Business Valuation Guide for Sellers

1. Why Valuation Matters

Knowing the value of your business helps you:

- Set a fair asking price
- Negotiate confidently with buyers
- Secure financing or loans
- Plan exit strategies

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2. Simple Business Valuation Formulas

A. Multiple of Earnings / Seller's Discretionary Earnings (SDE)

Used mostly by **small businesses** where the owner is heavily involved.

Formula:

Business Value=SDE×Industry Multiple\text{Business Value} = \text{SDE} \times \text{Industry Multiple}Business Value=SDE×Industry Multiple

Where:

- **SDE (Seller's Discretionary Earnings)** = Net Profit + Owner's Salary + Non-Cash Expenses + One-Time Expenses
- **Industry Multiple** = Typically 1–4x for small service businesses; 2–5x for auto repair, trucking, or small manufacturing

Example:

- SDE = $100,000
- Multiple = 3
- Business Value = $100,000 × 3 = **$300,000**

B. EBITDA Multiple

Used for **medium-sized businesses** with management teams and less owner dependency.

Formula:

Business Value=EBITDA×Industry Multiple\text{Business Value} = \text{EBITDA} \times \text{Industry Multiple}Business Value=EBITDA×Industry Multiple

Where:

- **EBITDA** = Earnings Before Interest, Taxes, Depreciation, and Amortization
- **Industry Multiple** = Typically 3–7x

Example:

- EBITDA = $200,000
- Multiple = 4
- Business Value = $200,000 × 4 = **$800,000**

C. Asset-Based Valuation

Used for businesses with significant tangible assets (equipment, real estate, inventory).

Formula:

Business Value=Total Assets−Liabilities\text{Business Value} = \text{Total Assets} - \text{Liabilities}Business Value=Total Assets−Liabilities

Example:

- Assets = $500,000 (equipment + inventory + cash)
- Liabilities = $150,000
- Business Value = $500,000 – $150,000 = **$350,000**

D. Revenue Multiple (Top-Line)

Used when **profits are minimal but growth potential is high**. Common in retail, service, and franchise businesses.

Formula:

Business Value=Annual Revenue×Revenue Multiple\text{Business Value} = \text{Annual Revenue} \times \text{Revenue Multiple}Business Value=Annual Revenue×Revenue Multiple

Where:

- Revenue Multiple = Typically 0.3–1x for small service businesses, higher for franchises or tech

Example:

- Annual Revenue = $500,000
- Multiple = 0.5
- Business Value = $500,000 × 0.5 = **$250,000**

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3. When Buyers, Banks, or Sellers Use Each Model

Here's a **flowchart in text form** you can later convert into a visual diagram:

```
Start
 |
 |-- Is the business small & owner-operated? --> Use SDE Multiple
 |
```

```
 |-- Is the business medium to large with management? --> Use EBITDA Multiple
 |
 |-- Does the business have substantial tangible assets? --> Use Asset-Based Valuation
 |
 |-- Does the business have low profit but strong revenue? --> Use Revenue Multiple
 |
End
```

Notes:

- **Banks:** Usually prefer EBITDA or asset-based valuations for lending security
- **Buyers:** Often use SDE for small businesses or EBITDA for larger, established businesses
- **Sellers:** Can use any method to estimate a reasonable asking price, often combining multiple approaches

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4. Tips for Sellers

- Adjust multiples based on business growth, location, and risk
- Include detailed financials (profit & loss, balance sheet)
- Consider non-financial value: brand reputation, customer base, and recurring contracts
- Keep formulas simple for a quick “ballpark” value, then refine with professional valuation if needed