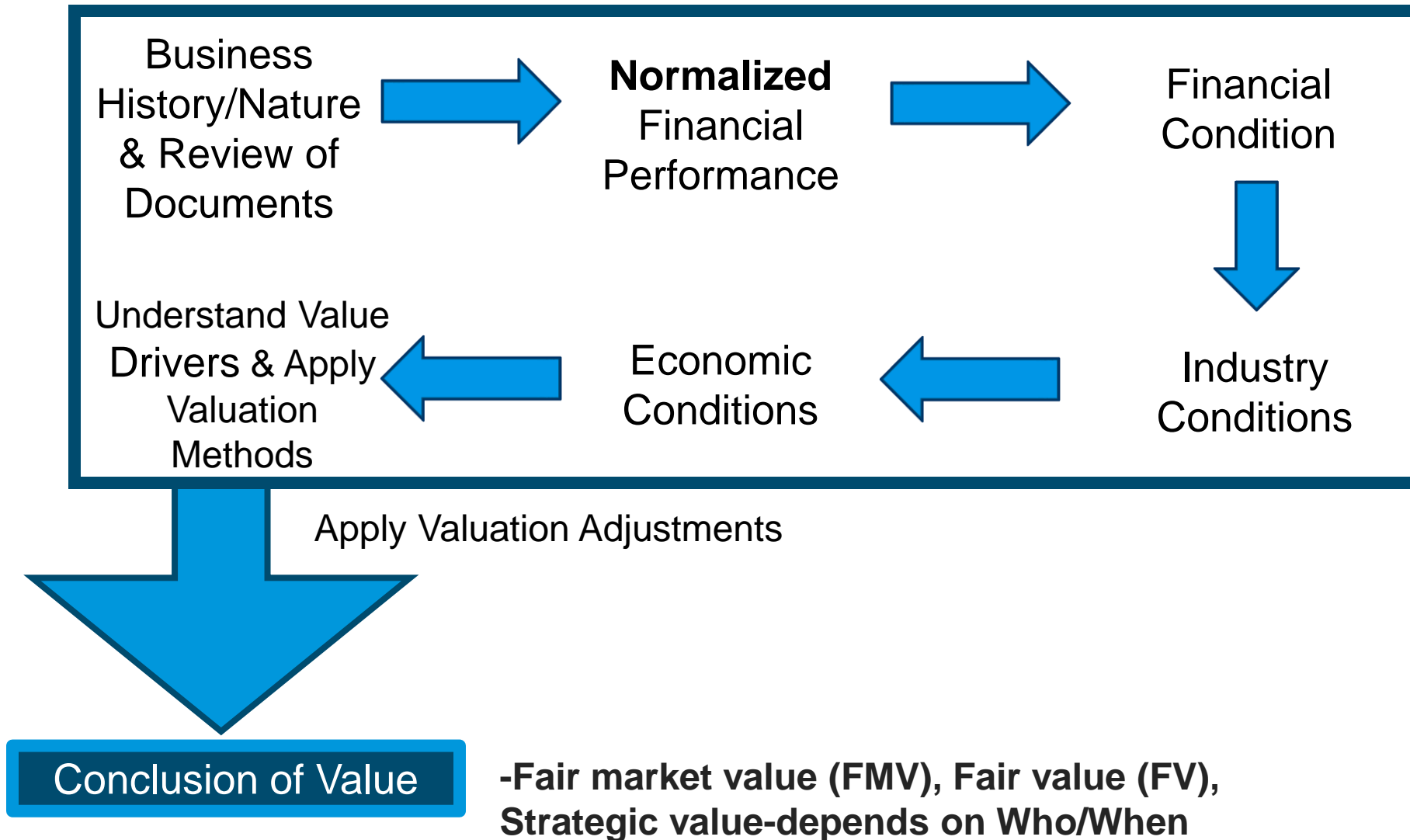
Today's objectives

Identify impact of COVID-19 on business valuations and an overview of how business valuations are performed

Understand how COVID-19 affects the business transaction market

Learn strategies to mitigate related challenges AND to exploit any opportunities

How is a business valuation done?



