hosting con 2015

Build or Buy? Case Study On Growth Strategies For Small to Mid Sized Hosts





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Agenda

Pros and Cons Financing Sources Nature of the Market Requirements for Organic Growth Requirement for Buyers Market Valuations What is Usually Sold? **Factors Affecting Valuations Overview of Buying Process Length of Process Due Diligence Case Studies More Money Summary**



Pros and Cons











Pros and Cons of M&A

Pros:

- Speed / Competitive advantage
- > Costs?
- Cherry pick profile (maybe)
- Efficiency / Economies of Scale



Cons:

- > Requires financing
- Risk and leverage
- Distraction
- ➤ Hard costs (travel, legal and CPA fees)
- > CPA may be higher (VPS and Dedicated)
- Disparate technologies, equipment, teams and systems
- > Time consuming with no certainty of a transaction





Pros and Cons of Organic Growth

Pros:

- Costs may be lower (esp if niche provider)
- Unutilized upselling opportunities
- > Steady and controlled (manageable) growth
- ➤ Hedge against churn
- Costs can be controlled and adjusted
- > Less disruption (migration, name changes, billing details, multiple brands etc)

Cons:

- Requires patience
- > Requires commitment
- Slower growth
- Hard costs with no guarantee of results







Financing Sources

- > M&A
 - Equity partners including VCs
 - Debt financing
 - Cash from operations
- Organic
 - Likely cash from operations
 - Investor?



Nature of the Market

> M&A

- Reasonably strong demand from buyers
- More strategic buyers but consolidators still exist
- Fewer sellers esp. mid and upper market
- Sellers exiting often due to:
 - Growth ceiling
 - Lifestyle and personal reasons
 - Partner wants out
 - Shift in focus



Nature of the Market

- Organic Growth
 - Extremely competitive
 - Niche companies doing better
 - Growth in SMBs
 - Channel partners
 - Upsells via ISV solutions





Requirements for Organic Growth

- Clear on target market
- > Track everything
- > Test
- > Have realistic expectations
- > Have dedicated resources
- > Be creative





Requirements for Buyers

- > Establish a process
- Build your team
- Be clear on objectives
- Secure financing
- > Allocate the time
- Valuation expectations
- Prepare examples of previous success







Market Valuations

- > 1 x annual run rate (12 months)
- Higher for larger transactions
- Public companies P/E
 - Rackspace ~\$46
- Compare to CPAs of <\$250</p>





What is Usually Sold?

- Most are asset vs. stock
- Customer base, equipment, licenses, leases, software, IPs, domain name, websites, employees, founders etc.





Factors Affecting Valuations

Revenue trends and churn

Nature of client base

Ease of account migration

Reason for selling

Owner's relationship to customer base?

Geography

Strategic benefit to buyer

Proprietary Software

Reputation

Inclusion of IP blocks

Different lines of business valued differently

Competing offers?

