"WHAT IS MY BUSINESS WORTH?"

The answer to that question is very much open to perception rather than a finite number.

I asked a farmer the other day how was the weather to which he replied – "Great!" Reasonably, I had visions of green rolling hills and warm blue sky however, his continued response was – "its been raining the past 24 hours and looks like we will get another couple of days of it!" The point being his response was pretty much based on short term need. At a different time of the year, I would likely have received a different response however, as someone far less affected by the seasonal weather patterns my interpretation of "great" would likely be more sympathetic to a clear blue sky and warm weather.

The analogy above is simply to demonstrate that often the problem is with the generalised question that is either based on or, results in flawed assumptions.

For example:

- "I have increased my sales by 40% this year, so my business must obviously be worth more".

Assuming you made the usual profit on this extra work, your P&L may indicate an improvement however the practical result "may" be that you have not only not increased, but in fact decreased the "worth" of the business, at least over the short term. It may be that all of this extra work came from just one client who unfortunately drags the chain with payment. To get the work out on time you hired a couple of new people. This in turn has caused a cash flow problem for you and has resulted in your being overly dependent on that client who may or may not continue to provide this volume of work into the future. With all that work coming in, little if any time has been allocated to fostering other new clients or indeed, taking proper care of the other regular clients. You are having to work longer and harder to manage this growth with little if any extra, actually coming into your pocket.

The other end of the spectrum may be:

- "My sales are down by 5% however, my P&L shows a marked increase in the (operating) profit".

It may be the case that a conscious decision was made in regards to the type and size of client the business focussed on. Depending on the business model, even where standard profits per order are calculated, the number of and total invoice values can positively or negatively impact various aspects of the business such as productivity and therefore profitability. Obviously both play a key part in the worth of the business.

The worth of a business is actually a little like the worth of a painting. Sure, the painting just like a business can be independently valued at any time however its real worth can only be verified at each point of sale – if that was not the case we simply could not have auctions. Equally a painting may be "worth" a lot more than a buyer can afford to offer at that point in time so it becomes up to the seller to decide whether to accept that offer. The same goes for a business. If a seller, for any number of reasons, finds themselves having to dispose of their business within a set period then then they generally have to accept they will receive a discounted offer – i.e. an offer lower than the real worth.

Perhaps the more correct question would be :

- "How do I best determine the worth of my business?"

One way is to step outside of the business for a moment and begin to look in. Knowing what you know about the business ask yourself to honestly assess why and why not you would buy the business and if so at what price.

For most people this is a particularly difficult and often emotional task and frankly one that many find difficult if not impossible to undertake objectively.

- That specialised piece of equipment bought for a particular job (that perhaps did not eventuate) is still just like new so obviously worth what it cost (15 years back). All those loyal clients (many of

whom you may bump into down at the local club – reminds you that you must highlight to Fred about that few hundred bucks he still owes you for that job). The in-house systems you have built to track all the jobs in production, to say nothing of all the quotes you write. You may be thinking "someone who can see the potential should pay a fortune for this place…? Well as Darryl Kerrigan in "The Castle"® stated …tell him he's dreaming!

OK, so perhaps just a little exaggerated for the most part but an essence of truth none the less.

An alternative is to ask an external accountant for a fair sell price – generally this will be along the lines of averaging the past 3 years earnings and applying a multiple of 1 to 4 times earnings, so if the average profit was say $300K then the value range would be anywhere from $300 – $1.2 mil with some consideration in that range being given to the state of the balance sheet and value of equipment held. If you are a fan of "Shark Tank®" they offer an insight into the rapid assessment that can be made with a few simple rules of the figures offered as to the real value of a business. Shocking as it may be from the frank and forthright delivery from the Sharks as potential investors point-view! In many cases to the shock of the person seeking investment, unfortunately who in many case see just sunny blue skies rather than the true reality!

