

# Canadian Pharmacists Conference 2015

Innovation and Collaboration

## What's the value of your pharmacy?

Mike Jaczko, BSc. Phm, CIM®



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# About Mike Jaczko

- Pharmacist
- Partner and Portfolio with K J Harrison
- 32 years Merger & Acquisitions in Canadian retail pharmacy industry
- 19+ years experience in Canadian wealth management industry
- Trusted advisor to pharmacy owners
- Advisor on broader issues of wealth management



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# Learning objectives

1. Identify the most common methods used to value a Canadian retail pharmacy
2. Understand the general difference between an asset and share deal
3. Understand the importance of cash flow in two of the most respected valuation methods
4. Understand the synergies between improving store cash flow and adding intrinsic value to your pharmacy business



# Disclosure

- The presenter of this learning activity declares that he has no conflicts of interest to disclose with respect to the facilitation of this program.



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# Profession of pharmacy and the business of pharmacy



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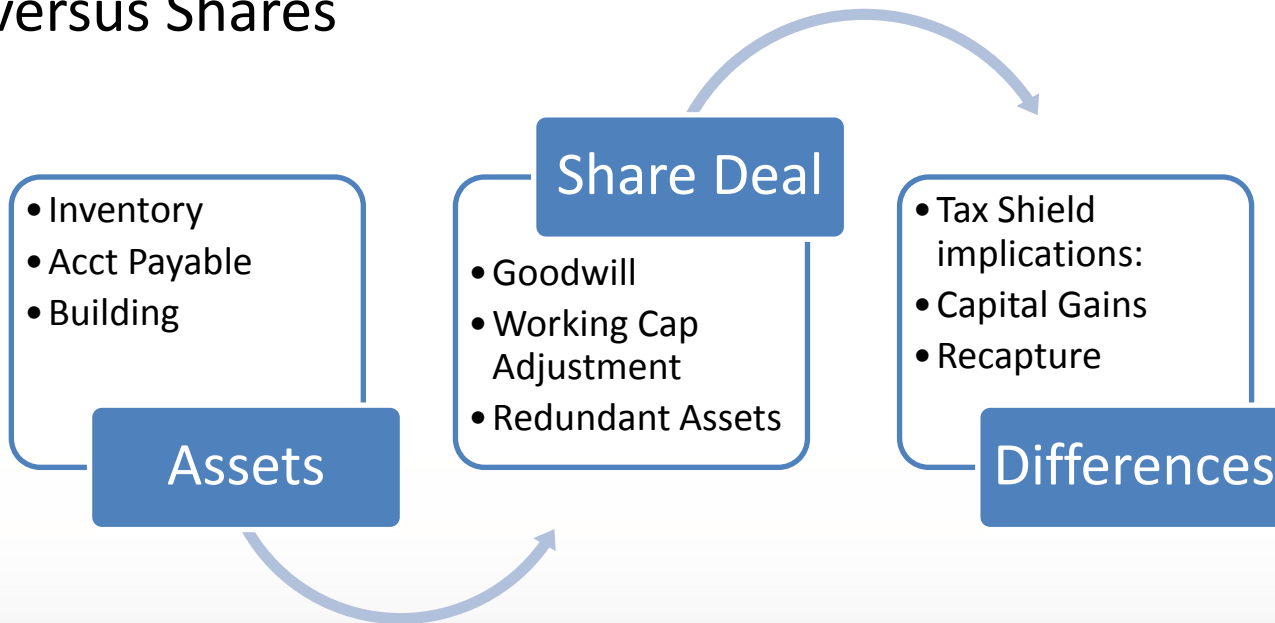


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# What are you valuing?

## Assets versus Shares



# Asset sale

- Company is the “seller”
- Capital gains exemption – is a non-issue
- Company assets are valued and sold
- Subsequently deposited into a new corporation
- Taxation occurs in:
  - the seller corporation
  - paid personally by seller to get proceeds out



# Selling shares

- Shareholder is selling the shares of the corporation
- Buyer purchasing shares
- Ownership is passed
- Corporation lives on
- Purchaser inherits liabilities as well



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# Asset versus share deal?