Review company documents

Business prenups or buy-sell agreements can be “ticking time bombs or reasonable resolutions”.

Elements of buy-sell agreements:

Define takes, puts or ROFRs

Address trigger events

Set price – formula, fixed prices, appraisal, discounts

Include terms for price payment & funding

Consider other permitted transfers

Satisfy business and legal requirements

POLLING QUESTION #1

Please answer for continuing education credit



Valuation is more than applying a multiple

Normalization adjustments put financials on a basis which reflects a company's true economic earning power.

Examples:

1. Remove extraordinary transactions
2. Adjust expenses to market level
3. Eliminate non-operating items
4. Consider ones related to COVID-19



“Managers and investors alike must understand that accounting numbers are the beginning, not the end, of business valuation.” – Warren Buffett

Value drivers

They increase growth of or reduce risk underlying **FUTURE** cash flow.

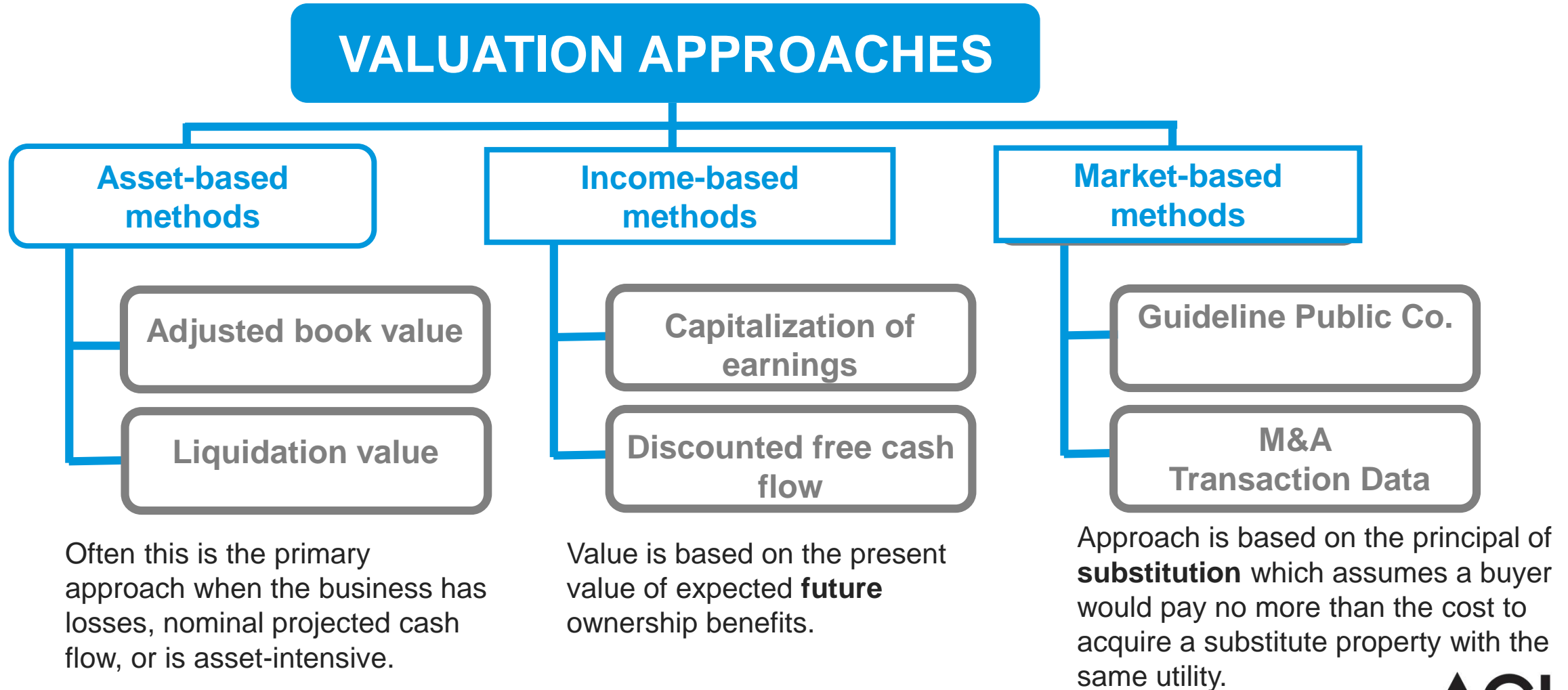
Key drivers:

