M&A Corner

Dealmaking tips specific to L&NW's readership

EBITDA…what's all the fuss?

By **Jim Anderson**

So, you were attending Label Expo in Chicago last month and during dinner at Morton's with a group of fellow label company owners on Wednesday nite (Tuesday nite you watched the "Great Debate" in your room) the conversation turned to "EBITDA". While you had heard the term many times, you certainly knew you were not fluent enough on the topic to contribute much (if anything) to the conversation. One guy in your party who seemed to "know-it-all", had sold his label company (for a "ton of money" per him) to one of the many private equity (PE) firms that have been consolidating the industry. He then mentioned something about the multiple of "adjusted EBITDA" he received as his consideration for the sale and by now you were now totally lost! BTW-hopefully he picked up the tab!

Let's see if this edition of "M&A Corner" column can possibly shed some light on this somewhat complex topic, albeit one that we deal with it every day in our boutique Merger & Acquistion practice…

EBITDA stands for **E**arnings **B**efore **I**nterest, **T**axes, **D**epreciation & **A**mortization

Share Price on	Times # of Shares	Equals Market Cap	Plus Debt (MRQ)	Minus Cash (MRQ)	Equals TEV	Divided by TTM EBITDA	Equals TEV Multiple

The above chart illustrates how every public company arrives at the multiple of EBITDA at which it trades…but your company is not public, so how do you get to yours?

For those of you familiar with CDA's PrintStockWatch®, you have seen the EBITDA trading multiples of the 15 publicly-traded companies in the "printing" industry. If not, you can see the most recent chart at: **www.printstockwatch.com**

Note: PrintStockWatch® is a registered trademark of Corporate Development Associates

INCOME STATEMENT	FY2023
Total Net Revenue	10,000,000
Cost of Goods Sold	
Raw Materials	
Sub-total Raw Materials	4,068,000
% to Total COGS	54.7%
Labor, Emp. Taxes & Benefits	
Sub-total Labor *et. al.*	2,232,000
% to Total COGS	30.0%
Plant Overhead (Inc. Dep.)	
Sub-total Plant Overhead	765,500
% to Total COGS	10.3%
Freight and Delivery	375,000
% to Total COGS	5.0%
Total Cost of Goods Sold	7,440,500
Gross Profit Margin $	2,559,500
Gross Profit Margin %	25.6%
S, G & A Expenses	
Selling Expenses	385,000
General & Admin. Expenses	
Owners' Salary	500,000
Misc. G&A Expenses	816,500
Sub-Total G & A Expenses	1,316,500
Total S, G & A Expenses	1,701,500
Net Operating Income	858,000
Other Income (Expense)	
Federal Income Tax	(23,000)
Misc. Other Income (Expense)	33,400
Total Other Income (Expense)	10,400
Net Income $	868,400

NET EARNINGS (LOSS):

Let's begin with your Income Statement…hopefully this has been prepared for your company by your outside CPA annually from your Internal reports as either a Compilation (Good), Review (Better) or Audit (Best). We dedicated an entire "M&A Corner" column to this topic in an earlier L&NW publication…email me at janderson@printmergers.com if you would like a copy. Different internal financial software programs (ie: LabelTraxx) and certainly different CPA firms report Operating

Income differently, so we will use after-tax *Net* Earnings as our starting point. If you are an "S-corp" this would not include any Federal Income Taxes, but could include some State or other Misc. "Taxes".

"Adjusted" EBITDA Calculation	FY2023
Net Income	868,400
Add back Income Tax	23,000
Add back Depreciation	197,000
Deduct Misc. Other Income	(33,400)
Add-back Excess Owner's Comp	350,000
*Add-back Owner's Perqs	95,000
"Adjusted" EBITDA $	1,500,000
"Adjusted" EBITDA %	15.0%

The "beauty" of arriving at an EBITDA number is that it brings all companies back to the same starting point. Again, this is going to get you to a valuation without any regard to Debt. Just as with selling your home (which is the most common experience of a "sale" people have), we are going to value your business based on a multiple of "adjusted" EBITDA without regard to Debt. Similar to your home mortgage (or HELOC), that amount will be deducted from your Total Consideration to arrive at your "net" proceeds.

