How Much Is My Business WORTH?

FLOWER SHOP VALUATION
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38 YEARS
FINANCIAL INFORMATION, EDUCATION & CONTROL

Floral Finance®

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QuickTakes

Ideas You Can Put to Work Immediately

1 The Word 'But'

Try to eliminate the use of the word "but" in conversation. The word "but" indicates you disagree with what has been proposed. If you want to move toward agreement, try using the word "and."

Example: Which is more likely to lead to agreement? "You have a good plan, but I would like to review it." Or "You have a good plan, and I would like to review it."

2 Fire Prevention

Fire prevention is something we don't think of often. When was the last time you checked your fire extinguishers? Are they fully charged? Do your employees know how to use them?

Walk through your shop looking for potential fire hazards. Especially wiring and overloaded outlets.

3 Listen & Agree

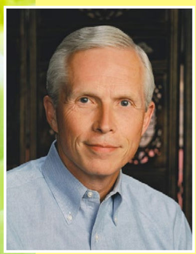
Whenever someone has a complaint, whether a customer or an employee, be sure to listen to what is being said. Make eye contact and convey empathy.

Agree on some level. Even if the customer gave you a wrong address, you can agree that an arrangement needs to be delivered to the right recipient.

Once a person knows she has been heard, she will be more ready to receive a solution.

FROM THE PUBLISHERS
OF FLORAL FINANCE®

MODEL YOUR VISION



How do you encourage employees to do what you would like them to do? It all boils down to inspiration.

You can set the rules. Write job descriptions. After all, shouldn't employees do what they are hired to do?

It's true that most employees will perform enough of what is expected to earn their paychecks. However, that's not all you really want.

You want employees who are enthusiastic. Who seek opportunities to serve customers better, or who want to perform at the highest level rather than be mediocre.

How do you get employees to work up to a level of excellence?

The answer is leadership—and true leadership means modeling the behavior you want to see in your employees.

A real leader of an organization is much more than a manager. Managers see that things are done properly and on time. Leaders inspire.

If you want your employees to be truthful and honest, you must be truthful and honest. If you want a pleasant, upbeat attitude in your shop, you must be pleasant and upbeat.

If you want employees to genuinely be concerned about customers and serving them, you need to demonstrate a commitment to customer service.

Acting only on the surface won't do.

You can't talk the talk in front of customers and then, when they have left, bad-mouth them. You have to believe in what you are doing and why, and talk about it with your team.

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On the cover: Teleflora's *Blooming Fall Bouquet*

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HISTORY

PHYSICAL PLANT

REPUTATION

INFLATION

A Shop Analy

Whether you are buying a shop, selling your shop or just hoping to maximize your potential, a good shop analysis is the place to start.

A business analysis focused strictly on the numbers is called a "valuation." It shows what the shop is worth today. (See the article on page 4 for more on valuations.)

However, some shops that look good on paper have serious problems or at least question marks when you go behind the numbers.

So, a deeper analysis also is important. This kind of analysis includes eight areas that, together, will help you evaluate the business' past, present and future.

1. HISTORY

How has the shop done over the past 5 years? Has there been steady growth? Stagnation? Or something in between?

Once you know how the business performed, identify why. What factors led to those results?

2. REPUTATION

Every shop has a reputation in three separate communities:

- Among other florists
- Among wholesalers
- With its customers

How do each of these groups see the business? No matter how much you want to change a shop's reputation, you are at least partially stuck with the one it has.

How can you find out what each group thinks about the shop? Do a survey. Ask them.

3. COMPETITION

Is your community already oversaturated with florists?

Is the competition growing or standing pat?

Are any new competitors on the horizon—for example, a larger florist opening a new location a few blocks away?

Try to uncover any negatives that will impact you. Ask your wholesalers what the talk is on the street.

4. PHYSICAL PLANT

Is the building owned or leased? If leased, is there any danger of losing the lease? An even more important consideration is whether

the current location is best for the business' long-term growth and health.

Next, look at the coolers. How many years have they been in service? What is their repair history? Are any warranties still in place? How many more years of service can you expect?