- Sustainable **profits**
- Competent management **team**
- **Diversified** customers/vendors
- Realistic **growth** strategy
- **Transferable** contracts
- **Proprietary** product/service
- **Noncompete** agreements
- **Management succession plan**



“If past history was all there was to the game, the richest people would be librarians.” – Warren Buffett

Business valuation approaches



COVID-19 effect on valuation approaches

Asset approach

- Becomes paramount at least as a floor value

Income approach

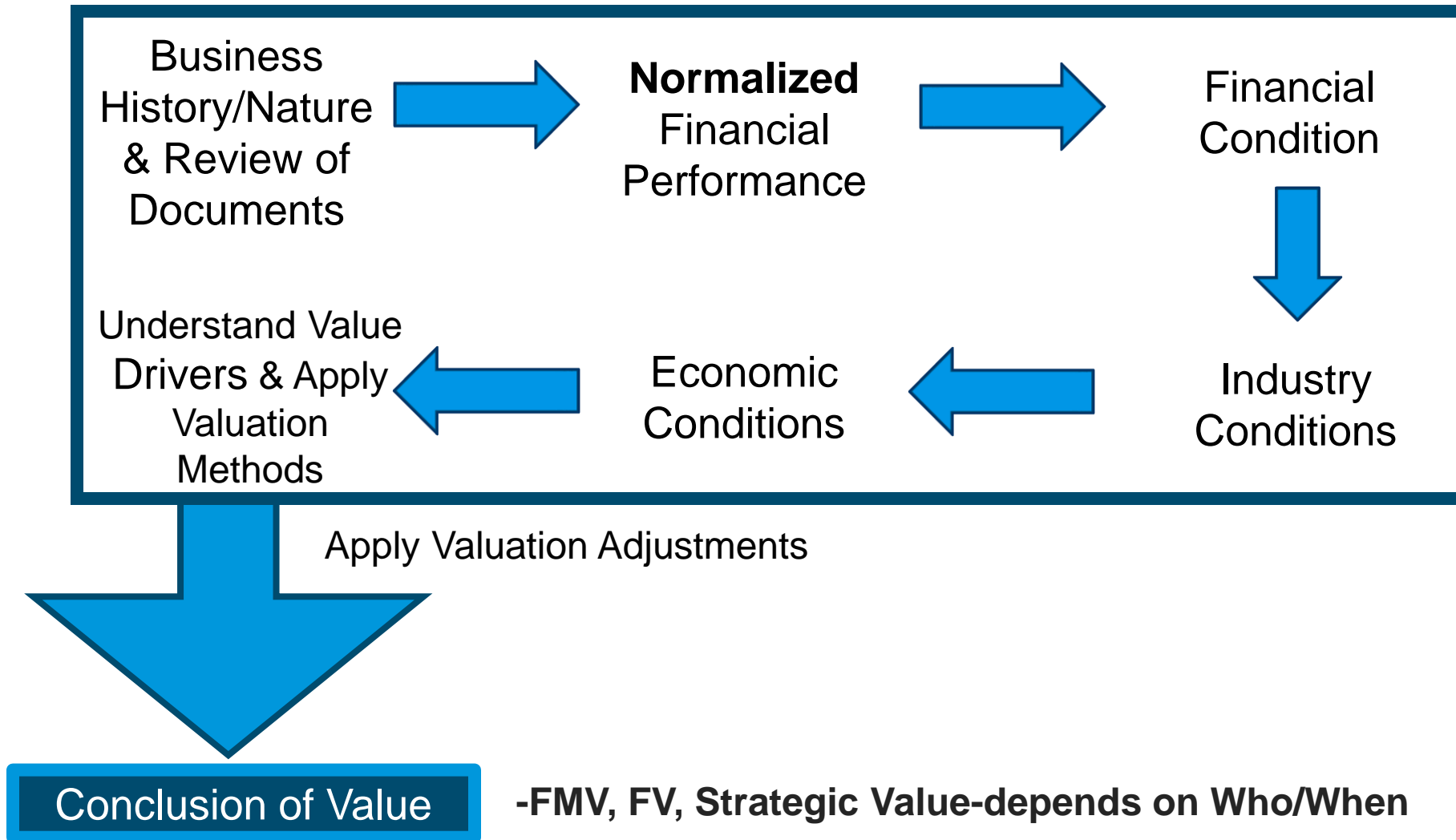
- Discounted normalized cash flow may be best methodology

