HOW TO GET THE TOP VALUATION FOR YOUR BUSINESS

By: David Walsh

When a business owner considers selling the first thing they want to know is "How much is my business worth?"

As an investment banker, I don't like the question. I love it. It's one of the easier questions to answer in an entire process of landing a new client. And the answer goes like this:

"I don't know."

These are not words I'm afraid to utter because I will look unprepared or somehow lacking knowledge in my discipline. These are words I'm comfortable with because they are the truth. And they typically lead to deep discovery about the business.

Here is what I do know:

Valuations = Theory, Multiple Offers = Current Market, Closed Deal = Actual Value

No disparagement meant to the many fine people certified in business valuation. That's very necessary and complex work. You only need to look at a few conversations in a valuation group on LinkedIn to see how the experts debate over the many nuances of determining company value. But as an investment banker, discovering real value comes back to how you approach selling a business. Because intermediaries don't create additional or less value in a business: they find some number of buyers who see or don't see the value in a business.

That's why shared belief about value between an owner and advisor is so important. No business is perfect. Every business could be better. It's this fundamental **belief in the possibility of better** that will drive a buyer to pay a higher price than would be allowed for the security of historical cash flow alone. To be clear, the potential here cannot be blue sky dreaming. It's got to be factual, tangible, and accessible for the buyer to execute on.

The buying motivations of different types of buyers… particularly strategic vs.

Financial… differ greatly. Their ability to see or capitalize on the **belief in the possibility of better** can be vastly different. The result of these differences affects their ability and willingness to pay for those possibilities of better.

Understanding the different motivations of buyers leads to the contemplation of deal averages and outliers in two specific respects. The first is that over time deals in the lower mid-market fall into certain EBITDA multiple value ranges by total enterprise value (multiple times cash flow). For example, for the last ten years businesses with a value of roughly $1.8-4.6M in EBITDA have sold at an average multiple of 5.5. But buried within those averages and ranges are both high and low outliers.

Assuming an owner is selling right now, what can they do to be the high outlier?

High outlier values are typically driven by:

- Having a truly exceptional business, or
- Having a buyer who thinks that it is an exceptional business for *them*.

There are subtle differences between these two things (both of course still require good advisors to execute the deal). Features of a truly exceptional business often include recurring revenue, low customer concentration, low cap-ex requirements, contractual revenue, history of growth, defensible space, barriers to entry, non-cyclicality, high margins, scalability, well defined exit buyers, availability of bolt-ons or tuck ins, complimentary customers or distribution, obvious cost synergies, market position, tenured managers, and many, many more.

It's no wonder that financial buyers often poke fun at themselves for the well-known "Goldilocks" approach to investing. It goes something like this in the case of say, revenue growth for 'identical' opportunities. The financial buyer says "Business A isn't growing enough, we need higher growth."

Then they say "Business B is growing too fast, we don't want to pay for that growth and we don't know if it's sustainable."

And then finally they arrive at Business C. This third business is growing "just right."

In the revenue growth example, the just-right investment allows a financial buyer enough revenue growth to de-risk themselves while not paying too much for their belief in the possibility of better. The just-right investment often leads to the average outcome for the business owner of the average business dealing with one buyer at time (financial or strategic). Again, this is the case unless the business is exceptional or the buyer thinks the business is exceptional for them — *and* there is competition.

When there is competition, many buyers of both types lose interest. Why? Is it because the business has suddenly become *less exceptional*? No. It is because that buyer believes another buyer will pay more than they themselves are willing to pay. And why are other buyers willing to pay more? Because the other buyers believe it is an exceptional business *for them* based on their belief in the possibility of better.

The axiom for a business owner is simply this: **Value is in the eye of the beholder.**

How will you really find the value of your business with all the different buyers that might exist? **Get lots of beholders**. Let's go back to where we started:

Valuations = Theory, Multiple Offers = Current Market, Closed Deal = Actual Value

In order to discover the value possibilities the business has to actually be on the market, and have offers from buyers whose timing, funding, and motivation matches that of seller.

The crux to finding the true value of your business contemporaneously therefore lies in multiple offers from all categories of potential buyers *at the same time*. Multiple offers define the achievable range of value right now.

With the range of value established, a seller can comfortably identify which buyers believe the business is an exceptional business for them. Those are the outliers. And having more of them means they will compete for your business, potentially driving value up.

As a seller make sure you understand the features of your business and don't ignore the less than stellar attributes and how these appeal to buyers (or don't, as the case may be). Remember that no business is perfect and few are truly exceptional. Talk with advisors who want to spend time with you in bi-directional discovery. Discuss the different types of buyers and their motivations. Find out what's going on in the market. Get opinions from multiple credible sources and tend towards conservatism rather than believing smoke and mirrors multiples or values that less careful advisors may tickle your ears with (deal makers, accountants, and lawyers alike).

To learn the market value of your business and how it compares with similar businesses in the United States, click the following link:

https://nericap.bizequity.com