



Session 4

BUILDING YOUR WEALTH

Peter Smith, Adrians



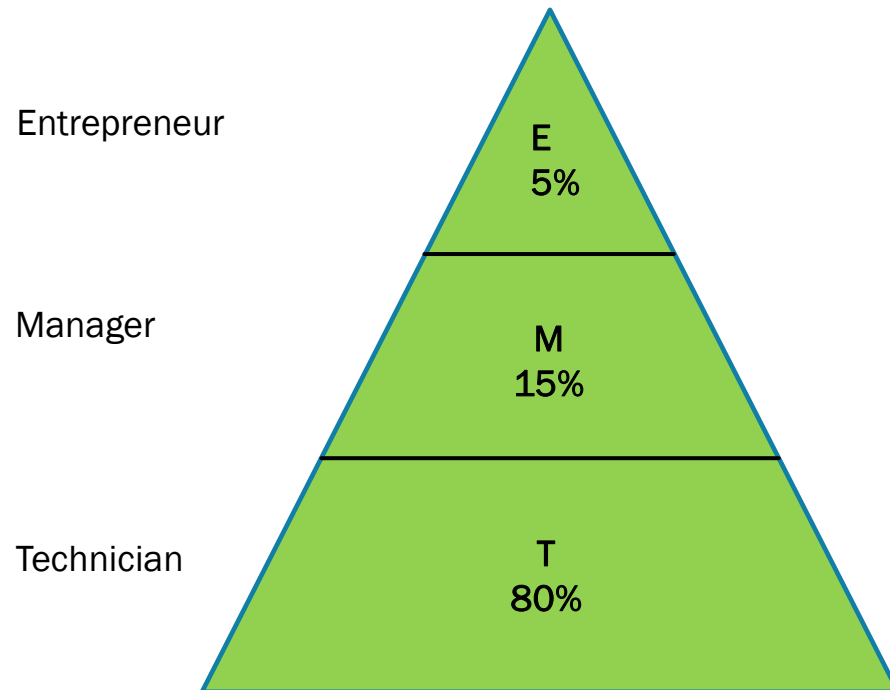
IMA CONFERENCE

PETER SMITH

THE CHALLENGE OF WEARING 3 HATS IN AN SME (E-MYTH, MICHAEL GERBER)

An **Entrepreneur** changes the business. A **Manager** runs the business. A **Technician** masters their craft.

Any successful businesses (business, not job) allocate focus and resource to the 3