Market approach

- Adjust market multiples downward generally, maybe higher for essential industries



How is a business valuation done?





When was COVID-19 known or knowable?

In valuing a company, only circumstances existing at the valuation date should be considered.

Late February/early March when the virus started to spread, and the stock market began to reflect the expected economic impact is generally considered the **known/knowable timeframe**.

Use any valuation with a valuation date pre-COVID-19 with caution.



POLLING QUESTION #2

Please answer for continuing education credit

COVID-19 effect on value

COVID-19 legislative benefits must be considered for business valuation purposes-

- PPP (Paycheck Protection Program)
- EIDL/EEIG (Economic Injury Disaster Loan/Emergency Economic Injury Grant)
- SBD RP (Small Business Debt Relief Program)
- Employee retention credits for payroll taxes
- Payroll tax deferrals
- Business income tax changes:
 - Net operating loss utilization
 - Excess loss limitations
 - Business interest limitation
 - Bonus depreciation on qualified improvement property



COVID-19 effect on value

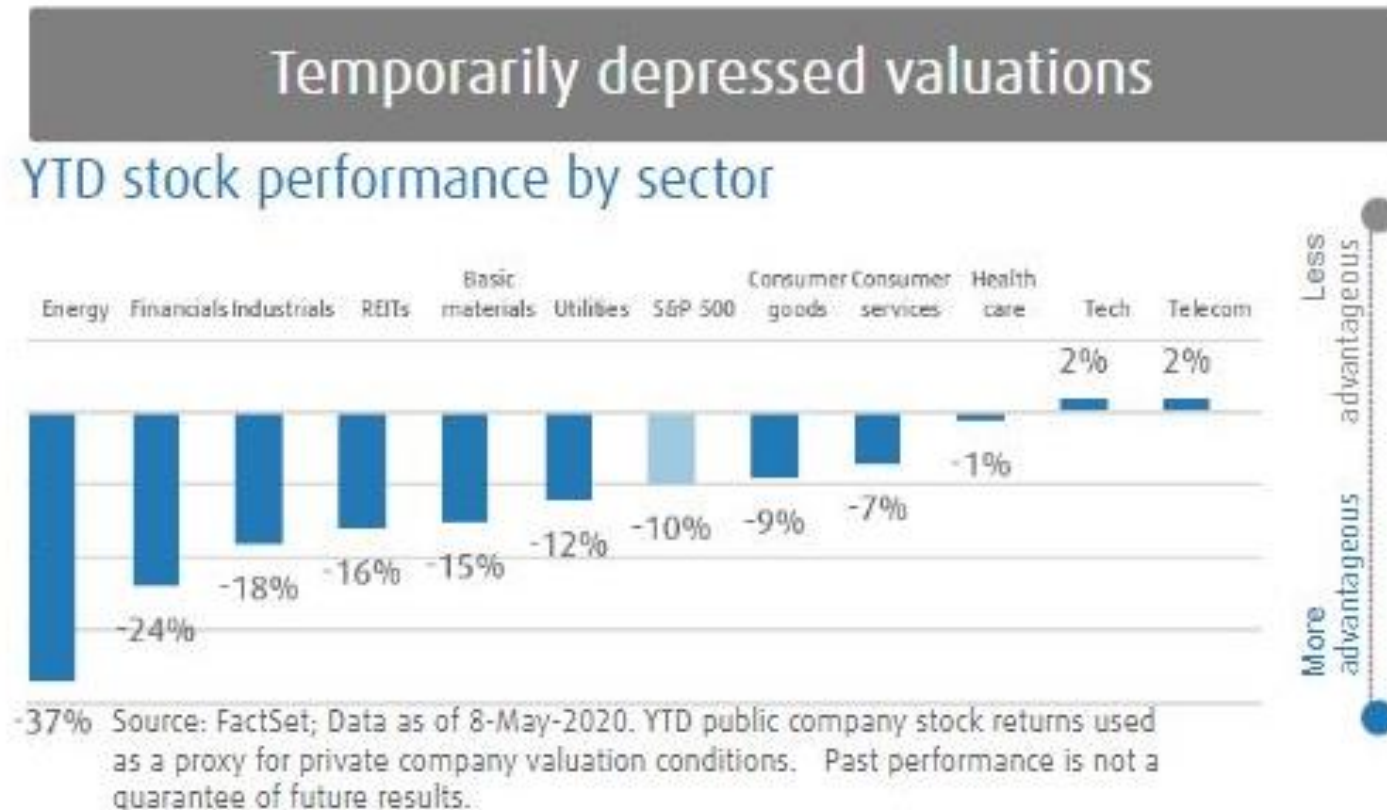
Valuation pundits estimate 10-20% decline in overall closely-held business value due to these factors which **reduce** value:

