"How to Sell Your Pest Control Business for Maximum Profit: 8 Key Factors that Impact Valuation…"

By Ryan Levesque, PCMS President

with Cyril Jones, RKJ Partners, LLC

Table of Contents

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Introduction

Ryan: **Hey, this is Ryan Levesque, president of Pest Control Marketing Systems,** and I'm here with another Genius Minds of Pest Control interview.

Today's guest is Mr. Cyril Jones. Cyril is the founder and managing partner of a company called RKJ Partners, LLC. RKJ Partners is essentially a strategic advisory company, which sort of operates in many ways like an investment bank.

So for example, **they focus on helping smaller, middle-market companies in a few select industries,** like pest control, and they help with things like raising capital, negotiating joint ventures and **the topic of today's call, which is selling your company.**

In today's call specifically, **we're going to be talking about how to sell your pest control business for maximum profit,** and we're specifically going to be covering eight key factors that impact the valuation of your company.

Cyril, thanks so much for being with us and agreeing to being on the call.

Cyril: Ryan, thank you for the introduction. I appreciate being here. **I appreciate the opportunity.**

Ryan: Cyril, before we dive right in, I have a question for you. If I'm a pest control business owner and I'm listening to this right now and **maybe I have no intent on selling my business today,** but maybe 10, 15, maybe 20 years down the road when I'm closer to wanting to retire, I might consider selling my business.

So if I'm in that sort of situation, I have no intent on selling my business today, **why should I pay attention and listen to this call?**

Cyril: Well, for a variety of reasons. We run into this issue a lot, in talking to clients or perspective clients, in that in order to **maximize value at exit or at the sale, you need to be prepared to be sold.**

That encompasses a lot of different things, from the perspective of **is your back office really in a position where you can maximize value?** Can you really show that you have a **strong track record for growth?** Can you show that you've been profitable? **Can you show that you have good relationships?**

Those are the things that really impact value and could drive potential inquiries to you.

Ryan: Okay, so talk to me on timeline on that, before we dive into the eight key factors, which is the meat of our conversation today.

If I'm looking to sell, maybe I'm not looking to sell today, but someday I might want to sell my company, **how far in advance do you need to really start making preparations to put yourself in the best possible position?**

Cyril: Well, it depends on your starting point, to be perfectly honest with you, and the most critical aspect of the sales process is **how clean are your numbers.**

And when I say clean, **are you using an outside accounting firm or is it all just internal?** And if you are using an outside accounting firm, **are your numbers audited, are they reviewed, are they compiled?**

Basically, it gives the outside investor some comfort, if there's a third party reviewing your numbers.

So let's just say for instance, that you have an accounting firm you've used for a while. They're doing a great job for you, and **they're producing timely reports.**

That process of trying to **sell your business could span anywhere from three to six months,** but if you have got to start from ground zero of trying to find a firm, downloading information and going through that fun process of working with a new CPA firm, **that timeframe could span anywhere from six to nine months.**

Ryan: Got it. Okay, that's a really helpful benchmark.

How Strong are Your Current Revenues?

Ryan: Let's dive into the meat of the conversation, **the eight key factors that really impact the valuation of a pest control company.**

What's the first key factor?

Cyril: Well, I guess the most important factor, which an acquirer would look at, is **how strong are your current revenues.**

By that, we're **looking for a lot of repeat business from former clients that you've had for a number of years.** They're looking for a low churn factor. Churn factor would mean that you've got a number of clients, and if you were to look at it over a historical period of time, let's say you're on average looking at about 100 clients that you're providing services for.

Does that number change dramatically over the years? Are you currently servicing that number of customers? Are you losing 10 and picking up another 10, or are you actually growing?

Based on the recurring or the stable level of customers that you have, it **should generate a stable recurring revenue model,** which allows the acquirer to predict, with some degree of certainty, obviously nothing is 100 percent guaranteed, but with some level of certainty **what that business is going to generate going forward.**

So that gives the acquirer a great deal of comfort, to know that they're buying a stable business, one that is not being positioned for a sale, meaning you're doing anything extraordinary prior to selling the business to prop up your sales or prop up your earnings.

They want to see a consistent level of revenue being generated by the entity.

Ryan: Got it. So a couple of questions on that topic. I've spoken to other pest control business owners that have actually sold their companies, and **I know one of the things the acquirers were looking at, was a volume of customers.**

In other words, they were interested in having a large customer base. However, for this particular operator, **his business was more of a niche business.**

So he had fewer customers, **but he was a premium provider, so he sold at a premium price point.** So his margins were extremely good. At the same time, he wasn't a volume business.

