Selling your business: some thoughts on how to get the best price

Much has been written in recent years about the retirement of baby boomers (born between 1946 and 1964). For many boomers a key component of their personal wealth is wrapped up in a business and a necessary step towards retirement involves selling the business.

Selling a business is by no means confined to baby boomers however. Businesses change hands all the time. Some “serial entrepreneurs” have been through the process many times. Prospective buyers may be (a) the current owner’s children or other family members, (b) employees in the business and/or (c) outside third parties. With the possible exception of sales to family members and employees, a common desire of the sellers is to maximise the price and optimize the terms of the sale.

So, what can be done to improve the sale price?

I suggest that the price at which a business ultimately sells is a function of

a) Its fair market value (FMV) and
b) The parties’ negotiating abilities.

Increasing the price is therefore really about both (a) increasing the FMV and (b) the seller improving his/her negotiating ability. Let’s look at each in turn.

(A) Increasing fair market value

Fundamental to increasing FMV is an understanding of what FMV is. Simplistically, it’s the risk adjusted value of the prospects in the business. To increase FMV we need to increase the prospects of the business and/or, at the same time, reduce the risks in the business, or at least the perceived risks. Both of these are very much easier said than done.

Enhance the prospects of the business

The prospects in a business are best represented by its sales. All else being equal, increasing long-term, maintainable revenues will always increase the value of a business. Assuming your sales process is already fairly good, there are two simple ways to increase sales:

a) Start selling the same products and services to new customers, or
b) Start selling new products to existing customers.

Do not make the mistake of trying to do both at the same time; once you have established a beachhead in a new territory, then would be the time to introduce new products. Alternatively, once you have proven your new products in an established home territory, then would be a good time to look for new markets.

Obviously costs play a big part as well in the prospects for a business. There is no point in gaining sales if added costs negate the gains. Costs are always a trade-off: higher salaries should give better productivity; higher rents should provide a more suitable location. Only the owner can decide where the benefits lie. The real key is not to lock the business into long-term costs (such as rent or salaries) that are both higher than they should be and cannot be changed with a change of ownership.

Lower the risks (and the perceived risks)

Many risks cannot be avoided or managed. However there are a few key areas that business owners can work on:

a) Ensure the financial statements for the business tell the real story. Prospective buyers rightly want to know the history of the business. Sketchy financials immediately increase the risk to the buyer and this will downgrade the value of the business in their eyes.
b) Ensure there is some continuity, or at least an adequate handover, in the management of the business. A business on its own cannot make decisions, only people can. It’s important that some of the people from the “old” business remain in place to help the new owner make day-to-day decisions in the first few weeks and months after the sale concludes.

c) Document the processes essential to the smooth running of the business, especially those processes under the control of the departing owner.
d) Ensure that all key agreements essential to the smooth running of the business are transferable to a new owner.
e) As far as possible, resolve all outstanding disputes, even those that will not impact the business under new ownership.

(B) Negotiating abilities

Negotiating is one business skill that does not correlate well with the level of education of the negotiator. “Street-kids” are often way more successful than well-educated folks with a tendency to over-analysis. In many ways good negotiating skills are innate, not learned. It’s difficult to learn how to be a street-kid.

That said there are a few key things that a business owner can do to assist themselves in an important negotiation:

a) Engage a trusted third party to advise you of the value of the business seen objectively.
b) Make sure you understand and are convinced of all aspects of the value in the business.
c) Consider your preferred style of negotiating and stick to it if possible: some shoot for the moon but settle for much less. Others add a much smaller margin but budge very little.
d) Try to get two or more prospective buyers. A single buyer will dictate the price; with at least two buyers the seller will have a better chance of achieving their desired price.
e) Allow sufficient time for the process. Never rush it.
f) Have a “Plan B” in case you cannot conclude a sale at a reasonable price. The need to sell at all costs will always lead to a lower final price.

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