- Lower cash flow
- Higher risk (environmental/external and operational/internal)
- Lower expected growth





Valuation changes by industry during COVID



Source: BMO

COVID-19 considerations

Economic	Length of positive or negative changes to revenue and costs and diversification
Political/governmental	Restrictions on business; funding; upcoming elections; income taxes
Demographic	Composition of and wherewithal of customer base
Psychographic (social/cultural)	Changes in consumer preferences
Legal/regulatory	Impact of restrictions on sales and capacity
Technological	Adaptations made using technology
Industry	Evaluate the elasticity of demand for the product/service and growth
Competitive	Consolidation and/or closings
Environmental	Nothing new COVID-related
International	Required travel may entail delays/additional costs

POLLING QUESTION #3

Please answer for continuing education credit

Effect of COVID on transaction market

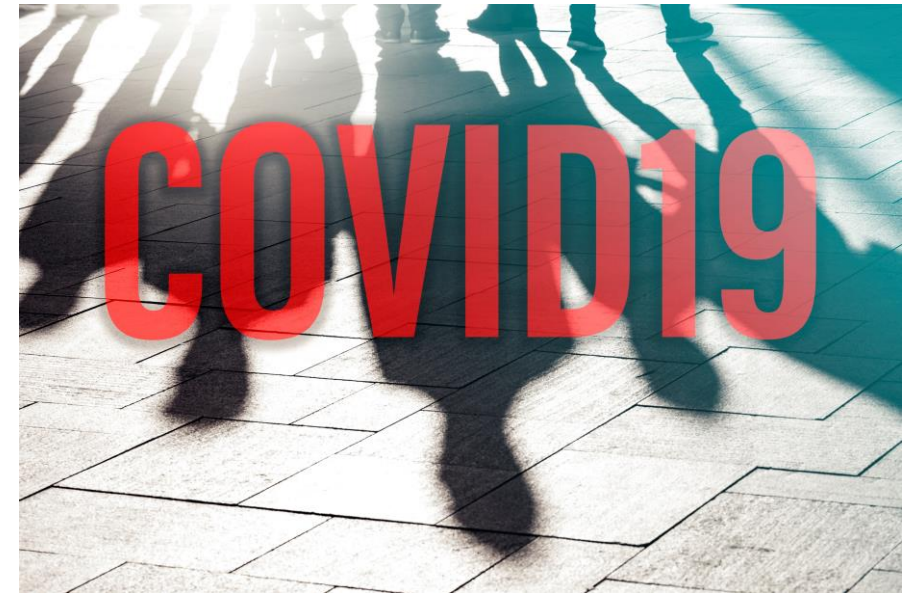
Huge discounts may be ascribed to businesses that are not recession or pandemic resistant or essential businesses