Don't forget other shop equipment. Cash registers. Computers. Heat and air conditioning. All the way down to buckets and shears.

Checking the equipment's book value on your balance sheet won't cut it. You need to know exactly what is there and how it will contribute to the business' future.

5. SALES

Have sales shown steady growth or gone through marked peaks and valleys?

Are there any new product lines? Do the new lines' sales justify the inventory levels?

What's the breakdown between online, phone and walk-in sales? Are any traffic disruptions that would hurt walk-in business on the horizon? For example, a shop with 40% walk-in sales that is located on a thoroughfare nearing a year-long widening project could have real trouble ahead.

6. EMPLOYEES

A retail flower shop is a personal business. Customers often base buying decisions on their relationship with the owner or employees.

Suppose several key employees are planning to leave. What will that do to the customer base?

On the flip side, can any tasks/roles be streamlined to cut payroll expenses? Review the shop's staffing plan carefully.

If you are buying the business, insist on a non-compete agreement that will prevent the former owners from walking down the street and opening a competing shop. (Non-compete agreements are difficult to enforce, so make sure you have an attorney draw up this document.)

7. EXPENSES

Are there any expenses you can cut without reducing service?

Start with big items that repeat month after month. A seemingly small overage in one month will be magnified if repeated over and over again.

Cost of goods sold (COGS) and payroll are the two prime categories to monitor to trim costs.

Depending on pricing formulas, COGS targets should be in the following general ranges:

Arrangements*	27% – 33%
Loose Flowers	40% – 50%
Green/Blooming Plants	33% – 40%
Gifts	45% – 55%

** Includes container and supplies. Fresh product alone should be 25% of arrangement sales or less.*

CAUTION: Base each product's COGS percentage on that product's sales—not the shop's total sales. In other words, divide COGS for arrangements by arrangement sales.

If any COGS percentage is substantially above the target, determine where the problems lie. Tighter control could mean real savings opportunities.

If the owner/manager takes a salary, the payroll target (including taxes and benefits) should be 30% of sales.

Compare the shop's wage scale to the community's prevailing wages. Could combining some functions take out a layer of management? A good manager can supervise seven to 10 people.

Or is the problem low productivity? Could fewer employees achieve the same sales and/or design levels?

