What is my business worth if I close? - by Dennis Serpone

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There are three major components that create the value of a restaurant.

First, and most important, is the good will as indicated by sales…traffic through the door. Without traffic, without customers spending money, you don't have a business…all you have is a facility. All evaluations of a business' value reference sales-minus expenses = profit. Profit creates value. Interestingly, buyers typically focus on the amount of sales to gauge a business' value before they look at the net profit. Simply put, a good operator can take a marginally profitable, or losing, business and turn it around making it very profitable. Conversely, a poor operator can take a decent business and run it into the ground if he doesn't know what he's doing. The common denominator in both scenarios is "the sales." If there are no sales, no good will, no value.

The second component of value is the lease. If a lease has at least seven or more years left, a buyer typically has enough time to recover his purchase price and make a profit. For example, if a buyer pays $150,000 for a business, and he has seven years left on his lease, the first $24,429 of net profit of his business is his own purchase price coming back to him. So, if a business has a net profit of $100,000 this year, the reality is that he's really only making about $75,000. However, that observation is mitigated if the business is resold for the same purchase price of $150,000, then the $100,000 per year is actually net profit. The other observation regarding the lease has to do with the percentage of sales as it relates to the lease or occupancy cost. If lease cost, as a percentage of sales exceeds 10%, it can be assumed that the rent is too high…the acceptable average today is about 7% of sales. The bigger issue has to do with the language within the lease that addresses a tenant closing…even for vacation. A legal opinion on this issue is important.

The third, and weakest component of value is the FF&E…furniture, fixtures, and equipment. Much like the example of buying a new car, once you drive it out of the dealer's showroom, it becomes a used car. In much of the same way, without sales, all you have is a restaurant full of used equipment. The world of used restaurant equipment is bursting at the seams.

With a well-organized kitchen, with a competent cooking staff, and with people coming through the door, success is within reach.

With an attractive dining atmosphere, a congenial staff, good food, and with people coming through the door, success is within reach.

With the emphasis on "people coming through the door"…without that you have no business.

The value of a business is the reflection of the moment. What are the sales…what are the expenses?

Without sales, the value of the "business" is a reflection of the value of the lease and the combined value of the "used furniture, fixtures, and equipment."

Our country is littered with thousands of closed restaurants…many of which will never reopen. Others will be bought by aggressive entrepreneurs for pennies on the dollar. The rule is that a restaurant should never close because you run the risk that your customers will be forced to go to your competition. You may never win those customers back. In today's environment, with so much at stake, closing, even for a short time, is the kiss of death.

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