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Dental Laboratories Valuation Guide

Overview

A basic guide to the valuation of dental laboratories

- This guide aims to provide a simple overview of the key factors influencing the value of dental laboratories
- Dental laboratories are generally valued by applying an Earnings Multiple to the profits (usually the EBITDA) of the business
- For example, an Earnings Multiple of 5x applied to EBITDA of £300k would lead to a value of £1.5m 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 dental laboratories 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 dental laboratories 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

£	FY20	FY21	FY22	LTM*	Run-rate**	Comments
Reported EBITDA	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**[ ]**	**EBITDA before any adjustments**
Add back costs:						
Director Salaries	[+]	[+]	[+]	[+]	[+]	Directors' costs are added back if exiting upon completion, or normalised to a market salary if they will continue operating in the business post completion
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 increased capacity	[+]	[+]	[+]	[+]	[+]	Adjustment to show the full year impact of recent capacity/volume increases
Synergy opportunities	[+]	[+]	[+]	[+]	[+]	Potential cost savings for the acquirer post completion (e.g. the removal of certain admin staff)
Underlying 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

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Earnings Multiple Drivers

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

Quality

- Laboratories that service high-quality private practices will attract premium multiples
- Producing larger volumes of aesthetic and complex restorative work generally leads to higher profit levels

Fee levels

- Higher fee levels will drive greater multiples as they will generally result in strong margins, this is also reflected in the revenue per technician metric
- Fee levels are inherently linked to the type of work the laboratory produces (Private vs NHS) the size of its distribution network and the skill level of technicians

Number of technicians

- Due to European technicians moving back to Europe after Brexit and the pandemic, the UK is experiencing a serious shortage of technicians– as a result, larger teams will attract higher multiples
- Training apprentices on the books will also look positive as it mitigates future risk

Location

- Affluent locations are generally sought after by acquirers as they generate higher fee levels, due to being in close proximity to quality private dental practices

Property & capacity

- Most acquirers, especially corporates, will look to have a new 10-15 year lease granted on the property
- Well invested properties will be favoured
- Acquirers will work to grow the laboratory – having available space for the addition of benches will be an important consideration

Client dependency

- The scale of the laboratory and its revenue dependency on its top 25 clients will also impact the valuation
- Generally larger businesses with lower dependency generate higher multiples

Illustrative Leasehold Valuations of Dental Laboratories

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

		Valuation: 5-5.5x EBITDA multiple
Valuation: 3.5-4.25x EBITDA multiple	**Valuation:** 4.25-5x EBITDA multiple	
Revenue per Technician: £50k - £80k	**Revenue per Technician:** £80k - £110k	**Revenue per Technician:** +£110k
% Private Revenue: <50%	**% Private Revenue:** 50% - 85%	**% Private Revenue:** >85%
Top 25 Client Dependency: >50%	**Top 25 Client Dependency:** 30% - 50%	**Top 25 Client Dependency:** <30%
Number of Technicians: 3 - 7	**Number of Technicians:** 7 - 12	**Number of Technicians:** 12+

* 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	**1,500**	**Adjusted EBITDA x valuation multiple**
Plus cash on balance sheet	250	
Minus debt and debt like items:		
Mortgage/bank loans	(200)	
Hire purchase creditors	(25)	
Corporation tax	(25)	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	**1,510**	**Value payable to the shareholders**

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