The Art of Selling Your Business with John Warrillow

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John Warrillow

James: James Schramko here, welcome back to SuperFastBusiness.com. Today, I'm delighted to bring back a guest we've had in the past, John Warrillow, welcome.

John: Thanks, man. Good to be back.

James: Great to have you. It's been a while, we'll cover that in a second. This is Episode 797 of SuperFastBusiness. And we are going to be talking about the art of selling your business, which is, coincidentally, the title of your recent book, which I've had a foreward copy of and been immensely enjoying reading.

John: Oh, good.

James: Yeah, terrific book, it really hits home some great information that I wish I had when I had sold some of my businesses. I could really relate to it, and I'm also involved in helping a lot of people sell their business. So it's going to become a great resource for me, as were your previous books.

Catching up with John

So quick recap, you've been running the Value Builder System, which helps business owners increase the sale price of their business. Last time we spoke, which is over five years ago, I think you'd had about 14,000 people through that. These days, you've probably had more like 55,000 people go through that.

And you've been helping companies increase their value by 71 percent, which is nothing to sneeze at. You wrote Built to Sell, which I love that book, it was such a good book, creating a business that can thrive without you. That was voted one of the best books by Fortune and Inc. Magazine in 2011, and then translated into 12 languages. So it's really a fundamental book. I think everyone listening to this podcast needs to have a library of Warrillow books, especially Built to Sell.

Of course, my favorite one after that was your Automatic Customer: Creating a Subscription Business in Any Industry. That has been like a textbook for me, because I work with so many recurring subscription business owners. Most of the memberships that we're doing are subscription business; that interview that we did about that book led to me having more discussions with people who I think, we even introduced you to Robbie Kellman Baxter.

John: Yeah. I just talked to Robbie today, actually, it's funny you mentioned.

James: Right. So our podcast was Episode 368, worth a listen; if you're listening to this and haven't listened to 368; that was back in March 2015. Shortly after that, you asked me where I learned about podcasting, because you quite enjoyed coming onto the show and talking about it, and you were considering hosting your own podcast.

Of course, we know that happened. I sent you across to a Noah Kagan post I did on how to get all the downloads and what to do, and then I sent you a bunch of strategies on getting guests, and even stuff on SOPs on how we do our tweetables. But, of course, you launched Built to Sell Radio, and Built to Sell Radio, you've interviewed hundreds of people, I think 250 at least, on their exits.

So you went from that podcast to having your own podcast, to creating a rich resource library that has now turned into the book that we're going to be talking about today. And your current podcast is ranked in the top 10 podcasts for business owners by Forbes. So well done on that.

John: Well, thank you. I've got you to thank.

James: Well, you know, I couldn't have done it without you. But of course, you know, I'm being cheeky there. You're always going to rise to the top with such a strong book following and immense amount of business you're doing with the Value Builder System.

Why half of business owners want out in five years

So what I want to talk about is the art of selling your business. It's something you've identified, that half of business owners are looking to exit in the next five years. Do you want to tell me about that kind of research, and if you were surprised by that?

John: Yeah, I mean, I don't know what's going on right now, in the pandemic where you are. I think you've got through a real tough period, and now it seems to be better. Would that be fair to say?

James: In Australia, I'd say, we're in very good shape. We pretty much eradicated it. It's partly because we're an island, partly because we don't have an unhinged lunatic running the country. We're good at doing what we're told for the most part. And I think that sort of speaks to the Aussie spirit, you know, just doing what we need to do, and I think we got into it nice and early.

We had good protocols early. And thankfully, I mean, our economy, there's obviously going to be a hit to some businesses, a lot of retail businesses, you know, you can see some shops are going under, but what's happened here is the government is very supportive. They're giving an allowance to employers to keep running. So I think they recognize they've got to keep the business running.

There'll probably be a hangover effect, you know, next year, but they'll roll out vaccines, and I think things will get back. But for the most part, we've actually had less deaths all up from this pandemic than what the United States would see in half a day. And we have, I think, you know, society itself is good, like, there's no masks, everyone's able to go and do what they need to do.

If you want to get married, or you want guests in your restaurant, that's all happening. It's like, you know, I'm at the beach surfing every day. So I think, you know, we really are the lucky country. And I've obviously connected with people all around the world, and I know right now, people are having really dire situation. But almost certainly, the business landscape has shifted. It caused me to change my own business model this year, to cater for the adjusting economy.

So it's been, I think, one of the greatest opportunities for responsive business owners who are paying attention, and there will continue to be enormous opportunities over the next few years, because I don't think we'll go back to the way things were. There'll be a new way. But almost certainly, I would expect your library of books would have been essential reading lately, especially subscription businesses, because that's what gives you the recurring safety net of time and the ability to adjust.

In terms of buying businesses, I'm sure there'll be plenty of opportunities where people have just had enough, and I think it'd be worth us going into the reasons someone would sell the business. Probably when you were writing the book, pandemic wasn't right up there. But I think some people, you know, some people would just be fatigued right now or just strung out. And maybe they can't wait until the recovery.

John: Yeah, you're absolutely right. So I'm in Toronto, which is right next to the United States, but we're in Canada. So our situation is slightly different. But I think we've got some of the same dynamics going on. And when we look at the research we've had, again, as you say, 55,000 businesses go through Value Builder, we looked at and just pulled the data set of folks who, about eight months prior to the pandemic, completed our initial intake questionnaire.

And then during eight months of the pandemic, we looked and compared the two. And what we discovered was that, first of all, business owners are very pessimistic right now, a lot of them expect their sales to be down. But more interestingly, as it relates to the sale of their company, business owners have pulled forward their sell-by date by 20 percent, meaning a much higher proportion are now planning to sell.

