



The Six Myths of Valuing and Transacting Family-owned Businesses

By

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Agenda

- Determinants of firm value
- Myth 1: Firms in my industry always sell for a multiple of revenue.
- Myth 2: Public firm transaction multiples are larger than private firm transaction multiples.
- Myth 3: Acquirer's of private firms over pay
- Myth 4: Most transactions are within the same industry.
- Myth 5: Foreign buyers play no role in the market for private firms.
- Myth 6: Tax status has no impact on firm value.

Drivers of Firm Value

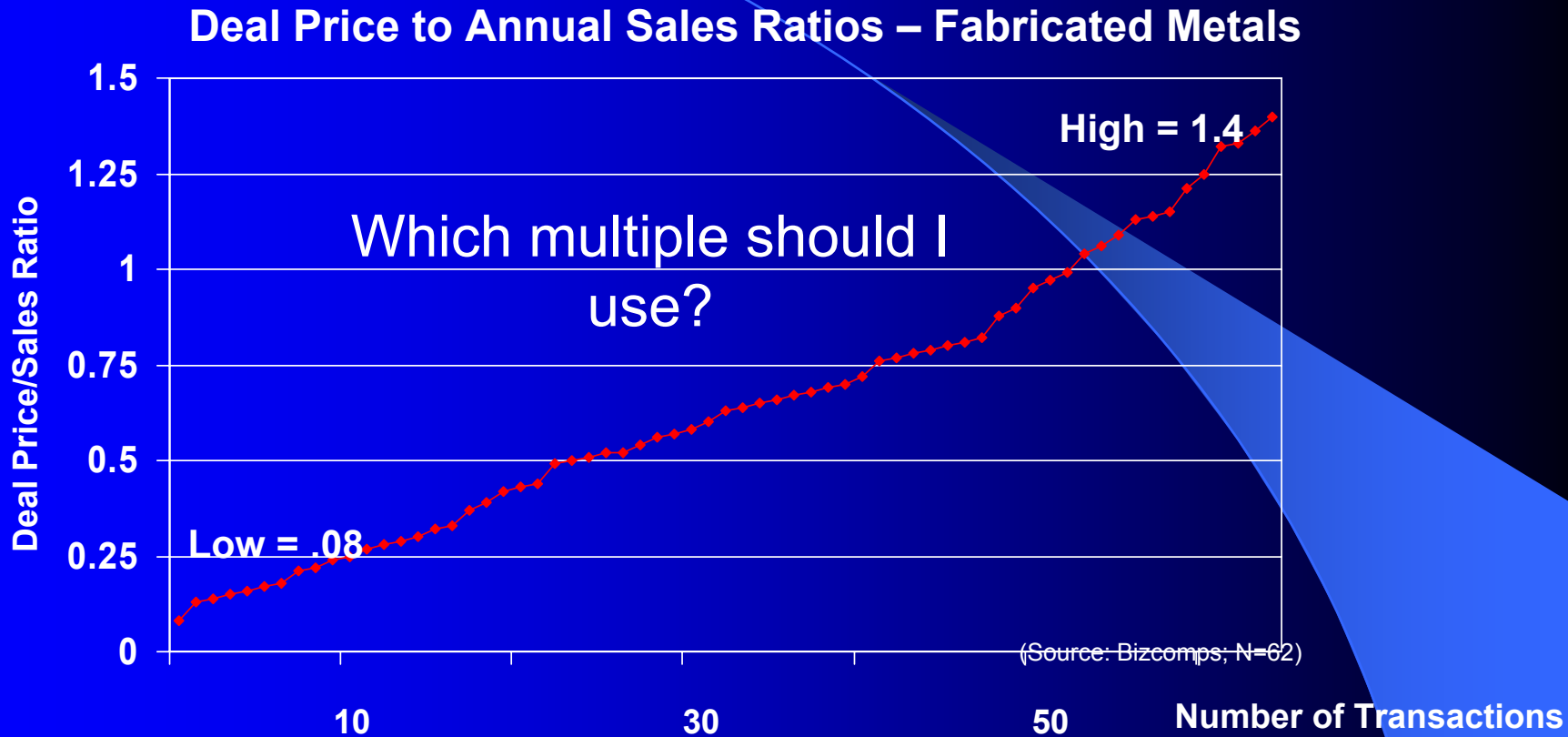
- Size of cash flow
- Growth in cash flow
- Cost of Capital