## Asset

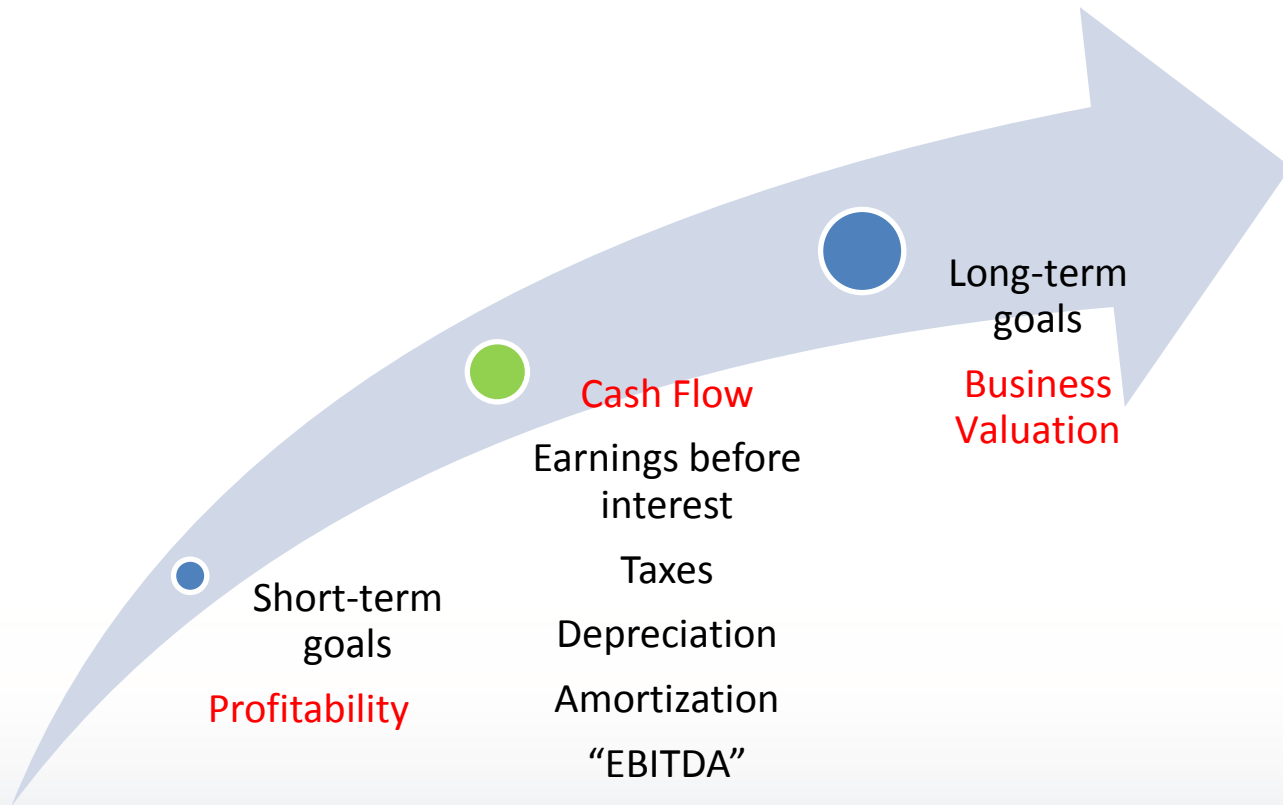
- Preferred by buyer
- Higher due to tax shield implications

## Share

- Preferred by sellers
- QSBC exemption \$800K
- Majority of transactions



# The relationship



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# Cash flow

- EBITDA
- Earnings before interest, taxes, depreciation and amortization
- Normalization – important process
- Key element in two major valuation models