And the other thing that's interesting, James - you know, I'm not sure how it is in Australia - traditionally, 100 years ago, in Canada, certainly, the first son would inherit the business from the Father. I mean, it's such a sexist thing to say. But that's just the way it was 100 years ago, right? And so passing businesses down through family transition was the way businesses were passed on. Well, that's obviously changed.

But when we look at the data of the United States, we discovered, as a result of the pandemic, the idea of passing your business to your kids has dropped through the floor. Very few people want to do it. And in lockstep, the proportion who want to sell to a third party has gone up.

And our thinking or hypothesis is just that running a business has been so stressful in the United States that the idea of continuing to pass that on to your kids is just a non-starter. And so we're seeing a high degree of interest in selling, lots of folks who wish they had sold in 2019 and don't want to make the same mistake again, in 2021.

James: Like that billionaire who bought a company out of spite, and then it collapsed, just as the pandemic came. It was like, the worst timing ever. Some people would have had a really bad run, maybe just bought a business or just exited a business; they could have been extra lucky, or extra unlucky, compared to normal.

I was smiling a bit when you were talking about generational businesses being handed down, because I came from the automotive industry. And notoriously, there's a lot of second or third generation motor dealers. And they're lucky they got the land, and that's the only reason there's any wealth in the business.

The average motor dealership in Australia makes about two percent profit, and a lot of the children are not running the business with the same fortitude that the first generation had because, you know, usually the first generation did something special or worked extra hard or had good timing and did something. And then the second generation sort of rides the coattails, and then usually the third generation has to get a wake up slap to the face, or they get bought out by a multinational.

So I think it's interesting with my own kids just to see how most of them are not following in my own footsteps and are doing their own things. So certainly, you know, maybe in Australia, it's not quite the same. Who knows? Let's talk about, what do we need to think about before we sell our business? Because you've got a whole section on that before you start, and I thought that was quite interesting.

The factors that push and pull

John: Yeah, you know, I mean, the first thing I think we need to think about is, what are you going to go do next? And we talk about pull and push factors. So push factors are things that frustrate you about your company, you know, like red tape, employees that don't do what you say, and all that stuff, those are push factors, right?

And then there are the pull factors that are things you're excited to go do - learn to surf, you know, write a book, start a podcast. It doesn't really matter what they are, what we've learned is that the people with more pull factors are much happier with the result of their sale than those with all push factors.

And what's interesting, James, is it doesn't really matter what they sell the business for. In the book, I talk about a guy who sold a company for between two and three times profit. And, you know, I asked him about his exit. And, you know, it was a fine sale, and it gave him some money, and I said, like, "Why are you so happy?" And he said, "You know, when I was 30, I decided by the time I was 40, I wanted to live on a sailboat. And that was on my vision board."

And so he spent 10 years, build a business up, on his 39th birthday, he engaged an M&A guy to sell his company, got two to three times SDE or profit, and sold it. And now, he lives on a sailboat. That's what I'm talking about when I talk about pull factors, meaning he was so fixated on this idea of living on a sailboat that, you know, selling for a relatively modest multiple was fine with him. And so I think even before you'd start all the technical mechanics of selling a company, thinking through what are your pull factors is definitely worth doing.

James: That is interesting. As a coach, I'm hearing a lot of these stories. I've got one guy I'm coaching at the moment, who came to me, absolutely fed up with his business. He's an influencer, he has a lot of followers, he built a substantial multimillion dollar revenue. And then he's getting all these hits, you know, difficulties with staff, difficulties with the business model not quite working as well. It's just like, it just pushed him down, and he just wanted to actually kill the business.

He got to the point where he just wanted to switch it off. And I said to him, and, you know, partly inspired by having had an advanced copy to your book, it was in my mind, like, why wouldn't you just ramp it up and get rid of it, and then at least, you're capturing the value for all the stuff you've put in, in the past?

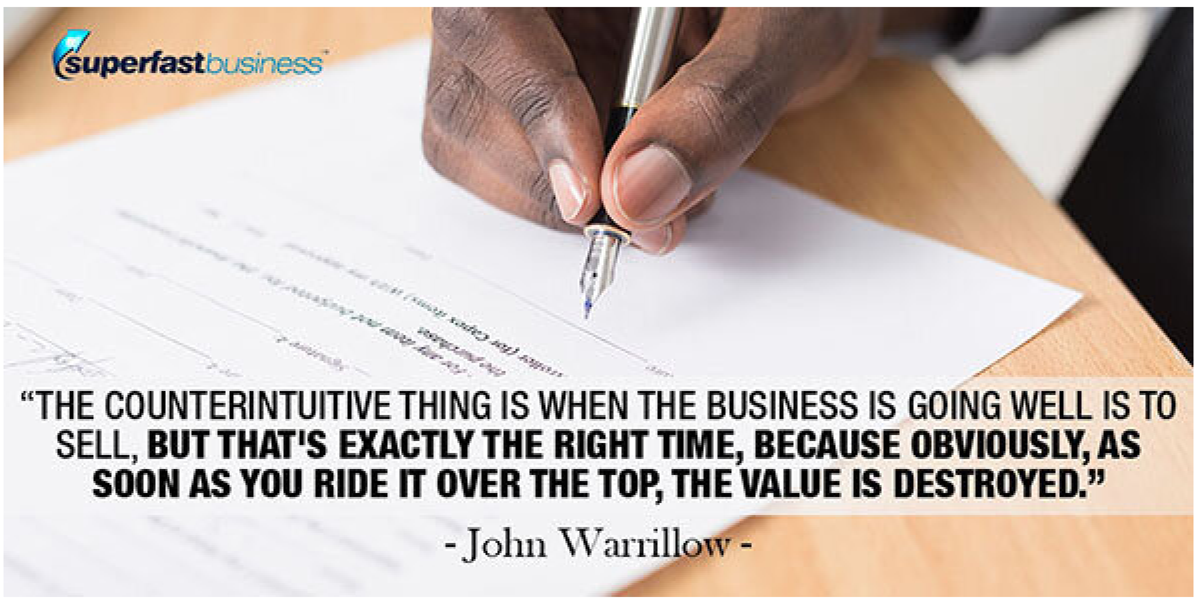
And in the space of just two months, we've switched that sort of, all those hot buttons, all the things that were making the angst, we've just flipped them on their head, changed the business model, changed the attitude about it, and he's flying. But I also have a feeling now that the business is actually going to excite him enough to keep in its new version. And there seems to be this sort of knife's edge of a business that you hate so much, you want to sell.

