

# What to Look For During Valuation Of A Deal

Valuations are becoming even more challenging in the current economic climate, which means that some aspects need to be considered more carefully.

In particular, in situations such as IPOs, transactions and reporting, valuations are subject to challenging debate, revealing certain weaknesses in the supporting analyses. Quite often the commercial aspects of valuations, which are fundamental to derive a well-founded and robust valuation, are reviewed less diligently.

Sales, profits, cash, working capital, book values of assets and liabilities are metrics often perceived as sufficient to calculate a value. However, these metrics are results as opposed to value drivers. A robust valuation not only requires thorough analysis of financial data, it also requires having a strong grasp on the key commercial aspects and the value drivers of a business.

Some key commercial aspects are often overlooked in the value derivation. It is important to conduct a thorough review of the wider commercial and non-financial aspects of a business to help derive a robust value assessment that can stand scrutiny in all situations.

## Brand & Marketing

Valuations often consider sales growth percentages achieved in the past and project them into the future with a trend analysis. However, a business's brand management capability and the existence of an adequate marketing function may be overlooked or not assessed carefully enough.

A business's sustainable sales growth is directly affected by its brand management and having a well-formulated marketing strategy. Damaged reputation and poor marketing directly impact revenue, which results in lower cash flows and a lower valuation.

## Cash Management

The reported cash balance at a valuation date is often taken as a direct input for the valuation in the net debt calculation. However, further consideration is required around the efficiency of managing cash through working capital, capital expenditure and the day-to-day financing of the business.

Issues such as over or under expenditure on capital items, higher collection days versus lower payment days, inefficiency of stock turnover can easily become escalating problems, which can impair business value over time. Cash-related issues can restrict working capital and the ability to pay dividends, which can also impact shareholder returns.

## Combinations & Integration

When valuing larger conglomerates or businesses that have grown through acquisitions, the track record of business combinations and integrations needs to be considered. Studies suggest that a significant number of acquisitions and mergers fail to achieve their planned objectives. Reasons include the inability to extract synergies, poor integration planning vs

implementation and a disjointed strategy, amongst others.

Acquisitions and business integrations, if conducted properly, should add value to businesses. While conducting valuations of businesses that have undertaken acquisitions or mergers previously, it is important to consider how well the integration process and if indeed the transaction enhanced the business with sustainable benefits. Any costs or liabilities associated with the acquisition and integration should also be reviewed in case they crystalize in future.

#### People & Governance

Adequate management teams, a well-constituted board, experienced leadership and regulatory compliance are commercial and operational aspects that are difficult to quantify but can impact business value over time.

Management and leadership are charged with operating a business that directly affects financial results. Maintaining adequate operations, internal controls and governance help sustain value in a business and mitigate the risk of fraud and misappropriation. Reviewing these matters as part of the valuation may highlight certain points that may negatively or positively impact a business's value.

#### Strategy & Planning

Having adequate strategy and diligently implemented plans are important for any business and its future success. As a fundamental and commercial consideration in a valuation, business strategy should be challenged, stress tested and mapped to the plans that are prepared.

The financial forecasts of a business should reflect the strategy and the related plans. Overly prudent or ambitious strategies with mismatched planning can cast doubt over the future financial performance of the business, which increases uncertainty, thereby reducing the price a prospective purchaser may be willing to pay for the business.

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