Deal Price to Annual Sales Multiples: Using a 20% Required Rate of Return

<i>Compound Annual Growth Rates -CAGR</i>	<i>After-tax Profit Margin</i>			
<i>Expected Future Earnings Growth</i>	20%	30%	40%	50%
0% CAGR	1	1.5	2	2.5
5% CAGR	1.4	2.1	2.8	3.5
10% CAGR	2.2	3.3	4.4	5.5

Myth 1: Firms in my industry always sell for a multiple of revenue

Business Values Vary Widely Within Industries

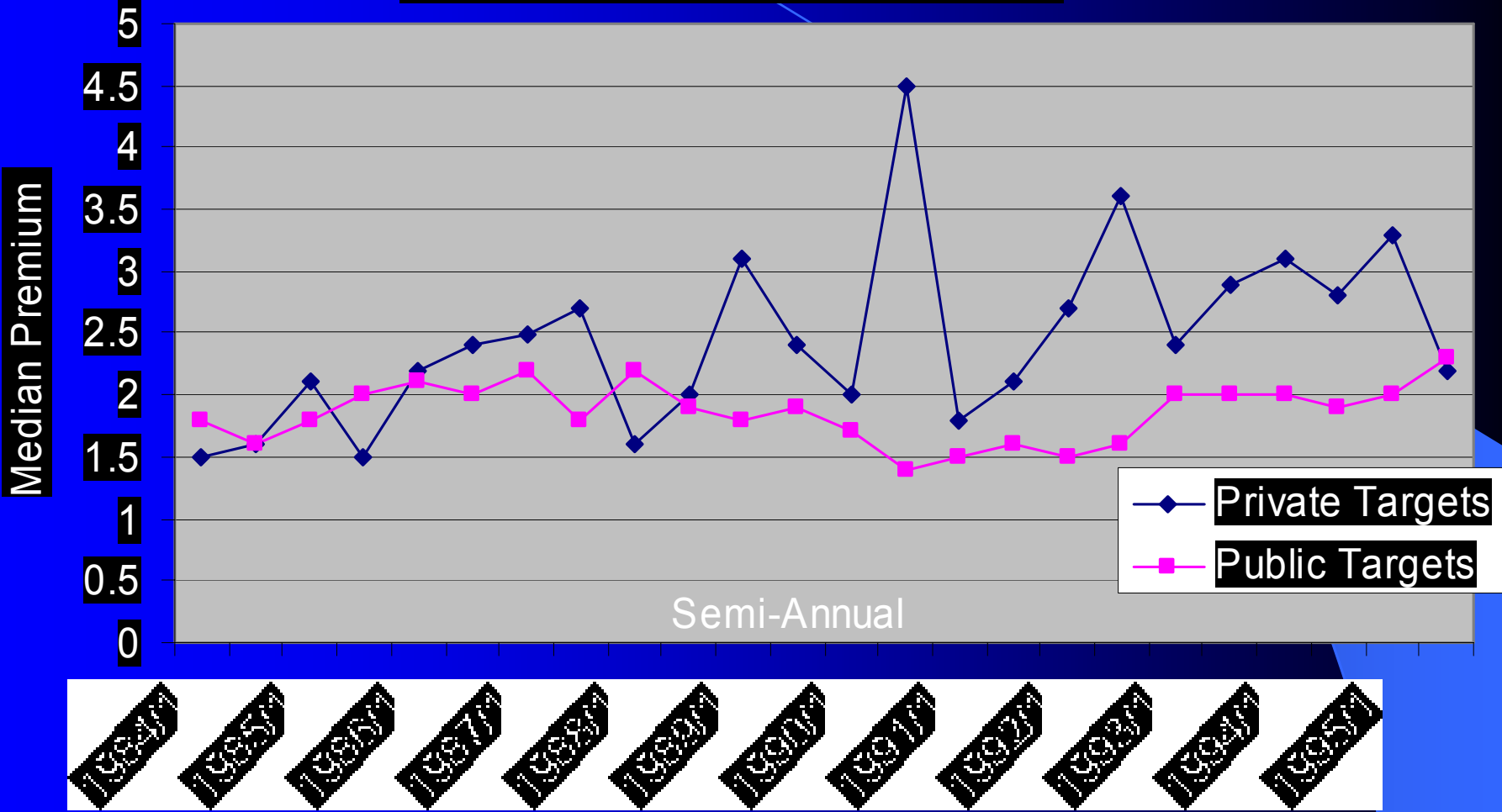


Example – Metal Fabricator with \$5M Annual Sales
Value could range from \$0.4 million to \$7 million

Myth 2

Public firm transaction multiples are larger than private firm transaction multiples

Private and Public Target Premiums



Private vs. Public Targets

	Private Target			Public Target		
	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>
Premium	2.3	2.2	4	2	1.9	1.85
Enterprise Value	35.62	49.89	47.1	26.05	71.45	69.99
Enterprise Value / EBITDA	3.14	21.12	12.19	2.1	16.15	9.38
Enterprise Value / Earnings	(16.2%)	(31.1%)	(16%)	9.5%	0%	0%

Myth 3: Acquirer's of private firms over pay

Private vs. Public Target

	Private Target			Public Target		
	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>
	2.3	2.2	4	2	1.9	1.85
	35.62	49.89	47.1	26.05	71.45	69.99
	3.14	21.12	12.19	2.1	16.15	9.38
Overpayment for Target	(16.2%)	(31.1%)	(16%)	9.5%	0%	0%

Private firm acquisition premiums are not high enough! Why?

- Over 30% of the time selling owners join the acquiring firm. Thus not all of the return is captured in the reported premium.
- Selling owners do not fully appreciate the value their firms create for the acquirer.
 - Strategic value
 - Fair market value

Myth 4: Most transactions are within the same industry

Private vs. Public Targets

	Private Target			Public Target		
