30 Second M&A Newsletter

Stay Bonuses Add Value

Confidentiality is important in a sale. But what do you do when critical employees must be informed? We recommend stay bonuses. A stay bonus provides an incentive for key employees to cooperate and assist with a sale.

We see stay bonuses ranging from 20% to 100% or more of an employee's salary. It's common to allocate around 50% percent at closing and 50% six months or a year later. Buyers want assurances the management team will stick around. A stay bonus significantly increases that chance. It's a nice carrot for the employee, and it makes your company more saleable because it lowers a buyer's risk.

Keep Widening Your Moat

When selling a business, one of the qualities buyers look for is barriers to entry. The harder it is for someone to get started in your business or take away your customers, the bigger the barrier. Warren Buffet talks a lot about moats. "In business, I look for an economic castle protected by unbreachable moats," he says. "If you have an economic castle, people are going to come and want to take that castle away from you. You better have a strong a moat."

The idea of a moat refers to how well your company can keep competitors at bay. Buyers see long-term value in wide moats. The better the moat, the greater confidence the buyer has that your cash flows won't fall to competition over time.

One way to gauge the width of your moat is to identify your unique selling proposition. The aim is to have "three uniques." Maybe you make widgets and you're one of only a few widget makers who can fabricate them out of carbon fiber. And maybe it's hard to find short-run manufacturing or someone who will provide widget engineering support for a customer's research and development work.

The goal is to identify a unique combination of valuable services that sets you apart from everyone else in the market. There may be a limited few who can claim two of your "uniques" but the goal is that no one else can claim all three things you offer your clients. Identifying your three uniques will show the buyer that you really do have something special – something difficult-to-imitate, and proprietary to you.

Then, as you evaluate your business from year to year, ask yourself if your three uniques still stand. Has your competitive advantage gotten stronger (or weaker) than the year before? To buyers, that can be a more important indicator of future value than your revenue and profit alone.

Buyers are looking for long-lasting competitive advantages. So even if your business is having record sales, you need to think about how you are widening your competitive moat.

As Buffet said, "We tell our managers we want the moat widened every year. That doesn't necessarily mean the profit will be more this year than it was last year because it won't be sometimes. However, if the moat is widened every year, the business will do very well. When we see a moat that's tenuous in any way - it's just too risky."

When it comes to selling your business, any perceived risk lowers the value. Lower the risk. Build wider moats. Bring more buyers to the table.

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