Generally, people let it run down and get a lower value for it. And the business that you actually love is probably one you want to keep. So if they do a good enough job of restoring it, for selling it - because I don't think he's thinking about a boat, living on a boat. I think he's just thinking about how much he hated that business. But if he falls back in love with it, he can have a second romance with this business. And I think it can really shoot well past where it was before.

Have you ever seen a near sale get turned around like that?

John: Yes, for sure. And here's the challenge that I would put on a table. It's something called the freedom point; and the freedom point's, you can calculate it for yourself, which is when the sale of your company, after tax and after you pay your broker, your M&A professional, would create a nest egg large enough that you could do whatever you want, whenever you want to, effectively, true financial freedom.

The question becomes, why keep the business? And you could say, 'Well, it gives me intrinsic enjoyment. I'm fulfilling a mission or a vision that I'm excited about.' All those things are absolutely genuine. But at least asking yourself the question, because every day that you own a business that would effectively fund your lifestyle for the rest of your life, you are like a gambler at the poker table, just putting the chips all in the center.



And that's okay, totally fine, but do it with knowledge that that's what you're doing, because you never know when the next pandemic is around the corner. And as good as it's going now for your friend and your client, you never know what's going to come around the bend. And so, you're absolutely right. The counterintuitive thing is when the business is going well is to sell, but that's exactly the right time, because obviously, as soon as you ride it over the top, the value is destroyed.

And so I just encourage people to think about the freedom point. And you can calculate it, by the way, if you figure out how much income you need to live the life you want, let's just say it's 100 grand, if you want to be conservative, multiply it by 33, to get to 3.3 million. If you want to be a little bit more risky, multiply by 25, and that corresponds with a four percent withdrawal rate, and that's essentially the nest egg you need to create.

And once your business is worth that, it's just tempting. It's worth, I think, asking yourself, why am I continuing to do what I'm doing?

James: Have you been tempted to sell the Value Builder System?

John: I have. We've had offers. And yeah, look, I've gone through four exits. And, you know, I guess, this business is not my entire network, so to speak. So I feel like I am able to do the things I want to do, irrespective of whether I ever sell Value Builder. So it's a little bit more of a passion business for me.

If it gets to the point where it's 50, 60, 70 percent of my net worth, then yeah, you can bet that I'm having that conversation about, this is a lot of risk on. You know, traders talk about this idea of being risk on. It means that basically, you're taking a disproportionately high degree of risk. And when your business is worth a big part of your net worth, it does beg the question, is it time to diversify? You know, we all do it in the stock market. Why wouldn't we do with our private businesses?

James: Yeah, I think that's the perfect answer. It really explains a lot about my own approach to business. I think I could have a much bigger business and a more saleable business than the one I've got. But since I've been more heavily focused on building licensing revenue and royalty income on a subscription basis, to some extent, I'm living the life I want to live now as well, and it wouldn't make that much difference.

When $10 million revenue is the goal

I mean, I only work three days a week now, and I still get to surf every day. So I've actually started buying my time back for me, instead of sinking it into, you know, a 100-hour week to build some massive enterprise. I deal with a lot of people, when they arrive to coaching, especially younger people, they have this blazing vision of making a $10 million revenue. That's like, it's probably the 90-something percent answer on their goals. They want a 10 million plus revenue business, very common seed that gets planted there.

Do you think that's a realistic goal for the majority of people that are in our field? Or do you think maybe they haven't given enough thought to what they're actually trying to do yet?

John: Well, you know, the old expression, revenue is vanity, right? So I think it's very, very common, right, for us to have some sort of external measure of success, and a $10 million revenue business is as good a number as any that you want to chase. You know, I would encourage anybody to think about why that's an important number for them, and what that will do for them, because a $10 million business that's got three clients that represent 80 percent of the revenue is largely a worthless business.

You might get a bit of money for it on an earn out, or you've got some scheme that enables you to get revenue or some payout for the business years in the future. But if the company is dependent on one or two clients to get there, it's virtually a worthless business. Equally, if the company is just really basically just reselling someone else's product, where you don't have ownership of the brand, you don't have control, it's a commoditized product, nobody's going to buy that business.

If you've got a $10 million business that's in a highly commoditized category, think about people who are these days selling masks, right, or PPE? Every manufacturer said, "Oh, we're going to do PPE."

James: That's a fad, right? Where is that going to be in three years from now?

John: Yeah. It's not only a fad, but it's also, think about it, if you're in an acquirer's shoes, and you're looking at a business that is very highly commoditized, in other words, tiny, tiny movements on the price change by behavior; if that's the case, then they're going to say, "We don't need to buy this $10 million company, we can just drop our price by three points, and essentially pick up all of their business. So we're not going to buy it, we'll just compete with it."

