What's It Worth?
Business Valuations, Mergers, Acquisitions, and Consulting
NEWSLETTER ARTICLE ARCHIVE

How to Read Income Statements Coming Out of a Recession

What do annual income statements tell you about a company when the economy is slowing coming out of a recession? Many of the businesses that I am working with have had reduced gross revenues or flat revenues. Does this mean that the value of the company is definitely down for the year? Will the bank finance a business with reducing revenue year over year? Will the Seller take less for their business? What can you expect?

This past year I have seen companies where revenue has dropped 50% and more yet, the company has been able to either maintain profits or increase profits over the previous year or two. This result has come from leaner inventories and payroll. For several years leading to 2007, many companies became complacent in watching their expenses. Profits continued to grow due to increased sales and no planning was being done concerning the future. The trick for a current buyer is to determine if the company can maintain the current profit level. Questions like the following have to be asked:

1. Is the staff too small now and will they burn out and provide less customer service?
2. Are inventories too low now to provide the needed turn around customers expect?

   and allows you the opportunity of finding Buyers who can even provide a better future for the company as it grows and has the economies of scale to provide better benefits.

   This is the year that can help you maintain and grow the value of your company, or it can be the year that makes your exit strategy more of a flame up, burn and crash exit in the near future. Buyers buy based on the future outlook and pay based on the past profits
3. Have the proper capital expenses been made recently or is the company borrowing from the future and large capital purchases will be required in the near future?

Even if profits have increased during gross revenue reductions, Buyers needs to look at customer concentration. Many times, you will find that customers that represented 10% or less of the total revenue, now represent 40%. This needs to be reviewed to make sure that the concentration can reasonably be reduced in the near future so that you do not pay too much for a company. If that one customer could easily leave, you will find yourself with a totally different company in your hands that might be bleeding red in the near future.

Banks are looking for stronger buyers but are willing to do deals when profits can be maintained and the outlook for the company and the industry is sustainable. Each deal is different, but profit (cash) is still king if the specific market the company is in can show that it is moving forward on a more positive note in the next year or two.

Paint your picture with oil and not water colors – so that the picture stays bright and does not run when the bank throws some water on your dreams!

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