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How Owners Can Bridge the Valuation Gap

By Gary Ampulski (http://www.axial.net/author/garyampulski/), Midwest Genesis | May 4, 2016

There is nothing more disappointing when selling a business than realizing the gap between what you, as the seller want to put in your pocket and what potential buyers are willing to pay. But in a sale process there are more gaps than you might imagine. Many more.

There are **valuation gaps (http://www.axial.net/forum/whats-driving-the-valuation-gap-in-the-middle-market/)** generated by timing issues between a "buyer's market" and "seller's market." There are gaps in the value you as the owner perceive you've put into a business and the value a buyer perceives he or she can get out of it. Even the various approaches used to establish business valuation generate gaps in assessments.

There are also differences between what an owner needs to support a retirement lifestyle and what can be extracted from a transaction at the actual time of sale, as well as differences between an offer to buy, what the buyer pays, and what the seller ultimately gets. (Yes, death and taxes play a significant role in the outcome of a transaction.) And finally, the timing of retirement and buyer's vs. seller's perception of risk in the future growth and earnings flow for the business play a significant role is the size of the valuation gap.

Why These Gaps Exist

According to the Business Enterprise Institute, perhaps the biggest issue is that owners aren't quite convinced these gaps exist: at least not for them. And if owners aren't convinced that the gaps exist, they will be reluctant to invest any resources into bridging them.

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Harvard Business School Professor Howard Stevenson has stated that this common misperception is based on the inherent optimism and lack of knowledge of the entrepreneur. Separately these issues are unhealthy, but together they create a formidable obstacle to planning a successful transition ultimately killing a satisfying exit experience.

Undue optimism and lack of knowledge are extremely dangerous to an owner when they are forced to estimate:

- The current value and likely growth rate of their business,
- The future performance of their non-business assets,
- The amount of money they will spend in their post-exit lives,
- Their life expectancy, and
- How to look after loved ones in the event of disability or even unexpected death.

Typically, owners overestimate business value because they appreciate how difficult it was to start and build a business to its current state. They fall victim to the notion that what they put into the business is the same as what a buyer will get out of it. They are bullish on future business growth and investment performance. They are in denial about how much money they will need in retirement to maintain a desired lifestyle, and haven't given a whole lot of thought to how long they will live after they leave their companies.

This warped ecosystem shaped by optimism and ill-informed assumptions:

- Blinds owners to how wide the actual gaps are,
- Handicaps their ability to appreciate how long it takes to bridge the gaps, and
- Creates a toxic environment for disappointment, frustration, and failure.

Owners often use this optimism and lack of knowledge as license to postpone taking the actions necessary to create the outcome they desire. Until they understand that where they *think* they are is a far distance from where they *actually* are, and that where they need to be is even farther than where they *think* they need to be, it is business as usual and nothing will happen. Knowing — not guessing — what you have and what you actually need is key to closing the many gaps that exist.

How to Close the Valuation Gap

The goal of a business owner when considering a sale is to achieve perfect alignment (zero gap) between the various factors. For most owners, this is extremely difficult to achieve without the help of experienced advisors. The table below shows some of the many areas that skilled advisors can address.

Element	Advisor
Current Business Value	Appraiser
Funds for future lifestyle	Financial Planner
Post transaction Business Leadership	Succession Planner
Business Value Enhancement	M&A Advisor
Seller "Peace of Mind"	Transition Planner
Purchase Offer Vs "Take-Home"	Tax/Legal Advisor
Pre-Sale Process Coordinator	Exit Planner

(http://www.axial.net/wp-content/uploads/2016/05/ElementAdvisor.png?e1e745)

Selling a business is largely unchartered territory for people who have spent their lives developing processes that provide, market, and sell a product or service at a profit. But when it comes to implementing an effective process that markets and sells a business, the game changes dramatically. In nearly every case, it takes a team of experienced subject matter experts to navigate a course successfully out of the briar patch of legal, accounting, valuation, planning, and marketing considerations that are involved.

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An exit advisor can address the biggest gap of all: providing an understanding and knowledge on the difference between imagination and reality ahead of the negotiation process. It takes time and experience to bring everything into alignment and owners struggle to coordinate this unfamiliar process while still running the business. It was Mark Twain who said "It ain't what you don't know that gets you into trouble. It's what you know for sure that just ain't so."

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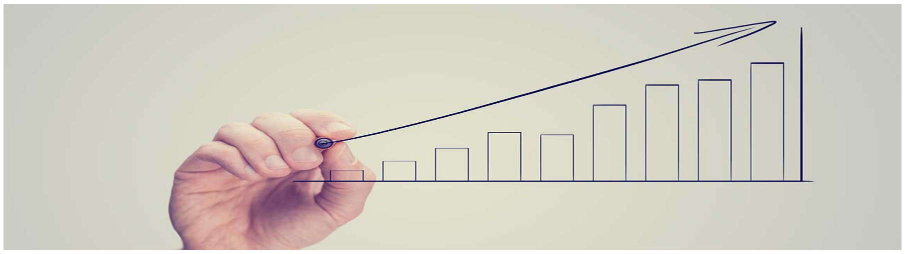
By Karen Sibayan | ***January 13, 2016*** ()



(http://www.axial.net/forum/what-is-ebitda-and-why-do-investors-care-about-it/)

During negotiations in an M&A deal, buyers and sellers look closely at several factors in order to agree on a price that properly captures a company's value. One of the closely examined metrics in this process is EBITDA, which stands for earnings before interest, taxes, depreciation, and amortization. EBITDA is used as a way...

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