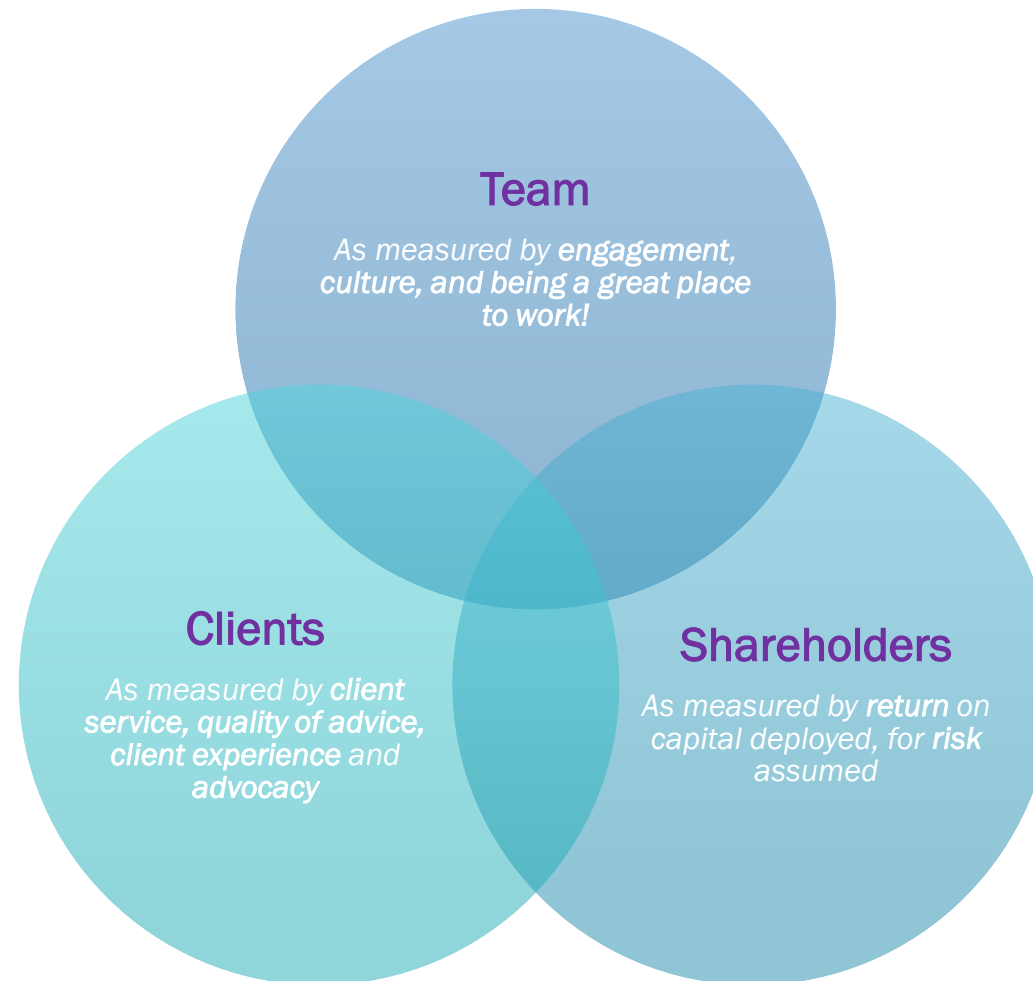
When you are playing the role of the Entrepreneur, you are finding **new ways to do things**, or thinking of new ideas to make happen, and focussing on **designing** and **executing** the **Value Creation plan**

As the Manager, you are figuring out **ways to optimize policies, processes, and procedures** and build a stable operating environment for the business to thrive

When you are playing the role of the Technician, you are focused on **better techniques** and technical implementation – the “how” – while you are mastering your craft

To build an **outstanding, high value** business the best firms a) *recognize this*, and b) *address this*

Everything we do in our business must **satisfy *all* stakeholders**



BACKING A LONG-TERM BUSINESS >>> 3 ESSENTIAL TESTS

MOAT

Is the economic moat wide and not easy to replicate? How robust is the competitive advantage?



MARKET

If the moat is wide, and the competitive advantage is strong - how big is the economic pool, and is it a 'winner takes most' dynamic?



EXECUTION

If the moat is wide, and the market is large with powerful economics - are the people skilled enough to execute?



Best Practice Strategy Framework

Structured process >> To be successful must start at top and work down – often occurs back to front...

1. STRATEGY

2. STRUCTURE

3. PROCESSES

4. PEOPLE & EXECUTION

As Leaders of the firm we all own the delivery of this

As a leadership group responsible for strategy formulation and execution we need to continually be asking these questions >> then pivoting or refining on a dynamic basis

