

How to Build Value in your **Towing Company**

Presented by George C. Metos March 22-24, 2023

About your Presenter



- George C. Metos
 - President of GM Consultants (a business brokerage)
 - Business Broker
 - Salt Lake City, Utah
- Currently representing owners of towing companies, auto recyclers and other light industrial companies in the sale of their business.
- Trade shows that I attend: national & some state level tow shows, Auto Recyclers of America and United Recyclers Groups shows.
- Twenty years in software development. Merged my company with a public company.

Why does Company Value Matter?



- To know if you are making the right decisions in building wealth. By monitoring the value, an owner can tune their company for optimal
- For settling accounts with shareholders or family members in case one or more are to be bought out.
- Bank loan purposes.
- We want to talk about the market, and the buyer attitudes, which we'll do once we have a basic understanding of determining the value of companies.

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- The premise of this presentation is that by examining how towing companies are sold, we can learn from historical sales data.
- Just as home values are in part based on prior home sales, we can learn from prior sales of towing companies. An asset is only as valuable as the marketplace proves it to be.
- Knowing the valuation methods and what the market will bear can help those who want to sell as well as those who only want to monitor their progress.
- The approach of this presentation is to study valuation methods, and the current attitude of the buyers.

The Two Basic Valuation Methods



A) Assets plus goodwill

- Assets in the towing industry are typically the fleet value. There is usually very little inventory in towing companies.
- Goodwill (synonymous with blue sky) is intangible, and is based on customer relationships, contracts, quality of driver pool, and general financial strength of the company.

B) Adjusted profit times a multiple

- The adjusted profit is not based on the net income shown on a tax return, because that doesn't tell the whole story.
- The multiple is based on the relative size of the profit.

Best of the Two Methods



- Fleet value of \$1.4m, adjusted profit of \$200k, goodwill of \$300k = \$1.7m valuation
- (profit is ignored)

Method B)

- Fleet value of \$1.4m, adjusted profit of \$800k
- Assume a multiple of 2.5
- 2.5 x \$800k = \$2.0m valuation
- Higher than Method A, and seller gets the best of the two approaches
- The equipment is included in the sale at this price

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In my experience selling towing companies, there appears to be a pattern regarding the financial value that the sellers have received. Let's briefly examine some actual deals that serve as examples to illustrate leverage.

- Great deal for the seller \$11m purchase price for a HD towco with \$2.8m of adjusted profit and \$3.5m in equipment value.
- Good deal \$4.7m purchase price for a HD/MD towco with \$1.7m of adjusted profit and \$3m in equipment value.
- Moderate deal \$1.7 m purchase price for a LD/PPI towco with \$500k of adjusted profit and \$1.4m in equipment value.
- Disappointing deal \$1.1m in purchase price for a LD/motor club towco with no profit and \$950k in equipment value.

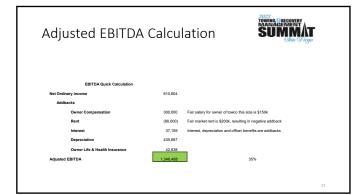
Comparison of Profit to Purchase Price

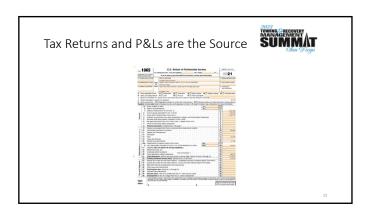
Analysis



- Adjusted profit (or EBITDA) must be determined
- Buyers will pay on a profit or an asset method.
- The good and great deals are based on a multiple of adjusted profit.
- Moderate and disappointing deals are based equipment value and some blue sky (synonymous with goodwill). Selling on an asset basis is a sign that the company is not well developed yet.
- When the analysis is not to your liking, don't kill the messenger (me or your analyst). Sellers may as well know the likely buyer response before going to market.