~80% of business owners' net worth in business

Worst case – health issues, “have to sell soon”

Best case – “cash rich”, look for distressed businesses

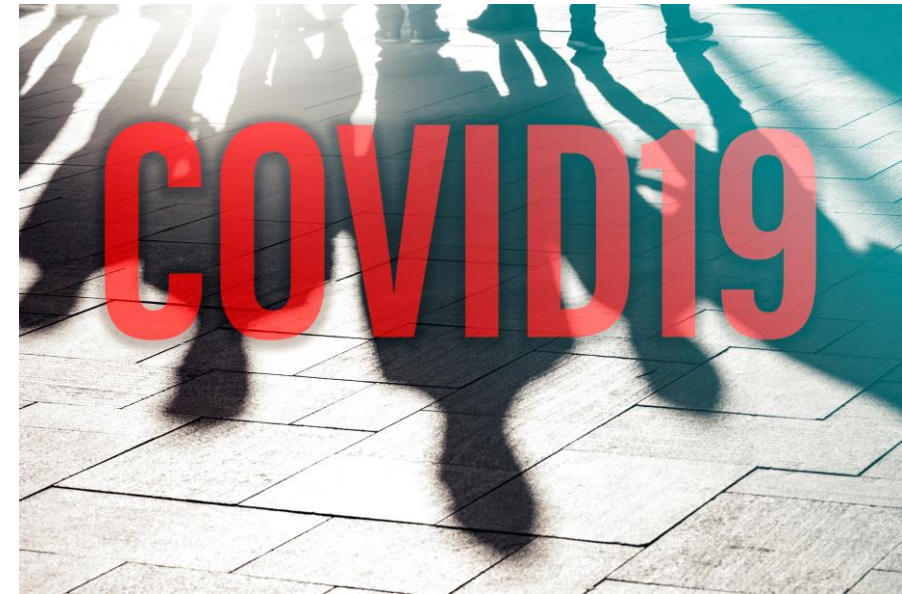
- Availability of financing and associated loan covenants may impact ability to close.



Effect of COVID on transaction market

Deal metrics impacted by COVID-19

- % of cash at closing
- Purchase price adjustments
 - Effect on targeted working capital calculation
 - Caps and limitations on price adjustments
- Earnouts
 - How much is seller willing to risk?
 - Will business return to normal as projected?
 - Is there a second wave coming in the fall?



Legal

- Expanded material adverse effect clauses
- Customer and supplier relationship representations / contract termination language

Win-Win Strategy – partial sale



Mitigate challenges related to COVID-19

Rewrite/amend value sections of buy-sell agreements to address times such as these

Contingency / backup plans

- IT systems including remote capabilities
- Supply chain interruption

Supplier concentration as important as customer concentration



Mitigate challenges related to COVID-19

- Management team – is there an opportunity to upgrade?
- Exercise CAPEX investment discipline
- Worker safety
- Employee mix – full and part-time
- Insurance policy check-up



Exploit opportunities presented by COVID-19

Huge premiums may be ascribed to recession- or pandemic-resistant or essential businesses

2020 gift/estate tax lifetime exemption amount of \$11.58M will drop back to \$5M on 1/1/26 or sooner dependent on upcoming presidential election

Transferring closely-held stock at depressed valuations may minimize these gift/estate taxes and help preserve legacy

Choice of valuation date



POLLING QUESTION #4

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Useful resources

AGHUniversity.com

Business transition on-demand section

AGHLC.com/Succession

Succession plan readiness assessment

AGHOneShot.com

Succession planning mistakes blog





Thank you for attending

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