And they make that decision behind closed doors. You're not in the room for that decision, right? They make that decision, the buy-versus-build decision, without you there. And if you've got a commodity product that you're effectively reselling, or you don't control, your business is largely worthless. And so again, I'm all about value, right?

I just did a podcast with a guy named Rob Wall, who started a company called Drip. Do you know Drip?

James: I know Rob Wall. I think we're in a similar community.

John: So Rob built his company up to $2 million of ARR, Annual Recurring Revenue, when he reached the freedom point. And he thought, if I sell this company, given the speed at which he was growing, his negative churn rate, he could literally get between nine, well he wanted to get, his aspiration was to get between nine and 14 times, not profit, but revenue. So just do the math on that. And so he decided to sell the company and he had an incredible exit. It's a $2 million business.

James: It's amazing.

John: it's worth infinitely more than a lot of $10 million businesses. So I would, just to go back to your point around, oh, I want to hit a $10 million business; that's vanity talking, that's ego talking. It's not necessarily what will make you happy or make you successful. I would argue that Rob, having built a $2 million business, is wildly more successful than someone selling PPE with a $10 million turnover.

James: That's like he's put all the chips on red, and it's come up red, and he probably should walk away from the table.

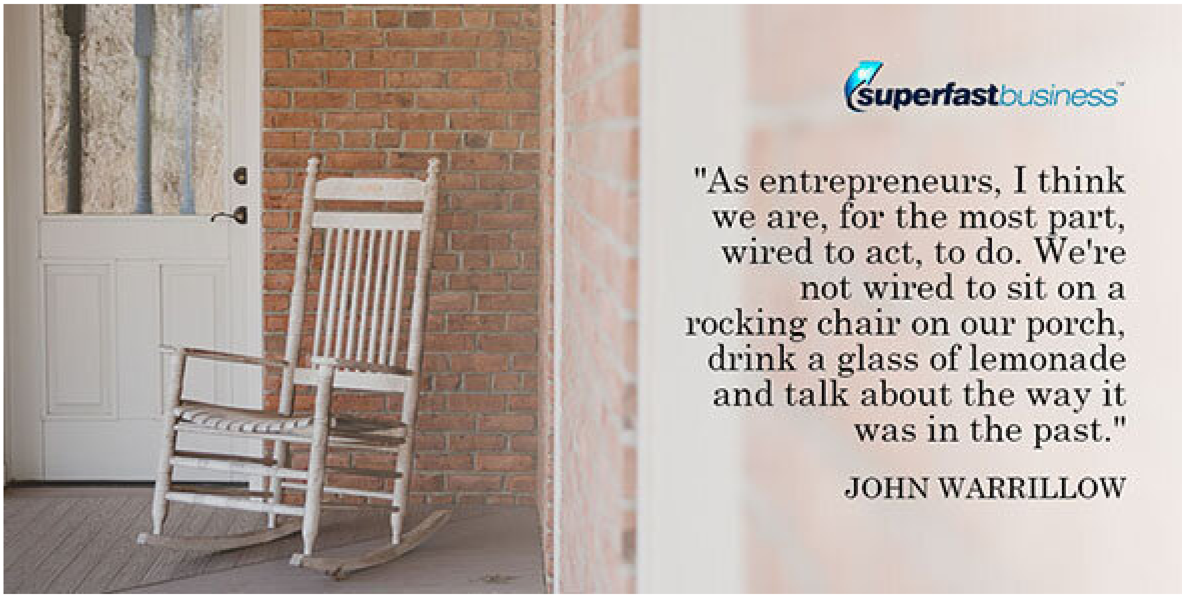
John: Yeah.

James: I'd take that deal. Like, someone gave me $20 million, they can have SuperFastBusiness. And I'll just surf more, I think that's fine. It sort of speaks to your point in chapter two, you sort of cover happy exit. And the mindset around this, it really reminds me of Maxwell Maltz with Psycho Cybernetics, who really is the foundational book on self help, when he realized he would plastic surgery someone and they'd still be unhappy.

So someone could sell their business and still be unhappy. And I think the $10 million thing, it speaks to your point where you say that a lot of people have their identity tied to the business, and that's who they are, and then they sell the business. It's like they're just collapsed, their soul is empty, because they've just basically sold themself out of it. They haven't detached from the business being a separate thing to themselves.

What you want, what you're doing, and when to let go

John: Absolutely, yeah. And it's all about, I mean, there's four steps to doing that. But the first that I think most important is figuring out your pull factors. I mean, if you were excited to go start another company, build a charity, write a book, I mean, you're going to sink your teeth into that, right?



As entrepreneurs, I think we are, for the most part, wired to act, to do. We're not wired to sit on a rocking chair on our porch, drink a glass of lemonade and talk about the way it was in the past. Like, if that's your vision, that's not going to be happy.

James: That is almost the literal definition of retirement for society. It's this notion that you will slave away in someone's business until age 65, depending on the country you're in, and then you stop. It's like, stop, you've got money now and your superannuation or your 401 or whatever you want to call it. And then you just, you know, live out the next 20, 30 years in a retirement home.

John: It sounds terrible.

James: Well, certainly in Western society. You know, some cultures don't even have retirement homes, which is interesting. They just live with the kids. But I think, you know, my grandfather, who was a timber broker, right up until he passed away, you know, he had this little shed in his backyard, and he would buy and sell timber, and he made a three percent brokerage, and he loved it. He absolutely loved it. It gave him a lot of purpose, and it was his hobby.

So I think this balance between what you want to do and what you're actually doing, and then where the point to let go is, is an interesting one. You suggest the vision board. Actually, Maxwell Maltz used to talk about, you know, doing visualization. That seems like a great idea, is to spend time thinking about what you want your life to look like, and then articulating your business to be a vehicle to get you there.