A simple lesson – experience and knowledge counts – like or loathe it – the "sharks" know the rules!

In any case rarely does (and in fairness can) this multiple of earning range take into account the non-financial factors of the business such as the business model, industry position, service levels, spare production capacity, skill sets of management a staff, volatility of market place, life span of product methodology, etc etc.

Nonetheless the price range method described above as a method of calculating worth is generally well accepted and forms the basis of price for a business.

Of course, engaging a (broking) firm to conduct a formal valuation of the business that encompasses a range of factors include those mentioned above. This valuation will obviously come at a cost and equally obviously cannot guarantee a buyer will pay the stated amount however does provide an objective assessment.

Ultimately it is the market that sets the price, with both internal and external factors contributing to the final outcome. The internal factors relating to how well the business is prepared and presented can be enhanced or offset by the external factors such as the state of the economy, availability of finance, numbers of active buyers etc.

The “market” generally has a number of segments and each of these will apply a different emphasis to the value proposition (perceived worth) of a business. Generally, the so called market can be divided into a few segments:

A) So called “trade sale” to a direct competitor. Generally this will yield the lower end of “worth” unless there is a compelling reason that actually adds value in which case it has “strategic value”. Often, the straight trade sale will involve business A) being acquired by a similar model business B). The reasons can be as simple as eliminating competition through to rationalising market position to give greater market share generally where one of the businesses is underperforming or the owners wish to retire. In this case the buyer must ask themselves the simple question of – what else can I do with the money I need to use to buy this business. For example, how would buying the business compare with buying better equipment or engaging more sales staff. Preferably the seller can demonstrate some aspect of the business that provides the buyer with greater advantage than alternative options to buying. In any case it is likely that the seller is defending their position which ultimately is likely to result in a lower rather than higher “worth”.

B) A strategically synergistic or symbiotic acquisition whereby the buyer recognises the acquisition will allow them to rapidly expand the products or services they offer. Often this is involving what is known as vertical market integration. A simple example may be a print equipment manufacturer acquiring an ink manufacturer so that they can offer both products to the same client. In this scenario the worth of the acquisition (seller) may depend on the external market factors as much or more than the internal factors

So, clear as crystal, right? – NO its not! The fact is … the only “real” price is the one ultimately agreed between the vendor, who (generally) feels the price is too little but is willing to accept and the buyer who (generally) feels the price it too much but is willing to pay.

The cornerstones are having a solid story backed up by quality financials as your greatest opportunity to maximise the sale price and return for your years of hard work. Other considerations to ponder and know that determine the outcomes include:

- Worth is relevant to type of buyer – direct competitor vs synergistic player wanting to expand into your product space
- Are any prevailing external factors at play a plus or minus influence – imports, change in technology, economic conditions, availability of funds to complete purchase., availability of trained staff.
- Have you reviewed the Internal factors such as organisational chart (dependence on owner operator), how robust the structure of your business is?, client retention, your (gross) profitability, the state of your equipment, how well does your company branding stack up, is your ongoing market relevance real? , how do you rate your business skill sets etc
- One way to measure worth is what outcome if you theoretically liquidate the business as is.
- Deliberate on several situations from a fire sale to a well-structured sale.

Why do you want to know at this point in time what your business is worth?

If you are considering selling what is the main driver – retirement, want a change, financially challenged? Each driver will impact the worth in a different way as will the urgency to complete a sale. The better prepared the business is the greater the likelihood of increased worth.

Have you recently (if ever) run a health check on the business – is your business well prepared to be able to best determine a fair worth.

The absolute smartest thing to do is talk to professional specialised broker – I sought assistance in putting this article together even though I bought several businesses in my 30 years owning a sign and print business. Michael O’Connell of AS Fisher Co is a consulting broker with extensive graphics industry experience who you can work with to establish and optimise the value drivers of your business. email Michael@asfisherco.com.au or fill in our online test www.controlzone.com.au/online_business_test