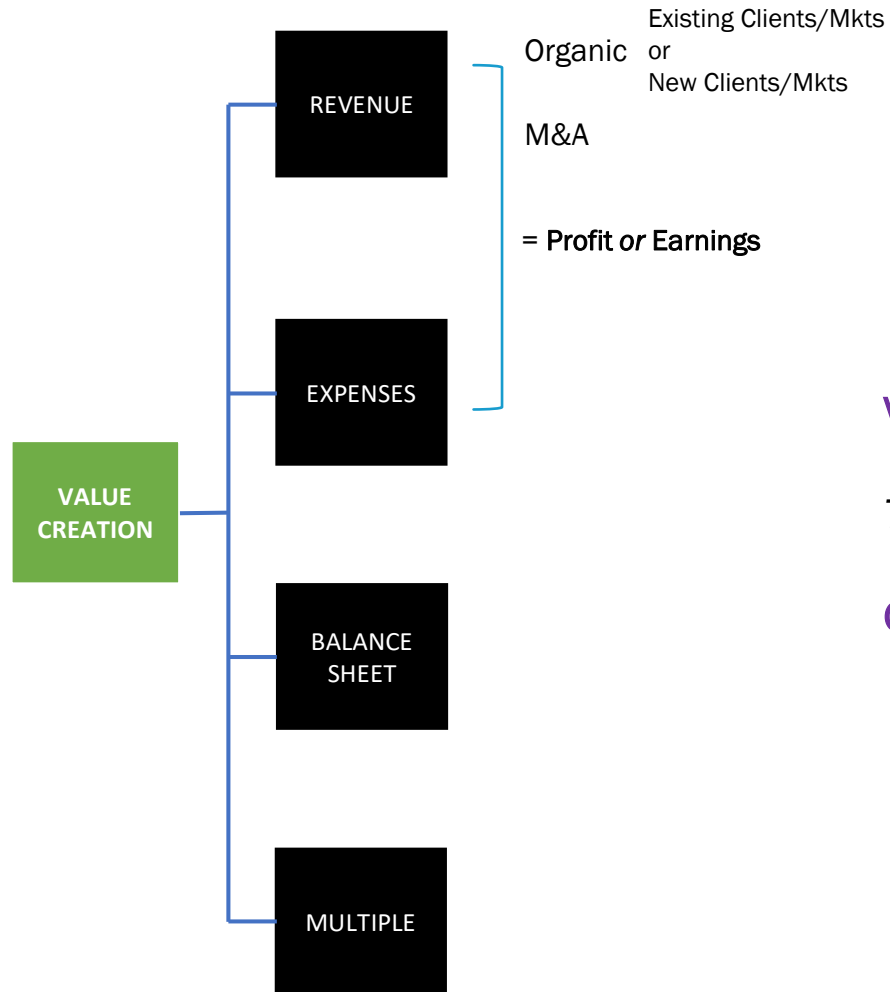
- Do we have a clear and sensible strategy?
- Do we have the ability to execute and are we measuring execution?
- Is it good for all stakeholders - Team, Clients, and Shareholders?

- Do we have a sensibly designed operating model and organisational model?
- Does it enable the delivery of the strategy now and into future (ie. is it scalable?)
- Does it facilitate a performance management and accountability culture?

- Do we have a single set of processes within the structure (one way/same way)?
- Does the single process ensure work flows through the system optimally?
- Are the single set of processes underpinned by a strong and scalable tech stack?

- Do we have enough people in the structure to allow us to execute the strategy?
- Are they the right people, and are they in the right seats?
- Are they skilled and are we developing them so they can carry out their role well?

Value Creation Plan - Value is a function of 4 controllable levers



Most common valuation methodology
= Capitalisation of Future Maintainable Earnings

$$\text{Value} = \text{Multiple} \times \text{Earnings} + \text{Net Balance Sheet}$$

Therefore...

$$\text{Goal} = \text{M Expansion} \ \& \ \text{E Expansion} \ \& \ \text{Strong Capital Management}$$

“Simplicity is the ultimate sophistication”

Leonardo da Vinci

THE VCP TO BUILD ENTERPRISE VALUE INVOLVES A STRUCTURED PLAN TO DRIVE EXPANSION ACROSS THE KEY VALUE DRIVERS



Multiple Expansion

X

Initiatives to improve the business model and show an EPS growth runway

Multiple Expansion Drivers

1. Scalable Infrastructure
2. Well structured entity map, organisational structure, and operating model
3. Disciplined Governance, Oversight
4. Client Engagement
5. Scale and liquidity
6. Human Capital Framework
7. Revenue Footprint
8. Growth Runway

