WHY PETRO BUSINESS MARKET VALUES FLUCTUATE WILDLY

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"The more stable and ample the supply is, the more attractive the deal."

One of the questions I get asked most frequently is "What is happening with market values?" For a marketer thinking of selling, the current trend in market values is hugely important for the best price.

On the other hand, active buyers are more apt to grumble about selling marketers wanting way more than the business is worth. What a marketer wants for his retirement slush fund is not always a good indicator of true business value!

What puzzles both buyers and sellers alike is why the same business with the same trends would have different prices in different years. Isn't the price the price? Not really. Here are six outside factors driving petroleum market prices today:

The current sexiness of the sector. Just as gentlemen's necktie styles come and go, the appetite for petroleum sectors is a moving target. I remember talking with a large petro company CEO about three years ago. At that time, he told me retail was the only sector they wanted. They were getting rid of everything but their owned and operated stores. Two years later, the same CEO called me and wanted Tankwagon wholesale in rural markets. Go figure!

The "sexy" sector historically varies by geography. For instance, last year retail was hot in the Northwest, lubes were lusted for in the central USA, and dealer contracts were the most attractive in the Southeast. So, the trick to getting value right is knowing what is hot in your own geography.

Margin Predictions. Because buyers who spend money today get their return on investment going forward, they typically look out into the next five year horizon. Whether a seller likes it or not, it's the buyer's perception of future margins that dictate offer price. If a buyer feels the margin on a particular product in a particular geography has already peaked and is headed downward, they will discount for what they consider to be a declining margin environment. Are they right about their prediction? Maybe. Maybe not.

The margin prediction discount can be extremely frustrating to a seller who has been working hard to build margin over the last few years, only to have a buyer tell him it won't and can't last.

Expense Predictions. Even if a company's margin is predicted to hold steady or grow, expense predictions also effect marketplace pricing. Those marketers selling larger chains of retail units were plagued with lower prices because buyers had no clue how much their health care would cost. This uncertainty created lower pricing throughout many labor-intensive industry buy/sell transactions, not just petro.

Expense predictions, however, are often more specific. For instance, a company with identical year after year EBITDA could be discounted if a buyer thought maintenance had been deferred recently. Even the cost of improvements can impact trends.

For example, when steel prices went screaming up, the propane sector took a hit on market values. While the companies were still cash flowing and growing, and theoretically should have had more value, the investment dollars required for tanks increased substantially, which caused buyers to lower their offers.

In this high price steel environment, companies with good tank control (documentation of company-owned tank locations) commanded higher prices than companies without good data on owned tanks since so much of the purchase price relied on the steel.

Management Culture – Another interesting market fluctuation is based on the emphasis (or not) on management depth. We've seen some years where buyers eagerly would pay premium prices for top-notch managers utilizing non-compete and key-man offers as part of their offering package and price.

In other years, the buyer marketplace trend was towards centralizing as many functions as possible, cutting back on duplicate personnel costs. Given these anomalies, identical cash flow companies sold at different multiples based solely on management preferences of the buyer.

Financing Availability – When credit is tight and lenders are pulling back on leverage or requiring stronger buyer down payments, fewer deals get done which generally depresses prices. When banks are eager to lend, prices get more generous.

More interesting during times of strong available credit and banks fighting for deals, is when some buyers are given ample acquisition lines of credit that must be used or forfeited by a certain date. That really increases prices as buyers speed to the marketplace!

Availability of Supply – This one gets tricky. It's again all about buyer perception. The market (collectively all buyers) decides the supply risk in any area. So terminal outages and shutdowns, completely out of a marketer's control, can and do impact seller offering prices.

The more stable and ample the supply is, the more attractive the deal. Of course, with ample supply usually comes more competition, which is where the margin prediction overlaps with the supply prediction.

All of this pricing uncertainly can be frustrating to marketers preparing their exit strategy. You just can't go by the old EBITDA multiple guess anymore and get it right. Usually if you hear of unbelievably large or low EBITDA multiples out at industry functions, it's just a matter of how a particular buyer or seller calculated EBITDA anyway.

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