Have you ever run into that situation, and how might something like that impact valuation?

Cyril: Absolutely. From that perspective, if you've got a smaller group of clients but you're providing a very specialized service, **that's going to be valued higher than the guy with 1,000 customers providing very generic services.**

So from a valuation perspective, **I couldn't tell you specifically without looking at the exact company,** you would be valued at a premium, because everybody is always, regardless of the size of the company, that is the acquirer, **everybody is always looking for points of differentiation.**

How am I different from the other guys? And a lot of times, you can develop that as a pest control company, or if it makes more sense and the price is attractive, you can actually go out and buy those capabilities.

So it would make sense for the company providing the more specialized services to essentially achieve a higher valuation, relatively speaking.

Ryan: That's really helpful, Cyril. When it comes to recurring revenues, **how important are formal contracts?** Because some of our clients utilize formal contracts, but then we have other clients that have no formal contracts in place. **They do obviously recurring business, but customers aren't locked in with a formal contract.**

At the same time, they have customers that have been with them for years and years, **because they're just satisfied and happy with the service.**

So talk to us a little bit about that.

Cyril: Sure. If contracts aren't a part of the mix, relative to your diligence package, **one way that an acquirer could get comfortable is to have a transition plan in place,** meaning the current owner would have a visible role throughout the process and allow for their sales teams to transition those relationships to the acquiring company or the new company.

You would have to, if contracts are in place and **customers are in essence locked up, it's a little bit easier, and the seller could walk away at a faster clip.**

But there would probably always, in all deals, be some sort of a consulting agreement or an earn out, if you will, where **that seller would basically become, I won't say an employee, but more of a contract employee,** if you will, for the acquiring entity, just to make sure that those relationships transition.

With every acquisition, **there's never any guarantee that 100 percent of the customer base is going to transfer over,** but the acquiring entity would try to be as creative as possible to ensure as many clients came over at the point of sale.

Ryan: Got it. That's really helpful.

Strong Management Team

Ryan: What's the next key factor that impacts valuation?

Cyril: **Well, getting a strong management team is probably going to be pretty critical,** understanding that different levels of responsibility have probably been pushed down, if you've got a pretty mature company and have **several layers of management.**

The key would be how much experience do these individuals have. **Do you have the right people in the right positions?** That would be critical as well.

In some situations, just to be perfectly honest about the sell-side process, **there could be some redundancy, relative to the company be acquired.**

If the acquiring entity is larger, and in a lot of instances positions such as accounting or the CFO, if you will, or the back office staff, the AR/AP person, **those persons maybe actually be displaced in the event of a sale.**

But it would depend on the situation. **It would depend on the level of sophistication of the acquirer,** but I think all good people that could add value post-closing would be retained.

But there is the possibility that some people could be let go in the process, so you just have to make sure that verifying those persons have had the right experience to drive the business, **but post-closing you've got to make sure the right people are still in place.**

Ryan: For most pest control companies that I work with, they're on the smaller side. **So for the non-essential functions, like accounting or payroll or HR, they're going to outsource those functions,** through a third-party contractor, or in this case, they might not have an in-house accounting team. They might have a bookkeeping firm that manages their books, and they have a CPA, obviously.

As far as the critical functions, **are there a few key positions that you want to have in place before considering selling?** The reason why I bring that up is because a lot of the operators I work with, or the business owners that I work with, they're owner/operators.

So they're still playing an active role in their business, and in some cases, they might be what I like to call a slack adjuster. So if an employee is sick or doesn't show up one day, they might actually be the guy who fills in for them and actually performs service for the customer.

They're the backstop. If there's a gap, they're the one that fills that gap.

But beneath them, and every company that I work with is a little bit different, but in your experience, **are there key positions that you want to have in place?**

Cyril: Well, if you have a small organization, you're dealing with a "Mom and pop," and a lot of those responsibilities**, if the individual is married, it may be taken up by the spouse who's not doing the day-to-day operation.**

So I think it varies from situation to situation, but I think **as you climb up the revenue chain and can afford some support staff,** critical functions would be absolutely the accounting piece, the dispatch piece and also just **back office billing and receiving of payments from clients,** would be some critical positions that would need to be filled.

Ryan: Okay, that's good to know.

Commitment from Good Employees

Ryan: What's the next valuation factor?

Cyril: **Well, just a commitment from good employees,** meaning it's critical in the service business to have a stable staff of reliable employees that could transition over, in the event of a sale.

