

## DEAL OR NO DEAL?

### Getting the figures right is crucial in the sale of any business

IT'S YOUR BUSINESS that you built up from scratch and you know every facet of its operation, so you should know how much it's worth - right? Not always. Small and medium business owners often have no clear idea how much their business is worth in market terms. So how should they go about calculating a true and accurate figure?

"Valuing your treasured business is a fascinating and highly argumentative topic with limitless variations," said John Carrasco, managing director of Wollongong-based business brokers Twenty Twenty SME.

"However, business owners generally have little idea of the true worth of their business. They either have too high an expectation on the value of their business or they under value. Numbers do the talking and the better their profitability is the more they can get when they place it on the market," John said.

To complicate matters there are many methods you can use to value your business. The simplest way is to add up all of your assets, cash, stock, plant and equipment and receivables and subtract your liabilities, such as any bank debts and payments due. This method is often used when an owner wants to liquidate a business. However, this doesn't take into account the ability of those assets to generate future revenue.

Capitalising future earnings is the most common method used to value small businesses. The method looks at the rate of return on investment (ROI) a buyer can expect to get from the business. With the ROI determined by the level of business risk, it is critical to determine what the future maintainable net profit is likely to be.

The value of the business also depends on its future net cash flows, discounted back to a present value at an appropriate discount rate. Called the discounted cash flow method, this is widely used in businesses that have sustainable contracts in place, such as engineering or contractors.

This method may not include the value for goodwill, which can come from physical features such as location, or from personal factors, like the owner's reputation or their relationship with customers or suppliers. Goodwill is the difference between the true value of a business



John Carrasco, managing director of Twenty Twenty SME Photo by Adam McLean

and the value of its net assets. It can be crucial to the value of retail and service-based businesses. However, do not be tempted to count it twice. The goodwill of a business can often be already factored into the profits.

The rule of thumb method, which multiplies earnings before interest and tax (EBIT), is often used to assess the value of businesses in certain sectors, such as medical practices or newsagents. A multiplier

is generally applied to the gross sales figure of the business. The difficulty lies in deciding which multiple to use, as it can be quite subjective as to what you think you will make in a year. Often different sectors have their own standard multiples. However, this is really just a guide only and needs to be used in conjunction with other methods.

Whatever valuation method you use, you should also look at prices

for recent sales of similar businesses. It makes sense to know what is happening in the market you're interested in. Do not try and value your own business. It pays in the long term to hire a broker who specialises in your type of business to do it for you.

"Generally we recommend that business owners plan at least 12 months prior to the sale of their business," said John. "However,

they need to ensure that any outside professional they use has the right skills to value their particular business."

**But whichever way you value your business you need to be able to back it up with reliable and verifiable data. For more information you can contact Twenty Twenty SME on 4203 2100 for an obligation free consultation.**

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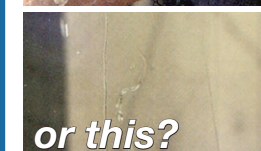
ClearShield is chemically inert or non-reactive with most substances. Working like 'non-stick' cookware, it resists staining and discolouration. A simple and economical aftercare program keeps ClearShield treated glass looking and performing like new.

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*like this?*



*or this?*