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# Valuation considerations

- Various methods:
  - \$/script, sales multiple – extremely crude
  - Retrospective - Cash flow multiple
  - Prospective - Discounted cash flow
- Asset vs. share deal
- **Intrinsic** Value versus **Market** Value versus **Sale** Value
- Driving Market Value (*price discovery*) drives the Sale Value
  - An art (*price discovery*)
  - Establishing internal valuation based on **cash flow**
  - Validated by the ability to service debt



# Retrospective valuation

- Multiple of normalized earnings
- Most widely used

Three components added to get final price:

1. EBITDA X Multiple = Goodwill +
2. Net Tangible Book Value Adjustment =  
\$+ inv + A/R – A/P + Accruals +
3. Redundant Assets (e.g. building, land marketable securities)  
  
= Total price



# Prospective valuation

- Forwarding looking - develop
  - “Proforma” five to 10 years
  - Measure the cash flow each year
- DCF - Discount back to a “present value”
- Forms the basis for the “Goodwill”
- Used by sophisticated buyers
- Useful to measure debt servicing



# Example debt servicing schedule

Total 2012 Cash Price	\$4,320,000										
Interest Rate	6%										
Term (months)	60										
Amortization (months)	120										
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	
Estimatd Maintable EBIT-DA (as projected)	\$870,519	\$904,112	\$938,862	\$974,808	\$1,011,987	\$1,062,586	\$1,094,464	\$1,127,298	\$1,161,117	\$1,195,950	
Deduct Interest Charges (current)											
Deduct Interest Charges (proposed)	<u>\$250,354</u>	<u>\$230,298</u>	<u>\$209,204</u>	<u>\$186,398</u>	<u>\$162,397</u>	<u>\$136,916</u>	<u>\$109,864</u>	<u>\$81,143</u>	<u>\$50,650</u>	<u>\$18,276</u>	
Pre-Tax Debt Adjusted Earnings	\$620,165	\$673,814	\$729,658	\$788,410	\$849,590	\$925,670	\$984,600	\$1,046,155	\$1,110,467	\$1,177,674	
Less Income Tax											
Small Business Rate @ 15.5%											
For First \$500,000	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	-\$77,500	
Prescribed Rate thereafter	<u>-\$32,445</u>	<u>-\$46,930</u>	<u>-\$62,008</u>	<u>-\$77,871</u>	<u>-\$94,389</u>	<u>-\$114,931</u>	<u>-\$130,842</u>	<u>-\$147,462</u>	<u>-\$164,826</u>	<u>-\$182,972</u>	
Total Taxes	<u>-\$109,945</u>	<u>-\$124,430</u>	<u>-\$139,508</u>	<u>-\$155,371</u>	<u>-\$171,889</u>	<u>-\$192,431</u>	<u>-\$208,342</u>	<u>-\$224,962</u>	<u>-\$242,326</u>	<u>-\$260,472</u>	
Net After Tax earnings	\$510,220	\$549,384	\$590,150	\$633,039	\$677,701	\$733,239	\$776,258	\$821,193	\$868,141	\$917,202	
Deduct Net Sustaining CapEx	-\$12,176	-\$12,419	-\$12,667	-\$12,921	-\$13,179	-\$13,443	-\$13,846	-\$14,262	-\$14,690	-\$15,131	
Adjusted Discretionary Cash Flow	\$498,044	\$536,965	\$577,483	\$620,118	\$664,522	\$719,796	\$762,412	\$806,931	\$853,451	\$902,072	
Deduct Principal Due	<u>\$325,176</u>	<u>\$345,232</u>	<u>\$366,326</u>	<u>\$389,132</u>	<u>\$413,133</u>	<u>\$438,614</u>	<u>\$465,666</u>	<u>\$494,387</u>	<u>\$524,880</u>	<u>\$557,254</u>	
Net Cash Flow	\$172,868	\$191,733	\$211,157	\$230,986	\$251,389	\$281,182	\$296,746	\$312,544	\$328,571	\$344,818	
Cumulative Cash Flow	<u>\$172,868</u>	<u>\$364,602</u>	<u>\$575,759</u>	<u>\$806,745</u>	<u>\$1,058,134</u>	<u>\$1,339,316</u>	<u>\$1,636,062</u>	<u>\$1,948,606</u>	<u>\$2,277,177</u>	<u>\$2,621,995</u>	