So that's something that will be looked at pretty critically, by the acquiring entity. **How are individuals identified? How are they hired? What's your churn rate?** Are you losing employees? Is there a central issue as to why you're losing employees? Are they going to a competitor? Are they leaving the industry?

Those are factors that the acquirer would like to understand better, from the owner, and hopefully that individual would **have a firm understanding, if they are losing employees, why.**

Ryan: **Are there any key benchmarks or numbers that you want to hit?** For example, average tenure of X number of years or minimum tenure of X number of years?

Cyril: Well, it would be great if you had **employees that have been with you over a year, maybe a year and-a-half,** depending on the level of skill required.

You expect some churn, you expect to lose some people over time, just with better opportunities or different opportunities, but if you've got a work staff that is somewhere in the year to maybe 18 months of experience with your company, I would think that would be a plus.

Below that number, you sort of get a little nervous from the perspective that something could be wrong here. It could be an issue of benefits may not be comparable, the pay scale may not be comparable, the dispatch may not be comparable. So you have to really look at employees that turn over too consistently.

Also, it becomes a cost for the operation, in that **recruiting employees and training new employees creates a cost burden for the company.** So you want to just make sure that you're retaining good people and keeping them happy.

Ryan: There are certain nuances specific to the pest control industry, like for example, because it's a licensed industry by each state, **employees are**

required to go through certification and training to become a certified applicator, to go from apprenticed to basically a licensed professional in this field.

Have you noticed anything to that extent, for pest control specific, that you want to have your staff gone through all the training that they need to reach licensed state, or **is it okay to have employees in various stages of their licensing or certification?**

Cyril: I found that it varies. **You can have employees with a variety of different skill sets or certifications.** If you have an acquirer that has the means or requires a certain level of sophistication, relative to the staff, they will invest in that training and that will be a factor in the valuation as well.

They'll look at, **"What will it take to get this asset up to code?"** Meaning, would they need to invest in training or find a new employee. So that would be factored in. I would not look at that as a determinant of whether or not you're ready to be sold. **I think many people look at that in a variety of different ways.**

Ryan: Got it, okay.

Reputation

Ryan: What's next?

Cyril: **The next most critical factor, I think, is reputation.** That is something that you can't really quantify, you just have to have a feel for. But hopefully all operators recognize that the customers are the life bread of the company, and that if you can't generate business through referrals, **it's going to be generally tough to gain new sales.**

And a lot of operators grow via word of mouth, and advertising is great, be it radio or print ad or even on television, but a lot of business is generated just through your reputation and referrals.

So without that, it's going to be difficult to generate value at a sale.

Ryan: **So what are some of the ways that a potential acquirer is going to evaluate your reputation?** Are there certain steps that they take in the due diligence process to get a better sense?

I'm thinking maybe an acquirer who is out of state or out of city, who might be **looking to expand in that geographic area,** and so they don't know all the nuances and subtle history of each company in a local area.

So they're kind of going into this a little bit blind, so to speak. **So they're going to want to do that type of due diligence.** What are some of the activities that they might perform, when they're going through that process?

Cyril: Sure. **It could be something as simple as doing an online survey.** Once you're pretty deep into the diligence process and you're comfortable with sharing customer lists, it could be as simple as them picking up the phone and calling 25, 30 customers.

It could be the utilization of some sort of an online survey, which there are tons of companies that do that and they're generally free. **You can gain a sense of the reputation of the clients that way.**

So I think it's boots on the ground, kind of **understanding of the marketing techniques that could be used to do that.**

But I think the techniques that we use once we get comfortable, are pretty varied. **But I think picking up the phone and talking to a random customer for that call is probably the best source of that data.**

Ryan: Got it.

Company Culture

Ryan: What's next on our list?

Cyril: **Company culture is probably pretty important, right up there with the recurring revenue model.**

I think if there is a **difference in philosophy on how employees are treated, how they're dispatched,** it could be the way in which they're managed, I think that could spell disaster.

You could have the best deal from a price perspective and from a structure perspective, but your employees are critical. And I think if there is a huge disconnect, relative to how the business has been operated in the past, you're looking for a very trying situation that will result in, I would imagine, **the acquired entity's employees leaving and finding other employment elsewhere.**

Ryan: Maybe you don't have a pest control specific example, maybe you do, but in your database of all the deals that you've done in your career, which have span multiple industries, can you think back to maybe a specific example, where all the other ducks were aligned, **yet there was a culture mismatch between those two companies?**

What's an example of what that might mean? The reason why I bring that up is because culture is one of these things that it's sort of intangible, and **so it's difficult to put your finger on why that might be a deal killer.**

So someone listening to this, I think hearing an example might be helpful.

