

SECRETS OF M&A

Understanding Quality of Earnings (QoE)



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Are you sure that the business you're trying to buy makes as much money as you think?

Are you sure you are selling your business for enough?

The best way to find out is to perform a Quality of Earnings analysis (also known as a “QoE” or “Q of E”).

Let's dive into what these analyses are...



What is Quality of Earnings (QoE)?



QoE is an assessment that separates a company's core earnings from non-core items, ensuring reported earnings are genuine indicators of operational success.

It answers questions about a business's financial legitimacy, sustainability, and reliability.



Who Prepares a QoE Report?



Typically performed by third-party accounting firms with CPAs, a QoE report demands specialized skills.

REMEMBER!

It's not a task for your usual CFO, Tax Advisor, or Bookkeeper.



When to Engage for a QoE?



Buyers initiate QoE after the Letter of Intent stage to validate expected returns.

Sellers can also engage pre-sale for a clear understanding of their business's value and potential perceived risks.



QoE in the Due Diligence Process



Though often used interchangeably, QoE is just one aspect of financial due diligence.

It joins analyses like Net Working Capital, Debt, and more under the due diligence umbrella.



Why is QoE Important?



- **Financing/Underwriting:**

Lenders and equity investors use QoE for creditworthiness and financial history validation.

- **Valuation:**

High-quality earnings positively impact a company's valuation for investment or acquisition.



- **Informed Decision-Making:**

Accurate financial insights are crucial for investors, lenders, and acquirers.

- **Risk Assessment:**

QoE is a risk management tool, revealing potential financial risks or uncertainties.



How is a QoE Performed?



The analysis involves adjusting financial statements for a more accurate earnings picture.

Key adjustments include normalizing earnings, removing non-operational items, addressing owner-related adjustments, factoring in synergies, and accounting for future changes or market adjustments.



Summary

QoE is a financial compass, guiding stakeholders to accurate assessments of a company's health.

Through meticulous adjustments, it offers a clearer view of a company's genuine earnings quality.

Investors, acquirers, and decision-makers can make more informed choices in the ever-evolving financial landscape with a QoE analysis.



Connect with QoE Experts

Curious about our process
and how we deliver
accurate, value-based
QoE in the lower and
middle markets?

**Reach out to learn
more!**