It's kind of like the rocket ship to Mars. If you want to live on Mars, you need your rocket ship, and building your business and then selling it could be the ticket there.

John: Absolutely, I mean, it gives you the ultimate freedom, right? So once you get that first run on Maslow's hierarchy of needs, and you've got your shelter and your foods taken care of by creating enough wealth that your business can basically fund your basic needs, it gives you a run that people can't take you off, right?

Beware of writing it off too long

I can think of examples of people I've interviewed for the show who wrote it off too long. They basically said, "Oh, I'll sell..." Have you had Rand Fishkin on the show, you know, Rand?

James: I haven't, but I've followed his story. I read about it in the book, and it sounds pretty tragic. You know, like, I never even understood his position, you know, when he was in the business, and he had great stuff like the Whiteboard Fridays and stuff. And then I could see it starting to go pear-shaped. And I thought, 'Oh, this is not good. It's not good.'

John: No. So look, if you haven't heard the story, I've interviewed him on Built to Sell Radio. He's got a great book, you mentioned you picked it up. It's called Lost and Founder, certainly worth the read. I'll give you the short story. Basically, as he described it to me, he built Moz, which is an SEO software, up to around $5 million in revenue, got an offer from Mark Halligan who built HubSpot. And Mark offered him 25 million bucks, about five times ARR.

Rand said, "Nah that's not enough, I want four times future revenue." He thought he was going to hit 10 million, your number. And he thought he was going to get there that year. So he said he wanted 40. Halligan said, "No, can't do it." And they parted ways.

Well Rand, instead of being sold to HubSpot, raised a bunch of capital, built a bunch of different businesses, different products, and in his own admission, started to get distracted. Ultimately fell into a state of depression, was removed from the board of his company, not the board, as CEO of his company, and the venture capitalists who invested in his business had what's called preferred shares, which essentially guaranteed a preferred return to them, before Rand gets a penny, in the event of a sale.

And because they've held it for so long, that has just gone up and up and up. And I asked Rand, you know, like, how is this going to work out for you? And he's like, I don't know if my shares are really worth anything anymore, just given the preferred shares. And I said, "Oh, that must feel terrible."

And he said, "Yeah. Well, I mean, like, what's worse is my entire net worth is $800,000, much of which I'm about to spend on elder care for my grandparents." And I said, "Rand, what would that offer be worth today? Because HubSpot stock has gone through the roof, and it was a cash and stock deal," and he said, "It would likely be worth north of $200 million."

James: Yeah.

John: That's riding it over the top, right?

James: It reminds me of my friend who's lost his bitcoin wallet.

John: Yeah, in Toronto, it's all about cannabis. Everybody has like, lost their shirt in cannabis. Everybody thought cannabis was going to be the license to print money. And, of course, it's all bombs fallen and all of that. But anyways, it's a good reminder that no matter how good your business is, how successful you are, blah, blah, blah, the best time to sell your company is when someone's buying. And when a guy like Mark Halligan shows up and says, "I want to buy your business," it's time to take notice.

James: Ah, look, I'd sell it in a minute. You know, like, I think for me, going through that process of selling my businesses was critical, especially as a business coach. I needed to put that chapter in my experience, and I needed to understand the psychology behind it. I needed to educate myself on deal structure. I needed to handle things like transitioning the team, the customers, moving on from that and rebuilding.

Funny thing is, my business now actually makes more profit than when I had a lot more team and more business units, because I was able to really harness that extra inspiration and energy and capitalize on the experience. And of course, you know, publish my own book and so forth. So I think it's a great thing to go through, but hopefully on the right side of it and not the Rand Fishkin way.

John: Yeah, yeah.

James: Should we have a look at some of the things that a buyer is going to look for? You mentioned a few in the book, I thought they were terrific, and one of them, I think, will be really interesting to ask you about. Obviously, growth is a big one, the current growth rate and the projected growth; recurring income, I feel like we've covered that a lot. Anyone listening to this podcast knows a lot about recurring income. That's a huge plus.

How much personal involvement should you have?

Standard marketing stuff. It's got to have a differentiated product or service. It can't just be some commoditized, like facemask. But personal involvement. That's one that I think is really interesting. I've seen a lot of articles, pro and con, against building an authority or not. Like, I wouldn't have heard of your business without John Warrillow.

What do you think is the right approach here? And you know, even the great Claude Hopkins, in his original marketing book said that wherever possible, they'll lend a name or a celebrity or you know, a person to a brand to increase, you know, the conversions, pretty much without fail, if you personalize it. It actually starts to differentiate. But it can also be harder to sell. So I'd love you to speak to that topic.

John: Yeah, it's a delicate line for sure. Because most CEOs are their number one salesperson, right? You think of Elon Musk and Tesla, I mean, you know, what would Tesla be without Elon Musk?

James: Steve Jobs, Bill Gates.

John: Steve Jobs, Warren Buffett, Bill Gates, I mean, you could go down the list. Somehow, you have to proactively transfer that equity that you have in your name to the company, and it's easier said than done. Bill Gates is a great example. I mean, Bill Gates has had a much more significant, in many ways, career after selling or leaving Microsoft than he had before in Microsoft.

But he focused on the products in the business, and tried to have that sort of halo effect accrue to the business, not necessarily him personally. And so, you know, there's lots of things that you can do to make that case. First of all, making a clear line between your company and your name. So, just because you have your name in the company, that doesn't necessarily mean you can't sell it, but it's more difficult.