Earnings Expansion

+/-

Initiatives to drive sustainable profit growth

Earnings Expansion Drivers

1. Organic Growth in revenue driven by expanding services and products to **existing clients (zoo)**
2. Organic Growth in revenue driven by the onboarding of **new clients** driven by BD and strategic marketing activity (jungle)
3. Organic Growth driven by **expanding profit margins** through repricing services
4. **Strategic M&A** opportunities assessed and executed in a upon when clear they are value accretive
5. **Operational Leverage** driven by using scale to increase operating margins (ie re-pricing supplier arrangements, driving down unit costs etc)
6. Critically assessing the **cost base** to drive down expenses where appropriate without impacting the businesses operating model
7. Development of a highly functioning **marketing** and business development operation to drive business growth
8. Embedding a culture of Customer **referrals** through the customer experience - > endorsements -> advocacy

Balance Sheet

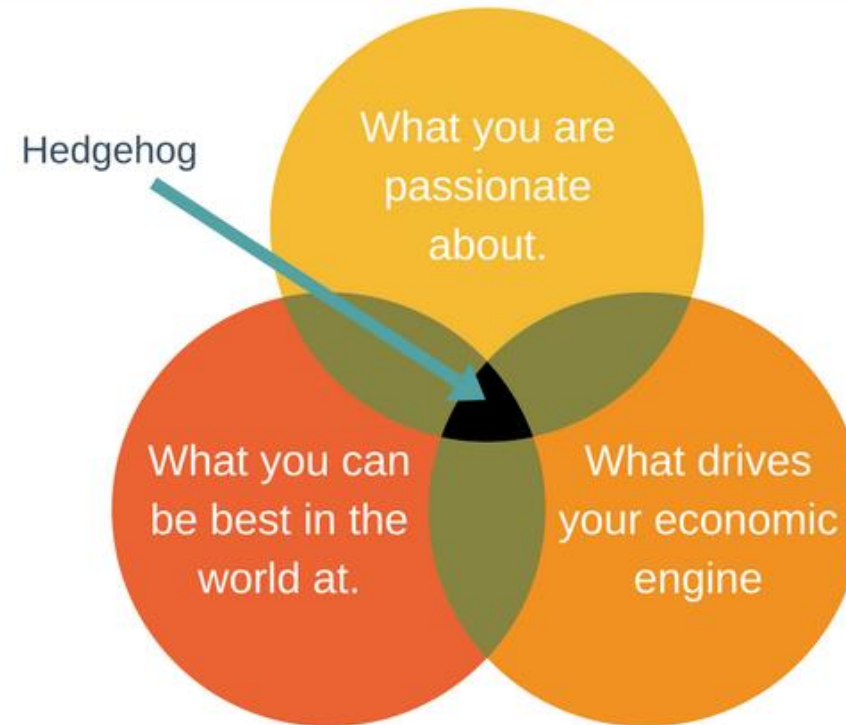
Initiatives to strengthen the balance sheet

Capital Management Drivers

1. **Working Capital Management**
2. **Cashflow Management**
3. **Strategic Financier Relationship Management**
4. Internal **Covenant management** to ensure working to best practice ratios
5. **Debt Amortisation Schedule modelling** to ensure capacity for succession planning, growth and minimal EV impact
6. **Cost of Capital** dynamic measurement and management
7. **Lock-Up Optimisation** – rigid focus on cash conversion cycle (CCC)
8. **Modelling and Management of Debt / Equity** mix in Capital structure to fund growth

The 2 biggest execution risks - Expertise and Focus

The Hedgehog Concept



Jim Collins, "Good to Great"

Vision without ***Action*** is merely a dream.

Action without ***Vision*** is a nightmare.

Vision *with* ***Action*** can change the world...

Japanese Proverb