

## Special Edition

### MERGERS & ACQUISITIONS – Part 2

#### Last week, I discussed the beginning of the process to “let go”:

- I indicated there are 2 components to any decision making process when you want to sell your business.
- The 1<sup>st</sup> process is--you need to be mentally prepared. I discussed the issues that face each and every potential Seller.
- The 2<sup>nd</sup> component is--your business has to be realistically priced. I stated that in most instances, pricing won't reach your threshold and the reason; it's very difficult to quantify the devotion, time, and stress that you've gone through, for a number of years, to get your company ready for this day.

#### This week, I want to focus on:

- How to price a trucking business?
- How to take a challenge and turn it into a positive situation?
- How to drive a business to create more value?

#### The 1<sup>st</sup> thing you have to understand is that the economy is in turmoil.

Therefore, many Sellers believe that now is not the time to sell and that's the furthest thing from the truth.

#### I've stated, on numerous occasions:

- If you have something to sell.
- You have a good business model.
- Your company has been historically profitable, and;
- You have a good management team, there is always a way to create value, if you're willing to assume a certain amount of risk.

#### Let me define risk; the possibility of suffering financial harm.

#### Any time you sell a trucking business, there is a certain risk involved if you want to maximize value.

#### For example; there are Sellers that believe;

- They are entitled to receive value for their company, if a Buyer can eliminate operating expenses when their business is acquired.
- There are Seller's that believe they should be paid, based upon a Buyer's ability to finance equipment and receivables at a lower rate;
- There are some Seller's that believe they should be compensated based upon projected growth in the future.

However; there are creative ways to structure an “earn out”, over time, in which you can receive a higher rate of return if you chose to assume some risk. I call this “put your money where your mouth is”.

MERGERS • ACQUISITIONS • DIVESTITURES • OPERATIONAL REVIEWS • MANAGEMENT CONSULTING

# THE AHERN ADVISORY

## in this issue

Mergers & Acquisitions –  
Part 2



Ahern & Associates, Ltd.

Accredited Member  
National Bureau of Certified  
Consultants Inc.

September 1, 2009

**To review; let's start with "the process"; the first thing that any Seller has to do is agree to a range of values based upon current market conditions:**

- This should be done, by a professional firm that has extensive experience in transportation.
- It should be done by an organization that understands that private transportation companies do not sell at the same pricing variables as publicly traded companies.

**In other words, you need to find a firm that has extensive experience in trucking transactions, so that you have a realistic idea of what you can anticipate receiving for the sale of your business.** As part of this process, you have to decide whether;

- You want to stay, or;
- You want to leave.

**The reason; if you're willing to stay and your company is being purchased by a strategic Buyer, you may be able to create more value; if you want to leave, (shortly after the sale), the value is what the value is at that particular time.**

**If you're an asset based company, there are specific challenges that you need to deal with. If you are a non asset based business, there are other challenges you must deal with.** However, the bottom line, there are values and formulas that are industry specific. These are the values that I work with daily, dealing with various clients.

**It's important to understand that;**

- I don't drive the market.
- The market drives itself, and;
- The market is a byproduct of specific needs.

**Is it a good time to sell? Yes! If you have something to sell;**

- The industry lacks freight.
- **There is a tremendous shortage of freight and larger trucking companies want growth now!**
- Larger carriers, have the financial wherewithal to "weather the storm".
- For smaller carriers, if you want to protect your retirement, you should consider selling.

**If you question whether you should wait until the market rebounds?** The answer is;

- **If you're waiting for the market to rebound to the 2006-2007 level, that's not going to happen!**
- Our industry, will see a "resurgence" in freight, sometime in the next 24 months, and;
- Trucking will return to economic profit, but;
- **Sellers will not witness pricing formulas as they were in 2006-2007 – that was a very unique period, in transportation history.**

**Historically, private trucking and smaller logistics companies never sold for multiples of EBITDA (earnings before interest, taxes, depreciation and amortization);**

- **Historically, whether you were asset based or non asset based trucking or logistics business, unless you were a firm with very strong earnings, and/or a specific market niche, EBITDA was a taboo word.**
- In 2006-2007, Private Equity investors went crazy. They had free money.
- **Profitable mid-size trucking companies were receiving 5 – 6 times EBITDA.**
- **Large transportation companies were receiving up to 9 times EBITDA;**

**The major reason; trucking companies weren't buying trucking companies, and logistics companies weren't buying logistics companies.**