So, you know, if you think of Johnson & Johnson, as an example, like, that's a sellable, valuable company. And yet, it's still two brothers, its namesake. So you can do it, but you want to focus and invest in the brands that you're building. So in Johnson & Johnson's case, they own Band Aid, as an example. So they built up the products. In Microsoft's case, it was the products, etc.

So look, I think you can be your company's best asset. Again, I would point to Elon Musk in that way. But over time, you've got to start having that halo accrued to the company. So some of the practical things you can do in that vein, you know, make sure that you're not the first face on the website that people see, for example.

You know, if you build in a management team, you might think about alphabetizing the names on your management team, as opposed to doing it in the Christmas tree hierarchy, where you as the chairman, CEO, founder are at the top of the Christmas tree, for example; little subtle things you can do.

James: That's a great tip.

John: Yeah, just subtle things you can do to communicate that you're there, you're driving, but you're not necessarily the most important person in the room.

James: That is a fantastic point. I've never heard the alphabet thing. You know, my big takeaway from our last interview was the being half pregnant thing. There's always a John Warrillow soundbite that's going to stick.

Consider what it’s worth in the buyer’s hands

The other thing that I thought was really interesting, and with a sales background, this appealed to me, you said that buying a story about what the business is worth in their hands.

John: So, so important. Yeah, look, anyone can pull out a table if you have a SaaS business right, and you're growing, you get low churn, you could Google it, and you can identify what a fair going rate for your company is. And that's looking at the value of your company. But that can wildly underestimate the value of your business in someone else's hands.

And so really, I think your job as an entrepreneur is to tell that story, make that narrative, that what they can do with the business in their hands. And so that's the definition of a strategic acquisition, by the way, when a strategic who has some assets, a distribution channel, lots of salespeople, lots of stores, whatever, they've got something that they can bring to bear to make your business worth more in their hands.

Oftentimes, they're in a Coke-Pepsi kind of battle, and your product or feature service allows them to differentiate. Well, again, if you think about what that could mean for a billion dollar company, if they get five percent more market share, I mean, that's a huge, huge win.

I'm reminded, you know, Jay Steinfeld, have you had Jay on the show?

James: Not yet.

John: He started Blinds.com. He's in the book. I talk about his exit. Blinds.com was started around the time of Jeff Bezos. Bezos was selling books, Jay Steinfeld had a blinds store, like window coverings. And he realized how hard it was to sell them in a retail shop. And so he started trying to sell them online. The challenge with blinds, unlike books, is it's a much more complicated product, right? You got to measure it, you got to figure out how to install it. It's a bit of a mess.

So it took him longer, but he eventually got the business up to $100 million in revenue when it was acquired by Home Depot, which is a big box retailer in the United States. And when you look at the reason that Home Depot wanted to buy Blinds.com, they wanted to buy it for two reasons. Number one, because they wanted a lead in every category that they are retailing, and in blinds, they were at number two position behind Blinds.com.

But the second reason is more interesting from a strategic point of view. And that is that they wanted to buy Blinds because they wanted to infuse what Jim and his team had learned about selling complicated products in all their other products, because Home Depot wants more people to buy at HomeDepot.com and not in their stores. And they've got a lot of complicated products, but they can't figure out how to get people to buy complicated products.

Sorry, it's not Jim, it's Jay. What Jay represented to them was the knowledge of not only how to sell blinds, but also other complicated products. So that's the definition of a strategic acquisition, where that business is worth much more in their hands than it is in Jay's hands.

James: Yeah, so they wanted to buy the intellectual property or the process.

John: That's right.

James: I've got a client at the moment, actually, he's looking to buy a particular type of business, which has a big user base, and the business isn't really doing that much with them. But my client has a product that is perfect for that audience. And I think the acquisition price was quite low, compared to if he had a really crappy conversion on offering his standard product to this audience.

It'd be cheaper for him to just buy the business than to promote it as a joint venture or whatever, because I think the person who's got the group hasn't figured out how to monetize this particular audience as well as he has. So strategic acquisition makes a lot of sense. That's actually part of the story of how I sold my SEO business.

John: Oh really, okay.

James: I sold it to my biggest customer, because I found myself in this interesting scenario where he was buying more and more and more and more of it. He was actually a student of mine. He was literally sitting in the audience when I spoke at a conference in Dubai. This was about 10 years ago. And he purchased my program and came on board and did everything I said to do and followed it. And then he was now set up selling search engine optimization services as an agency in Dubai.

And then he just was selling more and more. It ended up, he was buying more than half of my capacity. And I realized, I got a dilemma here. As a coach, I have to tell him, like, you should either replace me and build your own team, or you should buy the business and every dollar you spend, you get a 50 percent rebate, because we're running a 50 percent profit margin.

Of anyone on the planet, if he bought my business, it would pay him back much faster. Like it would basically pay itself back with just him buying what he already buys. And then he’s still got a business that he could sell later if he wanted. So it worked out great. And it's still going now, which I think is an interesting one.

The earnout that could become a flameout

You talk about in the book, where an earnout could also become a flameout. I'd love it if you could just cover that, because typically, no one's going to just hand over all the cash up front. I mean, maybe it happens, but it's probably rarer. And often, you're going to have some skin in the game or some delayed payment terms or you might have to stick around and do certain things or satisfy certain conditions.

This, I think is a really important one, because I'd say a lot of people would think, 'Oh, they'll just give me $20 million. And then I'm on my boat next month,' but it doesn't work that way, does it?

John: It doesn't, yeah, no. There's lots of different ways that you will have to participate or could participate in a transition period, the most common of which is, as you described as an earnout, where there's a set of goals that you agree to try to achieve, three, five years down the road. And if you achieve them, then you get an extra payment.