EBITDA Sample	e Calcu	ulation – P&L
EBITDA Quick Calculation		
Net Ordinary Income	610,804	
Addbacks		
Owner Compensation	300,000	Fair salary for owner of towco this size is \$150k
Rent	(80,000)	Fair market rent is \$200k, resulting in negative addback
Interest	37,159	Interest, depreciation and officer benefits are addbacks
Depreciation	435,687	
Owner Life & Health Insurance	42,838	
Adjusted EBITDA	1,346,488	35%
		10





	Jan- Sep 2022	_
Very simplified P&L		•
Gross Profit	2,427,720	
Expenses	, ,	
General & Administrative	304,335	
Owner Compensation	450,000	High for one owner
Rent	120,000	Business owner also owns the real estate
Interest	37,159	
Depreciation	435,687	One year's worth of new truck purchases
Owner Life & Health Insurance	42,838	
Other Expenses	426,897	
Total Expenses	1,816,916	
		_
Net Ordinary Income	610,804	16%
		=

Net Ordinary Income	610,804
Addbacks	
Owner Compensation	300,000 Fair salary for owner of towco this size is \$150k
Rent	(80,000) Fair market rent is \$200k, resulting in negative addback
Interest	37,159 Interest, depreciation and officer benefits are addbacks

435,687

Owner Life & Health Insurance 42,838
Adjusted EBITDA 1,346,488 35%

EBITDA Quick Calculation

Depreciation

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		,		The Best Towing Company			mpoja.
B Prin	cipal prod	luct or service	Туре	Number, street, and room or suite no. If a P.O. box, see instructions.		E	ate business started
			or	1234 Main Street			
C Bu	siness co	de number	Print	City or town, state or province, country, and ZIP or foreign postal code		FI	otal assets
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L S	13	Rent			[13	120,000
ogo	14	Taxes and licenses			[14	
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Her	е	 		· ·	with	the pr	eparer shown below?

EBITDA Mu	ıltipl	liers
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- Most companies are sold on a multiple of 2-4 times ebitda, <u>or</u> sold based on assets (truck equipment) plus goodwill.
- Higher ebitda implies a stronger company, having made lots of good decisions and accumulated lots of beneficial contracts or relationships. Therefore, buyers are willing to pay higher multiples.
- Capex affects multiples. For industries that have to reserve a portion
 of their profits for equipment, as in towing, buyers will pay a slightly
 lower multiple of ebitda. In other words, high capex (capital
 expenditures) will lower the multiplier.

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Goodwill (or Blue Sky)



- This is the intangible value of a company
- Goodwill could be based on favorable contracts or rotations, commercial relationships, specialized skills, a well-trained and deep staff, particularly drivers, and prospects for continued success.
- There is no formula for calculating goodwill. It takes judgement of the factors above, and anticipating how buyers will react.
- If a buyer will have a difficult time replicating your company, then goodwill would be higher than a company that is easy to replicate.

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Working Capital



- Sometimes called operating capital
- These are funds that many buyers expect to be left for them to operate the company after closing. They don't want to raise funds or take out a loan on top of the funds they raised or borrowed to buy the actual company.
- It is fundamentally a money grab, but "resistance is futile".
- Classic definition is the average of the last 12 months of current assets minus current liabilities. Many times this is simply Accounts Receivable minus Accounts Pavable.
- Nerd alert: a company that pays their bills more quickly than they get paid by customers will be penalized by this formula, but we can make special accommodations.

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- If the towco operator owns the real estate, then he/she has the option of leasing or selling outright.
- A right of first refusal for the tenant to buy the real estate is the minimum expectation.
- Many times, a lease with an option to buy years down the road is established.
- If the operator leases the property, it is wise to know whether the landlord will lease to a well-qualified buyer of the company.
- In rare occasions, an operator may own land that has become more valuable for another purpose than towing. An appraisal and calculation of market rate rents can be made to determine if this is the case.
- It is important to determine in advance if there are any issues with zoning, environmental, easements and clear title.

To Improve Profits (therefore Value)



- The consultants here at the Summit are likely the best resource.
- I'm not the operations guy, but I can tell you how buyers react.
- Peer groups have worked very well in other industries. I don't hear enough about them in towing, but there are a few.
- Continually monitor company metrics and stay up on current issues in towing, just as you would your personal health.

What Buyers Look for in a Towco



- Profit and EBITDA is the best way to communicate it
- Trained drivers. We all know this is an issue nationwide.
- Contracts and relationships, whether municipalities, law enforcement, DOT, or commercial accounts.
- Competitive pay and sometimes benefits.
- Buyers typically have a favorite type of towing: LD, Private Property Impound, Roadside, HD, Recovery, Transport, etc. Some look purely for profit, but most want to continue operating the type that they know.
- Expectation of continued success, whatever that might mean in your situation (employees, rates, competition, etc.)

