Eclipse
Corporate Finance

Nurseries Valuation Guide

Overview

A basic guide to the valuation of nursery businesses

- This guide aims to provide a simple overview of the key factors influencing the value of nurseries
- Nursery businesses are generally valued by applying an Earnings Multiple to the profits (usually the EBITDA) of the business
- For example, an Earnings Multiple of 6x applied to EBITDA of £500k would lead to a value of £3m for the business
- Most valuations of this nature are made on a cash free, debt free basis (see page 6 for further details)

Underlying EBITDA

- Whilst many may think that the EBITDA of a business is fixed, it is far from it for the purposes of business valuation
- The EBITDA used to structure a valuation should be the "Underlying EBITDA" – i.e. the true underlying profitability of the business to the acquirer
- A number of adjustments are generally made to EBITDA in order to present the most favourable figure for the purposes of valuing the business – see page 3 for further details

Earnings Multiple

- Multiples within the nurseries sector range broadly and illustrative ranges are often misleading
- Numerous factors will impact the Earnings Multiple applied to EBITDA
- These factors are unique to the nurseries market and should be carefully considered as part of a sale process – see page 4 for further details
- Presenting these factors in the best light and addressing any issues prior to commencing a sale process will help to maximise the value achieved

Underlying EBITDA

Presenting a credible Underlying EBITDA figure will be key in maximising value

- Presenting the optimum Underlying EBITDA for the business will have a material impact on the value achieved
- Rather than simply presenting the EBITDA from the latest statutory accounts, looking at trading performance over the last twelve months or run-rate period (often the last six months annualised) can be highly beneficial
- Exceptional costs or costs which will not continue post completion of a transaction should then be "added back" to increase the EBITDA figure
- Finally, any "pro-forma" adjustments, for example to show the true profit of new capacity which has recently become operational, should then be added back
- An illustrative example is outlined in the table to the right

£	FY18	FY19	FY20	LTM*	Run-rate**	Comments
Reported EBITDA	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**EBITDA before any adjustments**
Add back costs:						
Director Salaries	[+]	[+]	[+]	[+]	[+]	May not continue post completion of the deal
Other Shareholder Costs	[+]	[+]	[+]	[+]	[+]	Examples include leasing of private vehicles, memberships of golf clubs etc.
One Off Professional Fees	[+]	[+]	[+]	[+]	[+]	Exceptional costs related to a specific non-recurring item (e.g. legal fees for a bank refinancing)
Other potential adjustments:						
Profit From New Places	[+]	[+]	[+]	[+]	[+]	Adjustment to show the full year impact of recent capacity and occupancy increases
Synergy opportunities	[+]	[+]	[+]	[+]	[+]	Potential cost savings for the acquirer post completion (e.g. the removal of certain admin staff)
Adjusted EBITDA	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**EBITDA figure upon which offers will be structured**

* Last twelve months of trading
** Run-rate figures, often looking at the last six months of trading annualised

Earnings Multiple Drivers

A number of key factors will drive the size of the Earnings Multiple applied to profits

Quality

- Ofsted ratings are the key identifier of quality for acquirers of nurseries
- “Good” and “Outstanding” ratings will attract premium multiples, whilst “Requires Improvement” or “Inadequate” ratings will materially hamper valuations

Fee levels

- Higher fee levels will drive greater multiples as they will generally result in strong margins
- Fees levels are inherently linked to the location of the nursery and the style and condition of the property (see below)

Occupancy

- High occupancy levels are a sign that a nursery is operating effectively
- Waiting lists are also a positive sign of demand for places
- Consistently high occupancy levels will therefore drive greater earnings multiples

Location

- As noted above, affluent locations are generally sought after by acquirers as they generate higher fee levels
- Proximity to residential areas and accessibility are also vital in order to ensure there is sufficient local demand

Property

- Clearly freehold property ownership will attract higher multiples than leasehold
- Well invested properties will be favoured, with acquirers reducing prices for any perceived “catch up capex” required
- Basic issues such as property access, parking and utilities should be considered

Scale

- The scale of a business (whether nationally or within a particular region) will also impact the valuation – generally larger businesses generate higher multiples
- This applies to both the number of registered places and the number of sites that a business operates

Illustrative Leasehold Valuations of Nurseries

Earnings multiples range broadly for leasehold nurseries based upon the criteria previously outlined

		Valuation: **6-7x EBITDA multiple**
	Valuation: **4-5x EBITDA multiple**	**Ofsted Rating:** **All nurseries rated Good or Outstanding**
Valuation: **2-3x EBITDA multiple**	**Ofsted Rating:** **All nurseries rated Good**	**Scale:** **Large group (>5 nurseries)**
Ofsted Rating: **Requires Improvement/Good**	**Scale:** **Small group (3 nurseries) with 150 places**	**Location:** **South East**
Scale: **Single nursery with <50 places**	**Location:** **South West**	
Location: **North East**		

* All illustrations assume the sale of leasehold businesses.

Cash free, debt free offers

Offers will be made on a cash free, debt free basis, with a normal level of working capital

- When selling the shares of a company, the vast majority of offers are made on the basis of being "cash free, debt free"
- In simple terms, this means that any cash in the business is retained by the seller and that all debt is repaid by the seller upon completion
- Transactions should also include an adjustment to "normalise" working capital. This prevents the buyer from having to inject funds into the business if there is insufficient working capital to run the business after completion
- This adjustment is usually calculated by comparing the working capital at completion against the average working capital over the recent past
- The table on the right outlines an illustrative example of this calculation

Description	£000s	Comments
Enterprise value	**3,000**	**Adjusted EBITDA x valuation multiple**
Plus cash on balance sheet	250	
Minus debt and debt like items:		
Mortgage/bank loans	(500)	
Hire purchase creditors	(25)	
Corporation tax	(50)	Any outstanding corporation tax liabilities for the period up to completion
Deferred tax	(10)	Treated as debt if the balance will crystallise in the medium term
Plus/Minus working capital adjustment	20	Generally calculated by deducting the average working capital over the last 12 months from the working capital at completion
Equity value	**2,685**	**Value payable to the shareholders**

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