

Acronis Global Cyber Summit 2019

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CHEVAL M&A, INC
Internet Services M&A

What you should know about buying or selling a business

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Acronis Global
Cyber Summit 2019



CHEVAL M&A, INC
Internet Services M&A

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Agenda

1. Why/when you should buy or sell
2. What makes a good buyer/seller
3. Valuation & things that help/hurt value
4. Don't shoot yourself in the foot
5. Q & A

Who is Cheval M&A

- Investment bankers active in hosting/cloud and related Internet services space
- **500+ Internet services** type transactions since 1996
- **Deluxe, Rackspace, Web.com, Verio**, among many others of all sizes
- Represent buyers & sellers
- Distributes a weekly listing of small and mid sized sellers to several hundred prospective buyers

When should you buy or sell

Selling

- Are you enjoying your business?
- How do you see growth/cash flow going forward?
- Be aware of your opportunity cost.
- Is it time to take money off the table?

Buying

- How much does organic growth cost?
- Do you have excess cash flow?
- Do you have capability to integrate & benefit from scale?

What makes a great buyer

- They have the money
- They've done it before
- They are a good business fit
- Price makes sense
- Good transaction partner
- Good operating company

What makes a great seller

- Well defined business (that fits buyer's target)
- Good numbers
- Understandable risks & commitments
- Predictable customer growth & stability
- Good transaction partner

Valuation & purchase price

- Only three ways to value;
 - Based on future cash flows
 - Price that someone will pay for it
 - Cost to build it (aka replacement cost)
- Purchase price vs terms
- Stock vs Assets

Purchase price calculation

- **Value** of business/operations
 - Customers, equipment, domains, software, servers, and all related assets
- **Less:** Assumed liabilities, if any
 - Including excess contractual commitments
- **Plus:** Other assets, if any
 - Does not include assets used in operations
- = Purchase price

Things that help/hurt value

Perception of risk

- Surprises
- Quality of financial or business records
- Customer stability
- Predictable/unpredictable growth or decline rates
- Understanding of customers

Things that help/hurt value

Market conditions

- Number of buyers & sellers
- Cost and ease of organic growth
- Location
- Price of other potential transactions

Things that help/hurt value

Hidden assets or liabilities

Assets

- Non-CF assets (e.g. lightly used pre ARIN /15's)
- Products the buyer can cross-sell to their customers
- IP or products/services that can be spun off into a new business

Liabilities

- Old equipment / future capital expenditure needs
- Operational details that raise migration costs
- LT facilities leases

Things that help/hurt value

Operating efficiency / focus

M&A runs on marginal Cash Flow to buyer

- Most times, buyer CF % is greater than Seller CF %
- Consolidatable products can be worth more

Does buyer value only part of your business?

- Can be a huge issue in your business
- Example: Strategics vs Consolidators

Things that help/hurt value

How to fix issues

- Adverse market conditions?
- Buyer's business focus is different?
- Perception of risk?
- Spread between buyer and seller valuations?
- Hidden assets/liabilities?

How to optimize valuation

- Add recurring, compatible managed services
- Improve operating cash flow with automation, infrastructure changes, etc.
- Own your customers
- Understand who your customers are
- Improve quality of accounting
- Clean-up potential issues

Who you need to help you buy or sell

- Accounting (internal or external)
- Tax
- Legal with transaction experience
- Transaction / Banking help

Lastly – Please don't shoot yourself in the foot

- Disclose the issues up front
- Don't screw up your business by changing how you operate
- Don't take your eye off the ball
- Be nice
- Be responsive

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Alternatives to selling

- Employee buy-out
- Maximize cash to you
 - Earthlink
- Hire/promote a manager

What is the process

- Pre letter of intent
 - Teaser
 - Mutual confidentiality agreement
 - High level information
- Post letter of intent
 - Due diligence
 - Purchase agreement & schedules (APA / SPA)
- Closing

Due Diligence Example

Confirming Revenue

Revenue from
financials

Billing system
revenue

Merchant account
statement incoming

Bank statement
deposits



The numbers

	Operating Cash Flow				
	Ann Rev	Example A		Example B	
		Seller	Buyer	Seller	Buyer
Shared business	\$ 1,000	\$ 300	\$ 400	\$ 150	\$ 400
Design business	\$ 400	\$ 60	\$ -	\$ 20	\$ -
Total revenue	\$ 1,400				
Perceived Buyer Risk (e.g. Attrition)		\$ -	\$ (40)	\$ -	\$ (40)
Net Cash Flow		\$ 360	\$ 360	\$ 170	\$ 360

	Purchase Price as a Multiple of Op Cash Flow				
Purchase price	\$ 1,400	3.9x	3.9x	8.2x	3.9x

Price at a rate of return equal to;		
20%	\$ 1,800	\$ 850
25%	\$ 1,440	\$ 680
30%	\$ 1,200	\$ 566

* No taxes, capital expenditures or other transaction costs