

Using Multiples to Estimate the Value of a Business

In business valuation terms, a “multiple” is the relationship between Price and some measure of earnings. You may come across a rule of thumb that says “Accounting firms sell for between 1 and 1.25 annual sales”. In this example, the multiple (1 or 1.25) is multiplied by total billings for a year. You might also hear that “Accounting firms sell for 2.2 – 6 x EBITDA (Earnings Before Interest, Taxes, Depreciation, Amortization)”. In this case, you would calculate EBITDA and apply a multiple of 2.2 to see a low value range or a multiple closer to 6 to see a higher end value.

As business brokers dealing with small businesses, we frequently use multiples of SDE (Seller’s Discretionary Earnings). The rule of thumb for Accounting firms, using the SDE multiple, is 1 to 3 x SDE. The difference between SDE and EBITDA is the cost of one full time working owner. SDE multiples are lower than EBITDA multiples because SDE is a larger number (EBITDA plus one owner’s earnings). Multiplying SDE (see [How to Determine SDE](#)) by the SDE multiple will give you an estimate of the value of a business.

In addition to estimating an SDE multiple by using the Value Analysis Table (see [Estimating a Multiple](#)), you can find multiples for industries through sources like BizBuySell and Tom West’s Business Reference Guide.

Most likely you will get different values for the same business when you apply different rules of thumb. Generally, rules that are based on net profit measures (SDE and EBITDA for example) are going to give more reliable estimates than rules based on gross sales because they take into consideration the operating cost structure for the business. And even though you may use industry specific multiples for SDE or EBITDA, it is important to remember that there are many factors to consider and no two businesses are the same. Using multiples can give you a good idea of what the business is worth, but you may need more in-depth analysis of the business and its financials to determine the most probable selling price.