Again, the proportion of your deal that's at risk all depends on how risky they see buying your business is. I've seen situations where it's 100 percent earnout, and all of the risk you are bearing on your shoulders. I certainly wouldn't recommend you do that deal. But a more common scenario might be, you know, 60, 70 percent cash up front and 30, 40 percent.

It's enough that it hurts if you're going to walk away from the earnout, but not so much that they don't at least monetize or they'll allow you to at least monetize some of your company. So look, I think this is in many ways the enemy for the entrepreneur, right? Because as entrepreneurs, we don't thrive working for somebody else most of the time. It's like forced labor, right? The idea of working for a company for three, five years after you sell...

James: Oh, especially your company that you used to own.

John: Your own company. It's like having open heart surgery without the medication. It's terrible. So look, I think earnouts are a challenge, but you will have to do some sort of transition. When we're talking about earnouts, in the book, there's a story of Rod Drury. Do you know Rod? Have you had him on the show?

John: Not yet.

John: So Rod's a good guy. Those of you who know, you may have heard the name, he founded a company called Xero, which is the accounting platform that has just tremendous success, especially in Australasia, and certainly in the US as well.

James: Well, we use it, for sure, yeah. Everyone in my community uses Xero. Love it.

John: Yeah. So Rod founded Xero. What's interesting about that story is actually where he got the money to start Xero. And it's from building a company called Aftermail. So Aftermail was a way that big Fortune 500 companies could archive their email. And it was around the time of that legislation the US called Sarbanes Oxley. It made big Fortune 500 companies have to sort of like, archive their email and be a lot more rigid in the way they sort of archive stuff.

And so Rod, good Wellington, New Zealand guy, figures this, smells an opportunity, and builds this company called Aftermail. Gets two customers, two Fortune 500 companies, two big enterprise companies, to buy this software for a million bucks each. So he's got $2 million in revenue. What would 99.9 percent of people do with two customers? You go sell the rest of the enterprise market, right? There's 2000 enterprise customers or whatever.

So Rod takes a different tactic. And he says, "You know what, I'm going to sell this company," and he sells it to a systems integrator that had virtually all of the Fortune 500 clients. I'm going to see if I get the math right, he sold it for what I think is on the headline number, that newspaper in Wellington, New Zealand reported $35 million. But if you unpack the number; it was, again, a $2 million business; if you unpack the number, it was $15 million up front, and then another 20 in an earnout.

And so they don't report that in the newspaper. They just say Rod Drury, local boy, sells for $35 million, but in actual fact, it was 15. Still a fantastic exit for a $2 million dollar company. But just indicative of the earnout being at risk. And I asked Rod on the episode I wrote about it, I said, what would you do differently?

And he said, "You know what I would do, John? I would buy myself six months - six months to go on a vacation, six months to digest, metabolize what I've accomplished in selling my company, before the earnout clock starts. I would have that six-month cooling off period. It would allow me to meet the new employees at the company, meet the sales people at the company, network with the executives, blah, blah, blah, blah, blah."

Reenergize, so that when you're ready to go, you hit the clock, because what an earnout is, and you probably see this in your own business, James, it's, if you miss a gate, if you miss a target, they most often stack onto each other. And so it becomes impossible to hit your earnout if you miss one of the early gates, and Rod missed an early gate. It's like skiing down a downhill course, if you miss a gate, it's over.

And so Rod missed an early gate and realized, the gig is up. There's no point in me hanging around for another five years, just to be a vice president in this company. And so he took his winnings and started Xero. That's an earnout. In the case of Rod, it worked out just fine. But it can be a risk.

James: I think one of the other risks is, even if you don't have a performance quotient and even if you don't have to stick around and do things, if there is even just a delayed payment schedule, you have to rely on the company actually being around to continue those payment schedules. And then, you know, inevitable legal hassles and, you know, other stuff if there are defaults and so forth.

So I agree with you. I wouldn't do a deal to sell unless I was going to be comfortable knowing that the payment I got up front is all I ever get. And anything else after that is cream. I think that's my sort of own threshold.

The risk of financing with debt

John: I think it makes a ton of sense just to reinforce that. I just did a podcast this week with a guy who sold his business. He did a deal with a private equity group. And a lot of the guys, you know, a lot of the people in our kind of world, are most likely to sell to a private equity group. Private equity groups are right now rolling up lots of SaaS businesses, lots of technology businesses, digital companies, etc.

And in the space of say, valuation between say one and $50 million, as you want to use that as a broad spectrum, the private equity group is going to be the most likely buyer for a business like that. And their game is to buy your business and finance it with a lot of debt, right?

So what they typically do is buy 60, 70 percent of your company. So it's a controlling share, and they lever up that with debt. In other words, they borrow that money. And they make you carry 30, 40 percent of the equity into a new entity. And the argument is that, hey, look that 30, 40 percent is going to be worth a whole lot more when we roll you together with a bunch of other companies, and we sell the entity five, seven years down the road.

And so it's just enough to hurt. To your point, you know, you wouldn't want to do a deal where anything was at risk. Forty percent is a big number, right? So in this guy's case, he sold 60 and carried 40. They put a ton of debt on the company, on the new entity. The story is, you know the ending before I can even tell it; essentially, the business fails to meet its debt obligations. It can't make its payments, they bring in a bunch of executives to try to fix it, they can't.

And as a result, the new entity goes bankrupt, he loses everything on all of the 40 percent. And none of the 60 percent was at risk, but he lost everything that was at risk in the 40 percent. And that's not an uncommon story.