Cyril: Sure. **It could be something as simple as reporting,** meaning if you've got a situation where you're used to, as an employee, picking up the phone, shooting an email to your boss, providing them with an update on, maybe you're in a sales capacity, on who you've spoken with that week or who you're planning on speaking with and the results of that information, **you may find yourself in a culture that is very much driven by paper.**

They want you to fill out reports, relative to call sheets. This is who I'm going to see this week, and you're filling out an entire document. **It's a very formal process.**

I've run into that situation with a computer software company. There were actually **two software companies getting together, and one had a very informal structure and one had a very formal structure.**

The one with the formal structure was the acquirer. So you had a lot of turnover in the sales staff within the first 12 months of the deal. **They simply could not come to grips or get comfortable with the idea that they would micro-managed.**

So that's huge, and that's **something that you couldn't predict, going into the deal.**

Ryan: Got it, that's helpful.

Customer Relationships

Ryan: What's the next factor that impacts valuation?

Cyril: **Just customer relationships, the strength of those relationships,** and I think it goes back to the reputation point that we spoke of earlier.

I think you can get to that level of comfort necessary, by again **picking up the phone or having some sort of interaction with the customers.** You may have a situation where unsolicited customers have sent in testimonials or letters of appreciation. **Those things are compelling and they're useful.**

But I think having some sort of interaction with the client base, once you've gotten to the point in the diligence process where you're comfortable sharing that customer information, once you get there and **sharing that list and giving a couple customers a call and just understanding how they feel about your business,** how they feel about you as a company, is pretty compelling data.

Ryan: **Are there any benchmarks or magic numbers around customer renewals?** For example, as you know, in certain industries there are sort of rules of thumb, from a valuation perspective.

It might be 3 times net operating income or 10 times gross sales, depending on what industry it might be, and it's **sort of a quick and dirty rule of thumb, as like a benchmark.**

When it comes to pest control and customer renewals, someone listening to this, they might know what their customer renewal rate is year-over-year. **Are there certain benchmarks or numbers that an acquirer might be looking to see as either a minimum or a target?**

Cyril: Well, to be perfectly honest with you, I'm not sure if that number exists, but I will tell you just as a general rule, I would say that **if you were renewing less than 65 to 70 percent of your customers on an annual basis, something is probably amiss.**

Either your costs are probably too high, or there's an issue with your service. That's just what my gut tells me.

Ryan: Okay, that's really helpful. Is there **anything else related to customer relationships that we should cover, before we move onto the next factor?**

Cyril: No, I think it's pretty important, and again**, it goes hand-in-hand with the reputation point that we spoke of earlier.**

Service Mix

Ryan: What's the seventh item on our list?

Cyril: **The seventh item would be your service mix, and it goes back to the first point, talking about differentiation of services.**

I think if you really try to drive value at the sale, it's critical that you **stay away from as many generic services as possible and become more specialized, if you can.**

That generates, from a presale, just from a revenue-generating perspective**, it allows you to bill at higher rate.** It could increase your profitability using less people, so at the end of the day **your margins are better.**

And obviously at exit, you would be paid a premium, relative to a more generic provider.

Ryan: Interesting. So this goes hand-in-hand with one of the strategies that I work with our clients to implement, which is to do exactly what you're saying, to **add a product line to the mix that might differentiate you in the marketplace.**

So a great example would be something like critter control. **Not every pest control company out there will engage in critter control,** getting rid of mice, rats, raccoons, possums, beavers, whatever it may be, because **it does require somewhat of a specialized skill set.**

But there are a couple of benefits behind doing that. Number one, what you're saying is that because it's a specialized service, **you can command a premium,** when you eventually decide to sell your business, because there's a good chance that your acquiring company doesn't have that product mix as part of its suite of offerings. That's number one.

Number two, in a different context, for something like critter control, **that's one of the product lines that your customers tend to talk** about with their friends and family.

For example, **they might not be willing to mention that they have a cockroach problem** in their kitchen, because maybe it kind of conveys that they weren't hygienic or cleanly or whatever.

However, if they have a raccoon or a fox living in their backyard, **that's something you talk about with your friends and family and your neighbors.** So it's a great way to spread the word about you as a pest control company and the great work that you've done, **which can lead to business in your core product offerings.** Maybe it's general pest control or termite control or anything of that nature.

So the fact that you're saying it commands a premium, sort of **adds yet another reason to consider adding that sort of thing to your product mix.**

Cyril: Absolutely.