	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>
	3.3	2.2	4	2	1.9	1.85
% Cross Industry	35.62	49.89	47.1	26.05	71.45	69.99
	3.14	21.12	12.19	2.1	16.15	9.38
	(16.2%)	(31.1%)	(16%)	9.5%	0%	0%

Axiom Valuation Solutions

Myth 5: Foreign buyers play no role in the market for private firms

Private vs. Public Targets

	Private Target			Public Target		
	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>	<u>Stock</u>	<u>Cash</u>	<u>Mixed</u>
	2.3	2.2	4	2	1.9	1.85
	35.62	49.89	47.1	26.05	71.45	69.99
% Foreign Acquirers	3.14	21.12	12.19	2.1	16.15	9.38
	(16.2%)	(31.1%)	(16%)	9.5%	0%	0%

Myth 6: Tax status has no impact on firm value

Tax status makes a difference

Comparison of purchase price multiples across target firm organizational form for 77 matched pairs of S corporation and C corporation acquisitions announced during 1994-2000									
<i>Panel A: Price to Book Multiple</i>					<i>Panel B: Price to Revenues Multiple</i>				
	S Targets	C Targets	Diff	Matched Pair Diff		S Targets	C Targets	Diff	Matched Pair Diff
Mean	7.54	4.83	2.71*	2.45*	Mean	1.29	1.01	0.28*	0.32*
Median	5.19	3.08	2.11*	1.77*	Median	0.95	0.83	0.12*	0.26*
% positive				65.6%*	% positive				63.4%*

Summary

1. Owners of private firms appear to leave money on the table even though private firms sell for higher multiples than their public counterparts; that is private firm multiples should be even greater than reported.
2. There is no such thing as “the transaction multiple: businesses in the same industry sell for vastly different multiples.

Summary

3. Tax status impacts value: S corporations are worth more than equivalent C corporations.
4. Foreign buyers play a major role in the private firm marketplace.
5. Cross industry acquisitions are common in the private market.