James: It's so common where people get offered or dangled the carrot of equity in a company that's going to be amazing in the future. And I actually can't think of a single example where someone's hit paydirt, and it's come big. It's like, almost always, people who want to structure those deals are working on a few of them panning out and most of them not, like the VC model. I'd say they have a lot more losers than winners, you know? For every Facebook, there's going to be a whole bunch of, you know, let's just sweep it under the carpet.

John: Yeah, look, I think there are, virtually anybody who buys your business is going to want some way to monetize it. So they're going to want you to participate in some sort of transition, you know, whether it's an earnout, in the case of a private equity group, some sort of shared or rolled equity.

The job, I think, of the entrepreneur, is to create competitive tension for the business, meaning multiple offers, so that you can tighten down or ratchet up your deal terms that are important to you. And so again, if you're negotiating with one acquirer, one private equity group as an example, well, they know that, and they're likely to take advantage of that and give you a deal that's not favorable.

Whereas if you've got three or four buyers at the table, you can say, "I know you want me to carry 40 percent of the equity, but really, I'm comfortable carrying 10, and I won't pay for the 90." It doesn't mean you're not going to participate in some sort of transition period, you might want to work as a VP for a year in the company, but you're not giving up everything in equity carry. And again, that only happens if you have multiple bidders at the table, and you can kind of drive your deal terms.

James: Yeah, it's good. You talk about, look, you set the price, I'll set the terms, some wonderful negotiation strategies. I want to be respectful of your time, John. I could actually talk to you for a week on this topic. Like, it's so easy having this conversation. I'm chatting to John Warrillow here, this is Episode 797 at SuperFastBusiness.com.

Between the covers of The Art of Selling Your Business

We've been talking about the art of selling your business. John, just to finish out, I'd love to just sort of do a little overview of what's in the book. I highly, highly recommend this book. I know if I had read this book, I would have sold my businesses better. I'll say that on record. I could have done better, because as I'm reading it, you filled in some gaps that I had at the time. And I think this is absolutely the best book I've read on selling a business, ever. I read two or three when I was selling my business, but this thing just comes straight over the top.

John: Oh, it's very kind of you to say.

James: So kudos for creating something amazing. So just a little overview, and I think we've covered some of them in our sort of conversation here, but you talk about building value in the first part of the book and what buyers are looking for. You talk about being happy with exiting, and I think that's definitely what was missing in some of the books that I've read.

The timing, really great ideas there. Like, you know, why you shouldn't really stag a high market or try and do it in a recession, and some good arguments back and forth about the tempo of a deal. You then go on to talking about how you do the slow reveal in chapter four. Chapter five is about positioning and making sure you're going to capture the most value.

Chapter six is about the three different types of acquirers, and you've hinted at a few of these in the podcast. Seven is identifying a buyer. This is really when you want to maximize the sale. Eight, you talk about the 5-20 rule. Do you want to say what that is?

John: Yeah, the natural buyer for your company is likely to be five to 20 times the size of your business today. So by definition, it's a David and Goliath bout, you're going to be smaller than them, so you've got to find a way to punch well above your weight when you sell your company.

James: That's what I think I could have done a lot better, because I was definitely the bigger one and having to host, you know, make the sale very easy for them. Chapter nine, you talk about teasing the sale, you just got to build the value without just giving it all away. And 10, critically, there's definitely an element of confidentiality. There's multiple warnings in this book about if you do things the wrong way, you'll basically be fleeced. They used to call this being Microsofted.

John: I've never heard that term before.

James: Ah, it's where they, you know, they come in and sidle up and do their sort of pre diligence and find out what you're doing to see if they want to buy you. But then suddenly, they have the same product or service, kind of like Instagram did with Snapchat and so forth.

You talk about some of the terms you'll want to know. Like, you don't want to walk into this like a rookie. You need to know what a sim is, for example. And then chapter 11, you talk about how long you carry this sort of secret with your team and the market and how you might communicate.

Chapter 12 is all about knowing your number. That's actually a conversation I have with my coaching students. One of the questions asked in their onboarding diagnostic is if they're looking to sell. Almost all of them say no. And then I say, "Well, what if I wrote you a check for $20 million today? Would you sell?" And they're like, "Yes." I said, "So you would sell. So let's figure out the number."

I actually had someone coach me, and the goal was to build their business to sell it in a year from now. And we sold it about two months later, for way more than he thought, because we'd had that conversation.

Then you go into negotiation tips, which you know, I have a sweet spot for that, talking about setting the price, setting the terms, the earnout versus flameout, how to nudge the price up a little bit. And then the concept of freedom. Overall, I'm glad we didn't just dredge through the book on this call. I think we had a really fantastic discussion.

Thank you for sharing so generously. And as I mentioned last time, five years ago, if you ever want to come back and chat about what you're up to, John, you've got an open invitation. Let's not leave it five years because...

John: Let's not leave it five years. I'm very grateful for your time.

James: I think our audience love this. Your book, I don't think it's even available at the moment, it's like pre-order in Australia, at least. But I think when this comes out, it'll be ready. So go and get it. If you want to send someone to a particular place, this is a good time to mention where you'd like them to go, John.

John: Yeah, you know what, BuiltToSell.com/selling, .and I'll tell you why. If you go there, we put together a couple of gifts with purchase. So folks of yours, listeners can go, and they can be opted into a really cool seven-part speaker series with some of the people featured in the book, and the guys that I mentioned today, like Jay Steinfeld's 100 million dollar company sold to Home Depot, Eric Levy, who we didn't talk about, but tremendous exit.

So they're going to kind of answer your questions on these events. So really, kind of a cool opportunity. So yeah, just BuiltToSell.com/selling. And you'll find all the offers there.

James: Perfect. We'll put a link in the show notes at Episode 797. John Warrillow, thank you so much.

John: James, pleasure.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