The Overlooked Owner

A Key Factor in Determining Business Value

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We widely accept that determining the value of a business is a scientific process. Most people think that determining the value of a business simply involves looking at the books, sizing up the market, and doing quantitative analysis. It is also common to evaluate the management team and their skills and track record.

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The most overlooked aspects of determining business value are often the owner and their intentions, specifically, the number of owners, the reasons for exit, and the steps taken to prepare the business for exit. Based on our analysis of 1,511 business owners and their companies, the owner's personal reason for exit and the actions they have personally taken to exit play a significant role in the value of their business.

When comparing two similar businesses in the same geography and industry and of a similar size, if each owner has different reasons for exiting, they will likely have drastically different business values. Other factors that can impact the value of the business include the owner's steps to prepare for exit and the proportion of shares owned. When added up, these factors can predict up to 53 percent of the difference in the value of two seemingly similar businesses. Here are the key considerations we surveyed regarding an owner's motivation to sell:

1. Personal Motivation. The personal reasons for exit we evaluated included: a. "Looking to diversify my wealth," b. "I want to cash out," c. "I have a new business I want to start," and d. "I'd like to get involved philanthropy."

When the owner is personally motivated to move on to a new project or chapter of their lives, the value of the business is higher. One might conclude that this category of owners has met the goals they set out for themselves and the business and are motivated to exit to move to the next phase of their lives.

2. Personally and Professionally Peaked. The exit reasons included: a. "I'm just bored," b. "I want to spend time on a hobby," c. "I want to travel," and d. "I want to focus on my health."

3. Personal Crisis. The second category included exit reasons such as: a. "I'm burned out," b. "I have health issues," c. "I'm stressed and time-starved," and d. "I have a family crisis."

It appears that when the owner is experiencing a personal crisis, they are negatively impacting a buyer's view of the value of the business. The owner may be operating ineffectively due to their circumstances, and they are failing to meet their personal and business goals. They may be focused on trying to survive rather than harvesting the value of the business.

Included in this category is the reason: "Time to retire." This response negatively impacts the business's value slightly, but less than an owner's personal crisis does. Some business buyers might conclude that the owner desires to retire because the business is not meeting their envisioned goals, and the owner is hanging up the towel and, thus, has not been focused on preparing the business well for transition.

Of the three exit categories, our findings indicate that "Personal Motivators" and "Personally and Professionally Peaked" have little adverse impact on business value. In contrast, a "Personal Crisis" will almost always have a negative effect.

Here's an absolute fact: 100 percent of business owners will exit their business — one way or another. Entrepreneurs are eternal optimists and usually operate as if they are immune to personal crisis. However, in our work as mergers and acquisitions advisors, the most common reason a potential seller offers as their motivation to sell involves some personal crisis. While the business might be sellable, they have not properly designed and set it up for an optimum exit. And their personal circumstance is such that they don't have the ability, desire, or energy to invest another year or two in strategic design work to do so. The common refrain is: "It is what it is. Let's sell it." You can pretty much bet that the outcome will not be as attractive as it could have been with a little prior preparation.

The good news, however, is it does not have to be this way. There is a very well-developed and proven set of strategies a business owner can follow to prepare their business for sale under optimum price and terms. The value of a small business be grown systematically, and it can be done while optimizing short term profitability. These strategies are not theories; they are not taught in business school. They come from decades of doing actual deals in the marketplace, helping entrepreneurs, buy, sell and build companies.

The first step is to decide you want to design your business like you would a product. In fact, your business is not just a cash generation machine. It is your ultimate product. Adopt that mindset. Set up your business to operate as if it was for sale, even if you have no short-term desire to sell. Then, if a crisis arises, you'll be able to exit well. You can't always predict a personal crisis, but you can prepare for it. We've been helping entrepreneurs do this for over 30 years. Reach out if you'd like to learn how.

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