Geography

Ryan: What's the last thing on our list, of eight factors that impact valuation?

Cyril: Sure. **Geography is huge,** because what you find, particularly with the larger guys, the Rentokils and the Orkins and the Terminix guys, they're looking for more national coverage, and in Rentokils' perspective, **they're looking for international coverage.**

So you could be the perfect fit for them because you're operating in a particular area of the country that they want to expand to.

And what a lot of the big and medium-sized guys have found is that it's more cost effective and it's obviously **quicker to go out and buy capabilities, versus trying to build them in house.**

So you could be in the right place at the right time and generate a premium in that value, if someone has wanted to for some period of time for some reason, wanted to get into your market.

So it could present an opportunity to really maximize value at the sale.

Ryan: When we talk about geography, there's sort of two scenarios that I see with the companies that I work with.

There are some companies that might be in an area like Atlanta or Austin or Detroit, and they might **find themselves sort of sparsely distributed across the city.**

So they have breadth of reach, but **they don't have concentration in any one corner of that large metro area.**

And then I have other companies that I work with, that they **might focus in on one specific district or neighborhood or suburb** or larger subdivision in some cases, that is their entire focus.

From an acquirer's perspective, with those two scenarios, is one more attractive than the other?

Cyril: Well again, I think it depends. **It depends on what one would deem to be attractive,** and whether or not it fits into an acquirer's profile of what they were looking for.

If you read the information relative to the M&A guys at Rawlings in particular and also Rentokil, **very different views on what's attractive and what's not attractive.**

So I think it varies from acquirer to acquirer, and it's **pretty difficult to anticipate what would be deemed to be attractive by both parties.**

So I think the goal would be to **try to focus on growing your business as best as possible,** making the best possible decisions at every turn and trying to maximize value, and hopefully that will be realized at a sale.

Ryan: Got it, good.

Patience

Ryan: We covered the eight factors that impact valuation. **Is there anything else relative to valuation and selling your business for maximum profit** that we haven't yet covered?

Cyril: **Well, I think patience is a word that everyone who is entering into the space and thinking about selling their business needs to be familiar with.**

It takes time. **It takes time to get prepared to be sold.** The process of attracting an acquirer takes time, and also once you have someone and you're locked in under a letter of intent, it's still a process.

So a lot of sellers tend to get frustrated, thinking that I'll list my business or hire an agent to sell my business, and 30, 60 days later I'm sold, and i**n most instances that's just not the case.**

So it would be great that if an operator was contemplating selling their business, that they had a **realistic expectation of a timeline.**

Ryan: Got it. And just to recap, you mentioned at the beginning of the call what that might be. **What would be a realistic expectation from a timeline perspective,** from deciding to list your business, all the way through realizing a sale?

Cyril: I think realistically, **anywhere between 6 and 12 months, and one of the biggest factors would be how prepared are you,** from the very beginning, to be sold.

And a lot of that has to do with accounting. **Do you have to go out and find a firm to basically get your books in order?** If you already have your books in order, it dramatically impacts the timeline, by making it shorter.

Ryan: Good, good.

Conclusion

Ryan: Cyril, this was extremely helpful. **Thank you so much for sharing your knowledge and your expertise on the subject.**

If one of my Pest Control Marketing Systems customers is interested in possibly selling their business and wants to learn more about what you do, how can they do that and when would be the right type of scenario to **reach out to your firm, to speak about possibly working together?**

Cyril: Well, a couple different ways they can reach out to me, but **you can call me at any time throughout the process.** We're always willing and open to having conversations with sellers or potential sellers, just about the process, what we see in the market, what we see from a preliminary valuation perspective.

I don't think there's ever too early of a time to talk to someone. We find ourselves in very much of a consulting role in speaking with clients that may not be a client today, **but 12, 18 months down the line, they tend to resurface and want to engage in a formal process.**

Ryan: Got it, and how might someone learn more about you and your company, if they're interested in possibly going down that path?

Cyril: **Sure, you can visit my website, it's www.RKJPartners.com, or you can email me directly at Cyril@RKJPartners.com.**

Ryan: Cool. Cyril, again, thanks so much for being with us. This was extremely helpful, and I think **anyone listening to this call definitely walked away with a few gold nuggets of information** that's going to give them a lot to consider.

Cyril: Well, Ryan, I appreciate the opportunity, and thank you very much.

Ryan: Take care.

Cyril: Thank you.

Ryan: Bye-bye.

Cyril: Bye-bye.