- **Private equity companies aggressively entered the transportation sector and felt that trucking was an undervalued industry and it was much cheaper, than the other industries they were previously involved with.**
- **Therefore, 5 – 6 times EBITDA was a very cheap entrance fee, in a space that they believed controlled 80% - 85% of specific market space.**

**Were they right? Obviously not!**

**With that stated; what can you expect to receive and how can a sale (structure) take place; if you want to sell your business? First, you must recognize;**

- **60% - 70% of all transportation sales** are asset sales. Therefore;
- **Don't try and demand a stock sale** or you will lose 70% of the market.
- There are ways to structure a deal to lessen the tax consequences, and;
- **Stock sales don't** eliminate exposure.
- **There is normally a "basket deductible" in a stock sale, that still holds a seller liable for claims over and above a specific dollar amount for a specific period of time, and;**
- **Buyers want to take depreciated assets and re-cast them on their balance sheet at fair market value.** In other Buyers words, don't want to buy depreciated assets without creating value.
- There are still ways to structure a deal and lessen the tax consequence, to a Seller, at the time a sale takes place.

**If you own equipment, most buyers will pay;**

- Orderly liquidation, or;
- Trade in value.

**Too many times, Seller's over inflating the value of their equipment and the deal falls apart.** If a tractor or trailer vendor advises you, your equipment is worth "x"; **when you receive an evaluation from your dealer, the first thing you need to ask is;**

- If I sell my company, and;
- The Buyer will not buy my equipment;
- **Will you write me a check for the value you have placed on my equipment?**

**If the answer is no; then ask what dollar amount they will pay you to purchase your equipment?**

**In other words, the market is driven by whatever the market is willing to pay at any given time.** Equipment values are in the "toilet";

- Equipment values continue to decline.
- **Therefore, if you're an asset based company, how do you sell your business if your trucks don't have the value that you need? You become creative.**
- **If you're "upside down", on some equipment, there are certain ways to structure a sale, so that you can become a fleet owner, receive a percentage of the revenue to continue to operate your trucks, until equity is "built up", and;**
- **Then, you can sell and be the recipient of the net equity.**

**In reference to an asset sale;**

- **Cash and receivables are the Sellers, to keep at the time of closing.**
- **Any pre-paid deposits** that can be utilized by a Buyer will be paid as earned.
- **Furniture and fixtures** have very little value.
- **Terminal properties, in most instances, will not be purchased** – they may be leased, but this is something that needs to be discussed with a buyer, at the beginning of the process, and;
- **The "Goodwill" of a selling company, (sweat equity, customer base); is predicated on 2 things;**
  1. The selling company's overall profitability, and;
  2. Seller customer's tenure and rates.

**If a company earns 2% pretax income and, historically has had less than 5% earnings, a Seller can expect to receive 2% of revenue for a 2- year, as the “Goodwill”, plus assets less debt:**

- **If you’re a \$20MM carrier, that equates to \$800,000, plus assets less debt.**
- **If you’re a \$10MM company, that equates to \$400,000, plus assets less debt.**

**On the other hand, if you’re a very profitable, larger carrier and have substantial add backs, you may receive:**

- **1 ½ - 2 times average earnings or 3 – 4 times EBITDA:**
- **Average earnings would be defined as the previous 3 years, plus projected earnings for the 2009 year.**
- **If 2009 year revenue and earnings are down, those will that impact the overall purchase price of the customer value?**
- **Can you structure a deal in such a way that you can receive an earn out, based upon increase profitability and revenue? – Yes!**
- **The magical question is; what will you receive at closing?**
- **You will receive all of your asset value as outlined above.**
- **The trade in, or orderly liquidation of tractors and trailers.**
- **You will be required to pay any and all trade payables, and:**
- **You will receive 30% - 40% of the estimated “Goodwill” up front, with the balance to be structured over a 2 – 3 year period.**
- **Will you receive all of your “Goodwill” up front? – No!**

**The reason; customer longevity is dwindling and revenue can be terminated by a Shipper at any time.**

**On the other hand, in some instances, you can negotiate a deal where you can receive a fixed payment, over time, assuming that the revenue for the first 12 months maintains at least 80% of its normal level.** If that type of structure doesn't meet with your approval, then don't sell your business.

**If you believe that you should wait 2 or 3 years for the market to improve** to receive a higher rate return, it will not. The only way that will occur is if you can sell to a private equity firm, and they are, for all practical purposes, out of transportation.

**Next week, I will discuss how to value a non-asset based business and the challenges that must be overcome to receive the highest rate of return and how to create more value.**

QUOTE OF THE WEEK: **“The trouble with facts is that there are so many of them”.**