

# SEEING MULTIPLES

**Does your business check all the boxes? Here's what you need to know about transaction multiples.** BY STUART AUST AND DANIEL AUST

**A** popular and sometimes controversial topic that continues to generate a great deal of conversation and buzz in the pest control industry is transaction multiples. We hear multiples being discussed at trade shows, industry events and among owners of pest control companies. Most of the readers will likely agree that while multiples are widely discussed in our industry, there are often many misconceptions regarding them. Frequently, business owners believe that if one of their competitors receives a certain multiple, then their business should yield a similar or higher multiple. While your business may in fact yield a higher multiple than a competitor, you also must consider the aspects of your business that create value and are attractive for a potential buyer. However, before we define the business attributes that yield a premium valuation, let's first lay some groundwork and define transaction multiples.

Multiples are ratios that compare a company's revenue to purchase price, earnings to purchase price, recurring revenue to purchase price and so on. In the private markets, investors don't have the luxury of looking at how a company is trading in comparison to its revenue, EBITDA, EBIT and so on. Thus, multiples are ratios utilized to compare transaction values from one company to another in related industries. They measure and track where valuations are trending in select industries and are indicators of the general direction of the overall marketplace.

However, just because the multiples are elevated at a certain point in an industry's history, it doesn't necessarily mean that every business will receive a high multiple. This leads us to the next question: Why do certain companies receive a higher transaction multiple than others in each industry? While the market ultimately determines the value of your

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business, there are certain business characteristics that check the boxes for certain buyers and are more attractive than others. So, let's take a closer look at the business attributes and boxes to check when building your greatest asset.

**STRENGTH IN SCALE.** First, it's important to recognize that the size and scale of your business plays a role when it comes to transaction multiples. While the terminology and criteria may vary from buyer to buyer, there are generally two types of companies that are acquired by buyers, a stand-alone business and a tuck-in business.

A stand-alone business generates significant top-line revenue, has a strong brand and presence in its market and a management team in place that possesses the talent and experience to operate the business effectively post-transaction. Likewise, the stand-alone business can continue to operate independently in its market and exist on its own without constant oversight and involvement from the acquiring party. Often these businesses, also referred to as "platforms," undergo minimal change from the perspective of the customer as the workforce, service offerings and name remains much intact.

Conversely, the tuck-in business may have similar characteristics to the platforms, but these ones lack the size and the market share to keep the core operations in place as they may consist of a single route or multiple routes with minimal management. The primary objective of

these acquisitions is to accelerate growth and add density by acquiring the customer base. Once the tuck-in business is purchased, it is absorbed into the buyer's primary operations and synergies are created, strengthening the operation.

The distinction between the stand-alone business and the tuck-in is important because of the value that is paid for each type of business. Since the stand-alone business is highly sought after in the marketplace, these multiples are elevated. Whereas the smaller-sized business, while accretive, is adding to the buyer's core operations and delivers a lower multiple compared to the stand-alone business. With this said, remain focused on growing your top line and reinvest into your business culture and infrastructure. This strategy will pay dividends when you decide to bring your company to the market and generate a higher multiple.

**EARMARK EARNINGS.** However, it's simply not enough to grow your top line without having a steady stream of earnings or cash flow in place. Earnings, also known as EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) is examined through the lens of what your business will look like post-transaction, removing all personal and extraordinary expenses.

Earnings are significant because the general market values each business based on its future cash flow. A business that is healthy should generate an EBITDA margin upwards of 20 percent now and into

the future. For this reason, the market will look at the key factors that will make this cash flow sustainable and expand these earnings in the future. On the other hand, the market will assess what risks are present in your business and which factors may slow down and impede future earnings.

Thus, operate your business today with your earnings in mind. Treat your business like an investment that generates earnings now and into the future. Some of the ingredients that will support your earnings growth and provide future stability include:

- High percentage of revenue characterized as recurring or subscription-based revenue.
- Diverse customer base that is priced at a premium and accustomed to regular price increases.
- Track record of offsetting annual customer churn through new customer sales and quality service.
- Expense accounts that are well-managed and in line or better than the industry standard.
- Stable and tenured workforce to operate the business post-transaction.

With your business having a financial history and future story of growth to the top and bottom line, it will be in high demand and yield a higher multiple.

**ALL ABOUT TIMING.** Life is all about timing and a successful investor "knows when to hold 'em, when to fold 'em," in the

words of Kenny Rogers' song "The Gambler." The year our pest control business, Bug Doctor, sold, our revenue was at its highest level and that growth trickled down to our bottom line, expanding our earnings.

Likewise, we were highly sought after and given the opportunity by many potential purchasers to operate as a stand-alone business.

Thus, we received one of the highest multiples at the time due to the makeup of our business and the competitive nature of the marketplace.

One recent development such as this in the market that will create more opportunities for pest control owners is the influx of private equity-backed companies into the pest control industry.

These firms make regular investments into companies from a pool of capital called a fund in a particular industry be-

fore making their eventual exit through selling, going public or some other offering.

To deploy its strategy, the private equity-backed firm makes investments into stand-alone or platform type businesses that are well-positioned in its marketplace to grow organically and through tuck-in acquisitions. Today, there are more private equity companies in the pest control space than ever before due to those companies being deemed an essential business during the pandemic and the subscription-based revenue model.

For this reason, pay close attention to the market and the dynamics of the M&A landscape. If you become aware of opportunities that place your business in high demand, that could very well be the time to act and put your company on the market.

**IN CONCLUSION.** As you can see, there is more than meets the eye when it comes to selling your business and transaction multiples. Even if you're not considering selling now, treat your business like it's an asset and always operate with the end in mind.

We recommend reaching out to a pest control broker/advisor that understands the space, can evaluate your business and help prepare your business for an eventual sale. While transaction multiples are good indicators of the general marketplace, they are subject to fluctuation based on market conditions. However, a business that checks all the boxes will always be highly attractive to buyers and demand a premium multiple. **PCT**

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The advertisement features a light gray background with a network of blue lines and circular nodes. At the top left is the Victor VLink Pest Network logo. To its right is the headline "WE CREATE VALUE. LET US SHOW YOU HOW." Below this, five key benefits are presented in blue text, each accompanied by a white hexagonal icon: "Instant Alerts" with a smartphone icon, "Data-Driven Insights" with a computer monitor icon, "Fast, Humane Kill" with a mouse and lightning bolt icon, "System Flexibility" with a location pin icon, and "Time Saved" with a clock icon. At the bottom, a red banner contains the call to action "GET A DEMO TODAY" and contact information for Mark Ebner.