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DIVESTITURES *of* SECURITY GUARD COMPANIES

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Dedicated to Buyers and Sellers of Security Guard Companies

REACHING THE *GLASS CEILING* . . . Time To Sell

Almost all security guard company owners have aspirations that their company will some day be a major force in the industry. But few get there. They fall victim to a force that limits the owners; ability to expand the company. It's silent and invisible. It's a force that pushes the owners down. It's a point that no matter how hard the owners try, they cannot get past. It has to do with the glass ceiling effect; and just how high this ceiling is depends on the owners' management abilities and degree to which they are willing to accept risks – a fact that usually is not realized until the company has lost value.

James Gordon, the majority owner of Protective Services, Inc., based in Dallas, first called our office on March 3, 1994. He started the conversation by talking about establishing a relationship with our firm so that we can follow his continued success. When he reached his sales volume goal, he wanted us to manage the sale of his company.

James was ambitious. He paid his own way through college by working part-time for a national security guard company. He came to like the security guard business. When he graduated in 1985, and with the financial help of his family, he started his own security guard firm.

In 9 years, he had grown the company to

an annual volume of over $15 million, with offices in 4 major Texas cities. His long-term business plan was aggressive, and called for 20% growth. He would sell the company when he reached $50 million in sales, which he anticipated would happen in about 7 years.

He called our office regularly over the years that followed. The conversation topics were about all the good things happening to his company. When he called in 1997, his volume was $24 million, not quite in line with his plan, but close and still very respectable growth rate. He had now moved into a couple of surrounding states and was making a good profit. He had a lot of proposals out and was sure he would get 90% of them, which would bring his volume to $28 million shortly.

When he called in July 1998, he said he didn't win most of the bids we talked about in our last conversation. He had some growth, but also lost several accounts to his low billing-rate competitors. Nonetheless, he was still enjoying running his company.

He was a hands-on owner/manager. He involved himself in all the aspects of running the business; after all, wasn't that the real reason he had been so successful? He was beginning to spend a lot of time with paperwork dealing with the increased government regulations put on businesses.

He also spent much of his time upgrading the computer systems, and helping the human resources department, which was having trouble finding qualified personnel. He regretted that he didn't have time to visit his accounts as often as he used to. Those day-to-day distractions kept him from spending time developing his marketing efforts.

His sales were now $27 million . . . far less than the goals established 4 years earlier. "But I'm going to really start growing" said James. "The customers of the 'majors' (national security guard companies) are calling me on a regular basis requesting proposals."

James called us several more times expounding on what was just over the horizon, but his sales volume stayed at the $25 million mark and sometimes dipped to lesser amounts.

The last call James made, which was about two weeks ago, ended on a more somber note. His competitors were making it increasingly harder for him to make a profit. They were approaching his accounts with the promise of lower billing rates and the accounts in turn, were looking to Protective Services, Inc. to match the bid.

If he lowered his rate, he would have to cut operating costs, which would mean that he would have to install yet another more powerful computer system, one that will give him frequent job profitability reports. A new computer system would cost over $100,000. The computer company wanted a financial commitment before it started work and James didn't have the funds available.

James had also become aware of some very fundamental economic principles that relate to bringing on new accounts. James commented that . . . "I've come to learn that the security business is cash intensive. Since we pay bi-weekly and it takes 45 days to turn our invoices into cash, every time I take on a new account, I have to have enough money in the bank to cover at least three payrolls."

In order to buy the computer and bring on new accounts, James would have to ask the bank for an increase in his credit line. The bank was considering it, but needed James and his wife to put up more of their personal assets as collateral. James already had to put some of his personal funds back into the business to keep it running. He didn't want to keep taking those risks, and managing the business wasn't fun anymore. He wanted to sell the company.

James admitted that he should have sold his company back when his growth trend was headed up and was more attractive to a buyer.

James Gordon and Protective Services, Inc. are fictitious names. However, the plight of James and his company are very real and one shared by owners of most privately-held companies.

When they start their company, they have a plan. The plan may have grandiose proportions that call for the company to be national or international, or it may be a more modest plan that calls for the company to be a regional or local leader. The plan may be written, as in James's seven-year formal plan, or may be just an idea sketched in the mind of the owner/entrepreneur, but nonetheless it is still a real plan.

Whether the plan is a success or a failure depends on the leadership qualifications of the owner, as well as the owner's tolerance of risk. As we will see in this article, about 95% of the owners of privately-held security guard companies unfortunately do not reach their goals.

Instead they reach a point where their growth is greatly curtailed, levels off, or the company starts to actually lose volume and profits. Most owners do not recognize when it has arrived; hence it's called the *"glass ceiling"* on growth.

It's also important to note that the company may be growing, but still have reached its *glass ceiling*. It's only the quality sales that count when determining a company's real growth. Some owners, in the anticipation of a sale in the near future, will put on a sales campaign to just bring in accounts. The accounts may be of a lesser quality and margin than the company's normal accounts. In that case, the company reached its *glass ceiling* when it stopped bringing in accounts consistent with its normal standards.

Companies are started by entrepreneurs. They are ambitious. However, such ambitions often exceed their capabilities. Most have a need to be in control, which limits their ability to properly delegate, a very important aspect of growing and managing a company.

Even though entrepreneurs take risks, which is another important characteristic needed to grow a company, there's a limit on how much risk they will accept, since it usually involves their personal assets.

Not all owners have the same level of management skills and tolerance for risk. Therefore, the *glass-ceiling* concept cannot be described in terms of a definite size.

To quantify *the numbers* of privately held companies that are victims of the *glass ceiling*, consider this: most reliable sources indicate that there are between 10,000 and 12,000 security guard companies in the U.S., and that this market represents $15 - $17 billion in annual sales. Sources also indicate that approximately 20 companies have sales exceeding $50 million annually. We estimate that there are less than 50 companies with sales over $10 million annually; which means that 95% of the *total number* of security guard companies have sales less than $10 million.

While these statistics only pertain to the U.S. market, a large percentage of the security guard companies in foreign markets are victims of the *glass ceiling* since these markets are highly fragmented as well.

Perceptive owners, although very few in number, recognize when they've reached their *ceiling*. To them it's not a silent, invisible force keeping them from their goal. They know their limitations and are aware when they've reached them. They also understand the buyer's viewpoint in evaluating their company. They know that one of the important characteristics a buyer looks for in a purchase candidate is the company's sales growth trend.

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An upward trend indicates that the managers, who will be a part of the transaction, are well-trained and still motivated to continue this growth into the future. Buyers see this as a valuable asset accruing to them after the purchase, and they definitely take this into consideration when arriving at an offering price for the company.

As one may conclude from this article, the *glass ceiling* effect, although limiting to the owner/entrepreneur, should be a necessary factor in the owners' decision on when to sell. The owner should realize that the skills needed in starting a company are different from those required to run a large organization. Neither set of skills is greater or more important than the other – they are just different. It takes the entrepreneurial skills and tolerance for risks inherent in the owner to start a company and take it to a certain point. But when the company reaches this point, it should be sold to a larger company with the financial resources already in place and run by executives with skills, quite unlike those of the owner/entrepreneur, needed to work within the often frustrating framework of the larger organization. These are the necessary ingredients for taking the owners' company to the next higher level. RHPA

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This periodic informational letter is published by:

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We initiate and manage transactions for sellers of security guard companies. Established in 1977, we have successfully represented over 100 sellers located in the United States, Canada, Western Europe, the Caribbean and South America.

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