Considering PR Agency Profitability

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Mergers and acquisitions are a constant fact of life for PR agencies. Have you thought about starting your own firm, and wondered about an exit strategy? Or do you manage your own agency and wonder what it would take to sell it?

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Profits, profits, profits. By now PR agency owners understand the mantra of profitability and how important it is to be able to sell your firm. You've undoubtedly read about how firms are valued and what they need to do to make sure their finances meet the minimum acquisition requirements.

But lest we fall into the trap of declaring that numbers are everything, let me set the record straight. Profitability is important in the following way: t opens the door to acquisition discussions. It is not the be all and end all. If it were, then deals would be done sight unseen where a buyer reviews financials and makes an offer for a firm. There are far too many other important criteria for a successful acquisition.

In fact, I would venture to say that profitability isn't even the No. 1 criterion. It is probably fifth or sixth. Does this mean I am advocating that a PR agency owner minimize the importance of profitability? No. What it means is that there are far more important criteria.

It’s been generally concluded that a PR firm should aim for a 20 percent profit. Does this mean that a PR firm that does 10 percent should remove itself from the acquisition marketplace until it does 20 percent?

Absolutely not.

A PR firm that does 10 percent profit may be just the right fit for the right acquirer. And the fact that the prospective seller isn’t at the highest level of profitability may be of no concern to the buyer.

By joining forces, both the buyer and seller can embark on cost savings items like rent, administration, HR, accounting, technology and so on. But more important are the synergies, the complementary business, the management team and growth potential.

There is one caveat though. The seller would get a better financial deal if his firm did 20 percent profit rather than 10percent. But if the synergies are there and both buyer and seller buy into them, then the seller could still generate a meaningful purchase price.

With cost savings, the seller’s profitability would take a dramatic turn upward. And with expected new business generated by both parties, the numbers could increase even more.

Consider this. There may be some very valid reasons why a PR firm’s bottom line is low. It may have erroneously gotten office space that is considerably more than the industry average of rent being 7 percent of revenues. If it’s 15 percent, then 8 percent of that amount is going into rent and not profits. Or the agency may be overstaffed for the business

it has. Or the agency may have too many low paying accounts.
A Remedy

Here’s what an astute buyer could do to help remedy these situations. It can help the seller negotiate with the landlord to get out of the lease with a reasonable penalty. It can take over the admin side of the seller’s business allowing the selling agency’s owner to focus on business development, clients and staff. And the buyer can help the seller generate greater proceeds by running the business more efficiently.

Many buyers can see well beyond the present state of affairs of a selling agency and that’s why a lower profit margin isn’t a deterrent at all. The most important component in any acquisition is the chemistry between the top management of both the seller and buyer. Without this chemistry even a 30 percent profit on the part of the seller can be meaningless.

Given all this here are the top criteria in selling a PR agency in this modern marketplace:

- *Talent and expertise of top management.*
- *Talent and expertise of second tier management.*
- *Synergies.*
- *Niche*
- *Client base*
- *Geography*
- *Profitability*
- *Size*
- *Culture*

I have witnessed what you would call “distress” PR firms find a home and prosper thereafter. All they needed was a fresh start and a nurturing buyer. Some PR agencies get themselves into financial binds and don’t know how to get out of them by themselves. Buyers can see through these challenges and develop a strategy for the sellers to turn things around and prosper going forward.

And, let’s face it. Some PR agency owners are simply not good at running businesses. They’re great at developing client programs, managing accounts and managing staff. But when it comes to running their businesses profitably – forget it.

There are great deals to be made by buyers who can see the forest from the trees. And there are great deals to be made by sellers without bearing the cross of 20 percent profitability.