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Ignorance Isn't Bliss: Professional Business Valuations



Business Valuation Stock photos by Vecteezy

Consider this scenario: A traveler wakes up in a foreign place with three items—the clothes on their back, a map in a language they can't interpret, and 10 coins. As they

begin walking down what they think is a path, a person approaches and says, “I can help you read this map and find where you’re going in exchange for one coin.” The traveler laughs, saying, “You want how much? That’s preposterous,” and continues down the path. As hunger and thirst set in, the path ends at an impassable ocean. The only option the traveler has is to turn back, but the traveler isn’t sure they have the strength to turn back and start over.

This scenario is similar to a common scenario business owners face when they balk at the cost of getting an accurate and professional valuation of their businesses.

What Determining Business Value Costs

Generally, a professional business valuation can cost between a few thousand dollars and \$20,000 or more. While that may seem like a lot of money, in the grand scheme of things, it’s more likely to be a small investment toward future success.

Determining business value isn’t a gut feeling. It requires understanding many variable elements about your business, the context your business exists in, and whether the business can function without you.

A professional valuation can clarify these elements by showing you why your business has the value it has. It will consider things like the strength of management, profitability, the clarity of processes, and the scalability of operations, among other internal elements. It will examine external elements, such as where the business is located, the state of the industry the business operates in, and whether buyers are interested in the kind of company you run at all.

And yet, many business owners predict that they can tell you what their businesses are worth without considering these elements.

What You Get for the Money

A professional valuation goes beyond simply providing a number. It often tells you why your business is worth what it’s worth, which can set you down a clearer path for future success.

The process that professional valuers use to determine value can provide clues about where your business’ strengths lie and how to leverage them, and where your business’ weaknesses are and how to strengthen them. Like a clear map, once you know where you are, it becomes much easier to determine where you need to go.

Professional valuations are much more objective and evidence based than guesses, gut feelings, and wishful thinking. This can help you avoid straying toward a path that may look attractive but is actually a dead end.

What Inaccurate Valuations Could Cost

The problem with business owners trying to determine business value on their own is multifaceted. But the biggest obstacle that self-valuation produces is that it can set you off course so early in the process that it’s hard to get back on track once you go too far.

For example, it may be tempting to say, “My business has produced \$3 million of profit over the past several years, so it’s probably worth around \$3 million dollars.” So, you begin creating a plan around that assumption.

However, profitability may be a direct function of you running the business. In that case, if you leave the business, it could have a negative effect on its profitability, which will then affect business value. If the plan you followed didn’t consider this element (and experience shows that this is a common blind spot for owners), it could send you so far off course that you need to start all the way over.

In addition to the functional challenges of determining business value on your own, there’s also the factor of bias.

You likely have an emotional investment in your business, which can cloud your judgment. It’s not uncommon for business owners to overvalue their businesses simply because it’s their business, which can set them down a path that diverges from their goals.

A business valuation can also require change, which can be difficult for business owners to accept if their business has been seemingly humming along well for years. Fortunately, professional valuations tend to be more descriptive than prescriptive. This means there may be several different ways to use the information to reach your goal. The key is having the right kind of information to pursue a path, rather than simply pursuing a path because it's there.

Cost vs. Value

The upfront cost of a professional valuation may seem high. In our opening scenario, the cost of a clear path for the traveler was 10% of everything they had.

But the long-term value of a professional valuation could lead you down a clearer path toward exiting your business on your terms. As a successful business owner, the cost of a valuation may likely be noticeably less than 10% of everything you have (especially because not all businesses need the most expensive kinds of valuations). And the accurate information it can provide could position you to strengthen the business you've built for years while preparing for an eventual exit on your terms.

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