

Presents ...

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Inflation, Supply Chain issues and Labor Shortages!

Is this a good time to sell your business?

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UNLOCKING OPPORTUNITIES IN THE SECURITY INDUSTRY

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INFLATION, SUPPLY CHAIN ISSUES and LABOR SHORTAGES! ALL CHALLENGES FOR OWNERS?

- Today, many business owners are struggling to stay on top of these 3 headwinds mentioned above.
- Owners/operators PROBABLY know what the effects of these headwinds better than I do.
- Inflation is never a good thing. It produces higher material costs and pressure to increase employee's wages.
- As a result, we expect owners to see declining gross margins at the very least. This will eventually affect the value of the company.
- Supply chain issues make life difficult for all security dealers but can make larger integration jobs twice as difficult to complete on time and on budget as many unique items they order are not in stock.
- Ever increasing material prices makes quoting jobs much more difficult.
- To counter act supply chain shortages, those that have capital are investing in inventory to avoid stock outs. But not everybody has capital.
- Labor shortages are a result of Covid and are affecting the economy the world over. Canada currently has 800,000 unfilled jobs. This is unprecedented.
- Labour shortages make it much harder to keep and find staff of any kind.
- Taken together, these 3 headwinds are taking up much more of an owner/operator's time.
- Selling a business requires an owner to be focused on selling the business – not trying to replace key staff members or dealing with parts not coming in on time.
- On the other hand, some owners, having been through Covid, now just do not want to face these headwinds and may just decide to sell.

WHEN IS THE BEST TIME TO SELL YOUR BUSINESS

- In simple terms, the best time to sell your business is:
 - ✓ when the business is doing well.
 - ✓ AND the overall economy is doing well.
- This is when you have the best chance to maximize your selling price.
- Sellers need to ask themselves whether these 2 factors are BOTH in place.
- The business doing well means it shows increased revenue/profit over the previous 3 years and a good forecast for the immediate future.
- The economy doing well means there is good overall growth, full employment, low interest rates and a general bullish feeling out there.
- Although some businesses thrived during covid and their owners may decide to capitalize on their good results and try to sell, in general buyers are not buying any Covid uptick in revenue and profit.
- While your revenue may be up, this may be due more to inflationary price increases rather than the number of units being sold. Buyers are actually checking on this very issue.
- In addition, most businesses will be experiencing lower gross margins.
- But it is on the buy side where things are cloudy on the horizon.
- The 3 headwinds we have been talking about have bred the one thing the acquisition market does not like – UNCERTAINTY
- In talking to brokers, I hear that more deals are simply not closing because of uncertainty. Buyers are not sure of the future. Are we going into a recession? How high are interest rates going to go?
- Now, some of these clouds mentioned above may not apply to the security industry which by all reports seems to be firing on all cylinders. Most dealers I talk to are very busy.

LETS LOOK AT WHAT IS HAPPENING ON THE BUY SIDE

Aside from uncertainty created by our 3 headwinds, there are other factors at play in doing deals today:

- Many companies are just recovering from the pandemic and have not completely fixed their balance sheets and income statements.
- Many are also dealing with the 3 headwinds mentioned above and can't think about selling.
- Only a minority of companies are showing increased “real” earnings where real means net of inflation.
- Some of those that are buying today are doing so in hopes of getting a deal.
- Financial buyers (Private Equity, individuals) are having a tougher time getting financing. Banks are being more hesitant because they don't know the future.
- As a result, strategic buyers currently have an advantage over financial buyers.
- Added to this those that do have to borrow are paying more because of increasing interest rates.
- Believe or not some deals are being held up because the professional firms involved in deals – the lawyers and accountants – are experiencing staff shortages.
- In the security industry there seems to be fewer buyers to approach.
- So far in 2022 overall valuations everywhere are down along with the number of deals being done.
- If you have good people on staff when you sell, this is a major asset. Buyers are looking to buy people.
- However, some buyers are asking when the staff they are buying last had a raise.
- Despite all this, for the bigger deals there is literally tons of PE money on the sidelines looking to be invested.

WHERE DOES THIS LEAVE US Re: M&A IN THE SECURITY INDUSTRY?

- M & A activity throughout the pandemic and after has been amazingly resilient. Although deals fell off dramatically in the March – May period of 2020, they roared back through the rest of 2020 and 2021.
- As one marker, I was busier through the pandemic than at anytime before that.
- Now if you look at the medium sized to bigger deals, the data I see says deal activity is down overall this year compared to 2021.
- My feeling is that valuations may drop a little but deals will still get done.
- It is important to note most of the smaller deals in the security industry are done by strategic buyers that don't rely on bank financing as much. So these deals will go on.
- The dynamics of smaller deals (\$750,000 to \$3-4 million in purchase price) is quite different from medium to larger deals (\$5-50 million in purchase price) .
- I have not noticed buyers backing away from deals that I am working on which are mainly both alarm account and guard company deals.
- As mentioned above, I am now seeing buyers asking about the people component contained in the target they are looking at buying. They want the staff almost as much as the rest of the company.
- I actually expect to see more owners decide to sell because they just don't want to face another year of inflation, and material and labour shortages.
- In summary if owned a security company today, I would:
 - Not hesitate to put it on the market if you were showing good financial results.
 - Expect the selling process to take a little longer than normal.

ABOUT HARDING SECURITY SERVICES INC.

Harding Security Services Inc (HSSI) was formed by Victor Harding in 2009 to provide certain consulting services to the security industry. The two areas that HSSI specializes in are acquisitions and valuations of security companies.

Regarding its acquisition work, HSSI acts as an intermediary to help owners buy and sell security assets. HSSI acts for buyers and sellers and is paid fees mainly when a transaction is done. HSSI builds on Victor Harding's more than 12 years experience in Canada buying alarm companies for two of the national companies there.

HSSI also provides valuation services to owners of security companies particularly those that have significant amounts of recurring monthly revenue.

Victor Harding lives and works out of Toronto, Canada, is a chartered accountant by training and had many years of both small and large company business experience in financial, sales and consulting roles before owning his own security company for several years. HSSI does work across Canada and the United States.

Visit us on the web: www.hardingsecurity.ca