In the above sample Income Statement, we begin with Net (after Tax) Income. If your company is an "S-corp" (and I certainly hope so!), this will not be relevant to you.

We then "add-back" Federal **T**axes, **I**nterest and **D**epreciation/**A**mortization which may be itemized on your financials. Your CPA has hopefully included Depreciation as a component of Cost of Goods Sold (COGS), so you may have to look at the Cash Flow portion of the CPA report to find that exact amount.

Now you have completed the "easy" part!

What is next are the "adjustments"…or "add-backs" as they are commonly called.

I always tell our Seller Clients this: *"If I purchased your company on a Friday, what discretionary Expenses can I expect to "go away" on Monday."*

Let's say you are the sole shareholder of your company and drawing $500,000 per year in Salary. If you sell the business and do not want to remain with the new owner (or they do not want you to), do you think they will need to spend "$500,000" per year to replace you? Probably not (sorry)…they will most likely need a General Manager who will probably be paid in the range of $150,000 per year. Hence, we can "add-back" $350,000 of your Salary along with the proportionate taxes, etc. This is called "Excess Owner's Compensation"…

You have a condo in Naples, FL (half the printing world has second homes there) that you have called a "Branch Sales Office" and written-off substantial Country Club and HOA dues expenses…these are legitimate "add-backs". Last year this ran about $17,000…

You have had four (4) box seats to your hometown professional baseball team for years…cost ~$50,000 annually.

You write-off not only your Mercedes lease, but your wife's…total ~$28,000.

I think you get the idea!

The sum total of **all** of these expenses is called "Owner's Perqs"…business brokers will call it an "Owner's Benefit" and probably want to include 100% of your Salary which implies that your do nothing. I usually do not agree with that…business owners don't do "nothing" or they would sleep better at nite.

At the end of the day, when you add-up all of these discretionary Expenses, you will arrive at an amount called "adjusted" EBITDA. It is a multiple of this number that will lead to your Total Consideration from which you will need to subtract your Debt to arrive at your net proceeds.

Typical multiples of "adjusted" EBITDA in the "label world" right now range from a low of 4X to a high of 8X (and perhaps more). They were higher just a couple of years ago when the "buying frenzy" created by the private equity (PE) firms was in full swing…that has stopped to some degree due to the fact that most PE firms now have their "platform" investment and "tuck-ins" do not command the same multiples as did their platform. Interest rates are a factor as well…

Positioning your company for sale can be a challenging experience, but the first step is knowing what your "adjusted EBITDA" is and what a knowledgeable person thinks the correct multiple might be for your label company.

If you are interested in finding out this information, your CPA should be of some help. That said, a firm that deals with sales of companies in your industry might be a better choice. Your Trade Association (ie: TLMI) or ads in the trade publications (ie: L&NW) might be great resources as well.

If you are now at a mental impasse, please do not hesitate to reach out to our firm…this is what we have been doing since 1987 while closing over 250 deals for business owners in the "Wonderful World of Print"!

Disclaimer: *This "M&A Corner" column was not meant to be a comprehensive tutorial on "adjusting" EBITDA for purposes of a valuation of your business. It was simply meant to get you sufficiently versed on the topic to be able to at least have a dinner conversation with fellow label company owners.*

Jim Anderson is the Founder & President of Scottsdale, AZ-based Corporate Development Associates ("CDA"). CDA is a boutique Merger & Acquisition consulting firm that has focused 100% on the printing industry since 1987.
Website: www.printmergers.com
Contact Jim via email: janderson@printmergers.com
or cell/text: 602-432-0426