What's Sel	lling t	these	Days?
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- HD/Recovery is favored by the big buyers, due to high barriers to entry (expensive equipment), driver skill requirements, customers travel from one location to another.
- Some Private Property networks are growing. Typically difficult for most operators to warm up to. But someone must do it, and three sources of revenue help (tow, storage, auction).
- LD and Roadside Assistance networks in metro areas are popular.

Preparing for a Sale



- Financial analysis and summary of tax returns and P&L statements.
 - See next slide for an example of a well-detailed P&L that indicates the revenue from various aspects of towing
- Analysis of equipment value, contracts and relationships, employees.
- Decision on asking price, which requires EBITDA calculations over several years.
- Development of a presentation package. Buyers will be frustrated if this is not prepared in advance. Just like selling anything.

Well-detailed Towco P&L



AFTER HOURS CHARGE
AIR CUSHION RECOVERY
BOOT SERVICE CALL
CLEAN UP
EXTRA MAN
FLAT TIRE CHANGE
FLATBED TRUCK
FUEL SURCHARGE
HEAVY DUTY TOWING
HEAVY DUTY RECOVERY
INSIDE STORAGE
JUMP START
LOWBOY SERVICE
MEDIUM DUTY TOWNG
ROTATOR
SERVICE CALL
SPECIAL EQUIPMENT
STANDBY TIME
STORAGE
TOLL CHARGES
TOWING PARTS

Jan- Sep 2022 Income 76,234 AFTER HOURS CHARGE AIR CUSHION RECOVERY 14,084 **BOOT SERVICE CALL** 4,855 66,134 **CLEAN UP** 48,684 **EXTRA MAN** 15,686 **FLAT TIRE CHANGE** 116,334 FLATBED TRUCK **FUEL SURCHARGE** 135,030 1,887,348 **HEAVY DUTY TOWING** 183,343 **HEAVY DUTY RECOVERY** 14,986 **INSIDE STORAGE** 9,833 **JUMP START** LOWBOY SERVICE 156,333 4,832 **MEDIUM DUTY TOWING** ROTATOR 486,906 SERVICE CALL 18,343 SPECIAL EQUIPMENT 51,699 STANDBY TIME 19,030 STORAGE 309,344 70,383 **TOLL CHARGES TOWING PARTS** 46,033 **TRACTOR** 96,010 **Total Income from Towing Services** 3,831,464

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Types of	Towco	Buyers
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- Rookies they should start with a small operation, whether they have a lot of money or not.
- Local towers want to expand their territory.
- Regional power multistate. Knowledgeable, but sometimes dangerous in terms of confidentiality, and may believe they can build instead of buy.
- Investment firms they are beginning to take interest in towing.

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Investment Groups



- They may go by several names: Private Equity Groups, Family Offices, Investment Bankers, and private investors.
- Favor towing because it is an essential service, cannot be automated or in danger of foreign competition.
- Like that the industry is fragmented. Compare LKQ to Guardian and United Road Towing.
- Prefer owners to roll equity forward (keep stock in newco) and continue to build. Can make money on initial and follow-on sale.
- Here to stay. Could be great for the strong operators who want to grow. Make no mistake...they will grow as a force in towing.

The Sales Process



- Advertising can be tricky. It can alert your competition. Still, some risks must be taken.
- Personally, I like making outbound calls to known buyers in addition to discrete advertising.
- NDAs are only as valuable as the integrity of the person signing it.
- Eventually a Letter of Intent
- \bullet Due diligence commences, to validate your information
- Keep operating as if no sale is imminent

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Final	Agreements
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- After the LOI and due diligence process.
- Asset Purchase Agreement (APA) describes what is being acquired, and the pertinent terms. Fairly sophisticated agreement, drafter buy buyer's or seller's attorney.
- Non-compete agreement for the seller
- Real estate lease or sale
- Closing is usually virtual. Funds are transferred.
- Seller may stay on for a transitional period, or long term.

Stay Informed!



- Information is power.
- Consolidation is happening, and will not stop any time soon. Be aware of how it may affect your business.
- Being informed is your best strategy. By being here, you are participating in knowledge sharing.
- Similar to preventive maintenance of your equipment, monitoring company value preserves what may be your biggest asset.

Thanks for Participating

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