Organic growth ...
not always the safest or most effective strategy

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Frequently, owner operators of small- to medium-sized companies are asked:
"How do you run your business today?"
Most answer: "We try to keep costs low and work hard to increase turnover."

The question that remains of course, is:
"What is the best strategy to accomplish this?"
Most medium-sized businesses envisage growth as an organic process. The emphasis on growing profits by increasing sales is common sense. However, for most businesses, this is easier said than done.

Why?
Because increasing sales usually means spending money upfront - either by opening more branches, hiring more staff or spending more on capital investment, advertising or product promotion.
This approach always results in sleepless nights and much hand-wringing without a guarantee of an adequate return. As a result, steps taken to achieve this strategy are small. Sales people are employed and evaluated one at a time before the next new hiring is considered. A new branch is opened only when the existing ones are profitable. Research and development expenditure are increased during boom years but not bust.

Sometimes (many times), things don't work out. Sales staff require time to become effective in new positions. Many (in my experience, over half) never reach an adequate level of success and leave their employer with a net financial loss.
New branches may never achieve enough turnover to be profitable and eventual closures always bring high extraordinary costs.
Advertising costs can also easily spiral upwards without a quantifiable return being established.

In short, organic growth is risky and expensive.
Yet, this fundamental strategy is the most common seen throughout the fire and security industry today.

Why?
Because it is the easiest to implement. *It is not, however, the safest or most effective.*

In truth, the most efficient and profitable way to grow any business is by purchasing bolt-on operations that complement your existing structure.

This simple truth applies to any size of business you run.
You see, the purchase of any operation that has a well-defined customer base enables you to minimise capital investment risk.
Minimising that risk is the driving force behind successful business growth, because in the long run it will lead to a steady, profitable increase in the size and value of your company.

Ask yourself, what is the probability of achieving an after-tax return greater than your cost of borrowing on every incremental Pound/Euro/Dollar you invest in your existing operations?
If your response is less than certain, you should consider growth through acquisition!

When considering the maximum price, you are prepared to pay for an acquisition, you should estimate the savings you may achieve in integrating these new operations with your existing business. If these savings,
plus, the existing ongoing profitability of the new business outweigh your debt service costs, you are off to the right start.

Usually, the potential vendor will not attempt to estimate your own savings on integration. Therefore, his asking price will be based on the return he would expect to achieve from a risk-free investment.
As a basic example, consider this: a vendor looking to cash out on a service business generating £100,000 annual pre-tax profit on a regular basis will expect about a 10 per cent return on his investment This
yields an asking price of about £1-million. If your borrowing costs are 15 per cent, you will need to generate an annual savings of £50,000 to cover the shortfall. If this seems realistic, ask yourself what the chances are of achieving break-even by investing the same level of funds into capital equipment or marketing? Where are your chances of future profitability growth higher? The build or buy decision is not always straightforward, but more often than not, the answer is ‘BUY’.

Why is that exactly?
Primarily because in today's market, the banking collateral from a stable historical earnings flow is better

quality than what you can achieve from hard assets. With over-supply in most industries, new fixed assets will not only depreciate in the long term, they will also be worth only a fraction of what you pay for
them immediately upon taking delivery. In any case, you can't use marketing costs or the expense of hiring and training new employees as collateral for your bank manager.

Does all of this seem like more trouble than it's worth?
Many business owners do.
They are content to sail steadily on, happy to subscribe to the motto that "you shouldn't stick your neck out if you don't have to."
However, consider this. *A business not in expansion mode is a business vulnerable to derailment.*
Factors such as product obsolescence, over-reliance on one individual customer, or eventually the health and energy of the owner, are all eventual threats to a company that doesn't bring in new blood, or new ideas, on a regular basis.
In such cases, it is better to consider an appropriate exit strategy when times are good and the profitability of an operation stable, rather than attempting to salvage an acceptable asking price once the business
is in financial decline.

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