The Downside of Just Milking It

If you have considered selling your business of late, you may have been disappointed to see the range of offers your business might attract from would-be acquirers.

According to the latest analysis of some 20,000 business owners who have used The Value Builder System/Sellability Score, the average offer being made by Buyers is just 3.7 times your pre-tax profit. Companies with less than a million dollars in sales attract significantly lower multiples, and larger businesses may get closer to five times the pre-tax profit. Regardless of size, private company multiples are still significantly less than those reserved for public company stocks.

Given the small "offer multiples", you may be tempted to hold on to your business and "milk it" for decades to come. After all, you might reason that if you hang onto your business for four or five more years, you could withdraw the same amount in dividends as you would collect from a sale and still own 100% of the business.

This logic - let's call it the "Just Milk It Strategy" - seems sound on the surface, but there are some significant risks to consider.

1. You Shoulder the Risk

The biggest downside of holding on to your business, rather than selling it, is that you retain all of the risk. Most entrepreneurs have an optimism bias, but you need only remember how life felt in 2009 to be reminded that economic cycles go in both directions.While business may feel good today, the next five years could well be bumpy for a lot of founders.

2. Disk Drive Space

If you think of your brain like a computer's disk drive, owning a business is like constantly running anti-virus software. Yes, in theory you can do other things like play golf or enjoy a bicycle trip through Tuscany and still own your business, although as long as you are the owner, your business will always occupy a large chunk of your brain's capacity. This means family fun, vacations and weekends are always tainted with the background hum of your brain's operating system churning through data.

3. Capital Calls

Let's say your business generates $500,000 in Earnings Before Interest Taxes, Depreciation and Amortization (EBITDA), and you could sell your company for four times EBITDA or keep it. You may argue it's better to keep it, pull your profit out in the form of dividends, and capture the same cash in four years as you would by selling it. This theory breaks down in capital-intensive businesses where there is usually a big difference between EBITDA and cash in the bank. If you have to buy machines, finance your customers, or stock inventory, a lot of your cash will be locked up in feeding your business and the amount of cash you can pull out of your business each year is a fraction of your EBITDA.

4. Tax Treatment

Depending on your tax jurisdiction, the sale proceeds of your business may be more favourably treated than income you would receive by paying yourself handsomely with the "Just Milk It Strategy". You may actually need to pay yourself $2 or $3 for every $1 you can net from the advantageous tax treatment of a business sale.

5. You Can Do Better

Finally, you may be able to attract an offer higher than three or four times your pretax profit. The businesses with who have a Value Builder Score (Sellability Score) of 80 + get offers that are, on average, 6.1 times their pretax profit.

If you'd like to get your Value Builder Score (Sellability Score), please let me know by replying to this email and I will make arrangements for you to complete the 13-minute questionnaire.
Or just click on this link to my website to learn more. [Value Builder Score]