Seller Support

Accounts prepaid or paid monthly

Contracts/leases

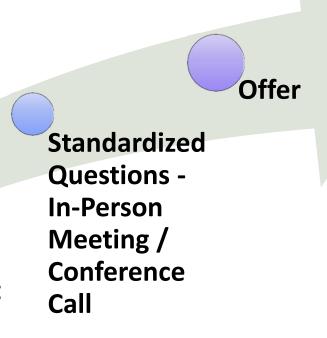
Payment terms



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Overview of Buying Process

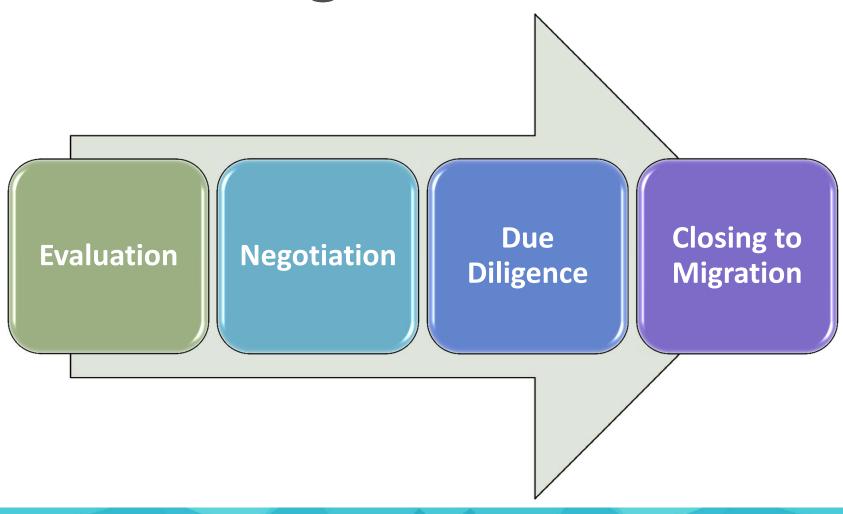


Nondisclosure Agreement

Broker's
Agreement
& Fees



Length of Process







Due Diligence

- > Financial statements or revenue and expenses
- > List of assets
- Customer breakdown
- > Leases, contracts
- ➤ Merchant & bank statements
- > Tax returns??
- Screen share walk-through





Background on Case Study #1

Domains #	2250
Equipment included	\$75 to \$150K
Control panel	Custom panel included in sale & Plesk
Billing system	WHMCS
Prepaids	Some prepaid expenses
Linux	100%
Windows	0%
Growing or Declining	Growing
Notes	Relatively attractive deal



Case study #1

Total Revenue	\$930,000
Price paid	\$1,110,000
Multiple of revenue	1.19
Shared - # of accounts	1097
Shared revenue	\$119,982
Shared as a % of revenue	13%
ARPU	\$9.12
VPS - # of accounts	1374
VPS revenue	\$676,664
VPS as a % of revenue	73%
ARPU	\$41.04
Dedicated - # of accounts	
Dedicated - Revenue	\$4,950
Dedicated as a % of revenue	1%
ARPU	\$275
Misc Revenue	\$128,405



Background on Case Study #2

Domains #	None
Equipment included	Yes but old
Control panel	cPanel, DirectAdmin and one more
Billing system	WHMCS
Prepaids	Majority monthly
Linux	99%
Windows	1%
Growing or Declining	Flat
	Inexpensive plans = low margin, poor
Notes	reviews



Case study #2

\$602,099.75
\$350,000.00
0.58
\$0.00
\$0.00
0%
n/a
7,175
\$567,000
94%
6.59
5
\$12,600
2%
\$200
\$22,499.75



Background on Case Study #3

Domains #	206
Equipment included	Yes
Control panel	Cpanel, Plesk, HyperVM
Billing system	WHMCS
Prepaids	Half monthly and half annually
Linux	Balance are Linux
Windows	12% of shared customers are windows
Growing or Declining	Flat
Notes	Higher % of dedicated





Case study #3

Total Revenue	\$250,500.00
Price paid	\$270,000.00
Multiple of revenue	\$ 1.08
Shared - # of accounts	434
Shared revenue	\$54,674.25
Shared as a % of revenue	22%
ARPU	\$7.88
VPS - # of accounts	126
VPS revenue	\$75,512.25
VPS as a % of revenue	30%
ARPU	\$37.46
Dedicated - # of accounts	37
Dedicated - Revenue	\$117,810.00
Dedicated as a % of revenue	47%
ARPU	\$200.36
Misc Revenue	\$2,503.50



More Money

- > Legal fees
- ➤ Brokerage fees
- > CPA fees
- > Time in due diligence and transition
- Possible migration costs
- ➤ Additional equipment?



Summary

- > Try something new
- Have a plan and know what you can pay
- > Have a team in place
- Start small and move to larger deals or campaigns
- Create success and replicate
- Remain focused





hostingcon 2015 Questions Please!





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