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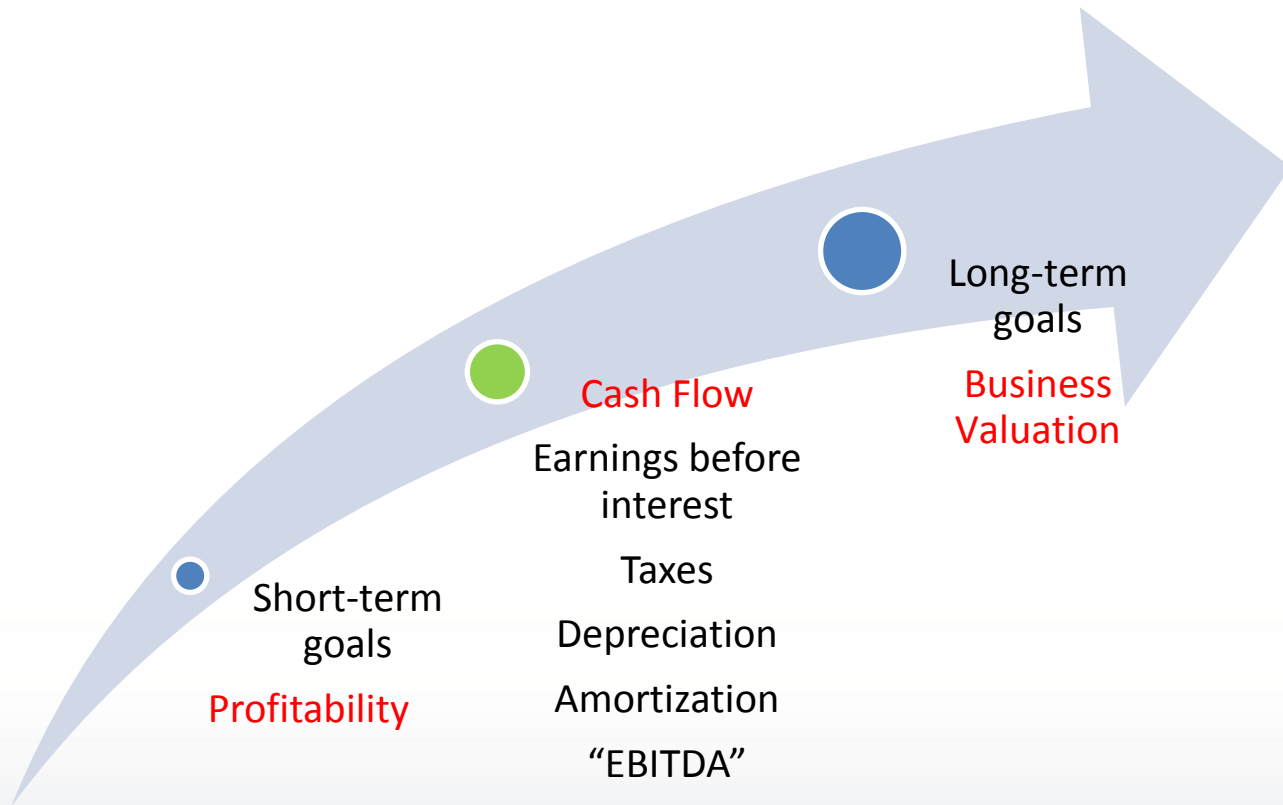
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# More information

- <http://www.kjharrison.com/advice/mjaczko>
- Articles 4 & 5



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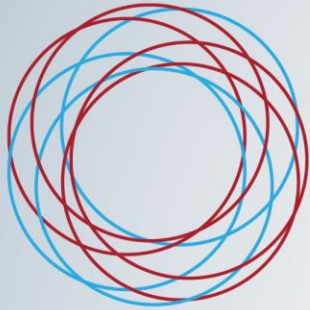
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## Questions?

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