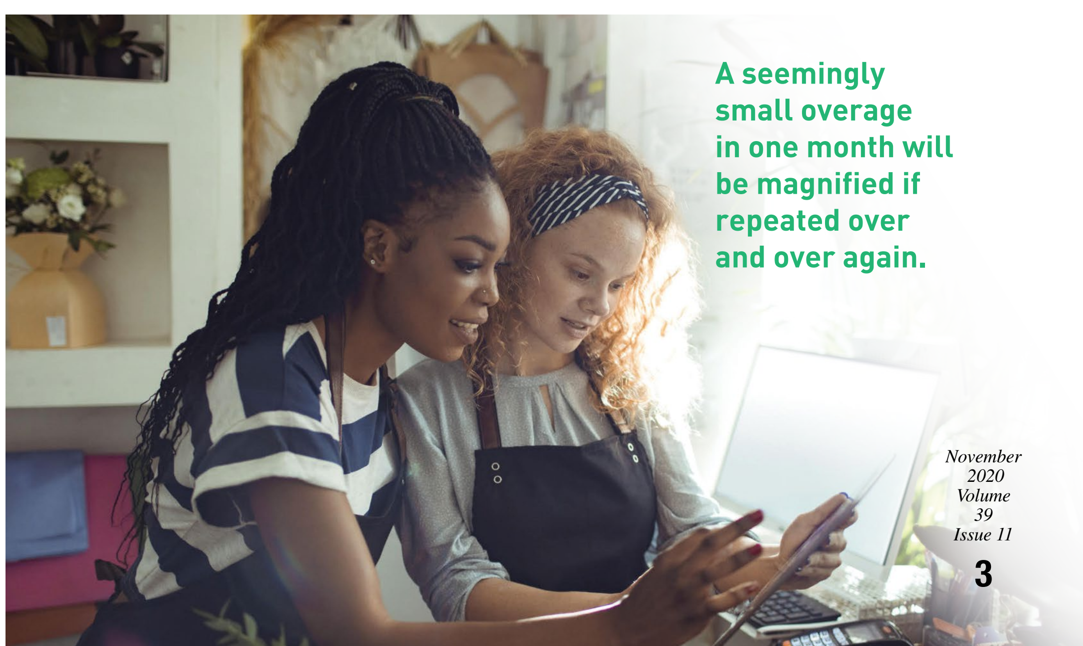
8. INFLATION

Increasing annual sales from $200,000 to $300,000 over 10 years may look impressive. However, the shop's "real" increase in business may be little or nothing. Retail prices may simply have risen to account for inflation. A 4% annual inflation rate will produce approximately a 50% sales increase over 11 years.

To get the true picture, have your accountant deflate the sales and profit figures.

You can also do your own informal studies. If the staff has remained about the same size, you can bet the "real" sales increase is minimal.

Also, look at the number of units sold. If you have sold roughly the same number of arrangements each year, you probably have only inflationary sales increases.



How Much Is My Business WORTH?

FLOWER SHOP VALUATION

This is the most frequently asked question *Floral Finance* hears from retail florists. The reasons are varied. A sale. A purchase. The buyout of a partner. An estate valuation. Whatever the driving force, at some point almost every florist needs to place a value on the shop he owns or the one he wants to buy.

Most small business owners will sell their businesses while they are still alive. Even if you're not ready to sell now, knowing the current value of your business will indicate how much you'll need to invest in improvements to maximize the sales price when the time comes.

There are just a few key points you need to understand.

WHAT'S TO BUY?

Two things: assets and the opportunity to generate an annual profit. The value of a business is determined by the fair market value of the assets plus the value of how much the business can generate in annual profit.

A quick look at the balance sheet outlines the assets of a business. Each asset needs to be viewed separately. What is the real fair market value of each? Fair market value simply means what a person would pay for it in its present condition. It's not unusual for most assets to sell for significantly less than they originally cost when purchased.

Accounts receivable is an asset that is very valuable; however, you must weed out all questionable accounts. Similarly, inventory should be examined to identify anything that is obsolete or of no value.

Fixed assets, such as furniture, fixtures, office equipment and vehicles, will generally need to be appraised to determine their fair market value. The depreciated value on the balance sheet may or may not reflect their actual fair market value.

Some shops own real estate: the building and/or land. Real estate is quite different from the operating assets of the business, and it should be valued separately from the rest of the business.

The fair market value of the assets sets one of the two numbers you need. The next number is the value for the business itself: How much profit can it earn each year?

NEXT STEP

Sales levels and profitability are the basis for determining the value of the business operation itself. Sales represent the opportunity for profit. The higher the sales, the greater the opportunity. The greater the opportunity, the more the business is worth.

Rarely is a retail flower business worth more than 40% of its annual sales volume, and that amount requires a net profit of 10% before taxes. Consequently, 40% of annual sales volume usually sets the top price for the business portion of the total valuation. Of course, in using these figures, sales and net profit must be defined properly.

Even if a shop has no profit, the sales volume is worth something. You'd clearly prefer to have a shop doing a million dollars a year over one doing half that much, even if it showed no profit.

At a minimum, a shop should be worth 10% of its sales volume.

To summarize, there is a fair market value for the assets alone and for the value of the profit-generating ability of the business. The minimum value for the profit-generating portion is 10% of sales. The maximum will be around 40% of sales.

Where you land in that range is a function of bottom-line profit before taxes. More on that later.

DETERMINING ANNUAL SALES

Sales must include all product and non-product sales minus any discounts. Outgoing wire orders need to be included at the 20% sending commission, and incoming wire orders need to be netted to the 73% that the florist receives from the wire service.

The recommended way to handle incoming wire orders is to enter the full value in the appropriate product and delivery categories, and then enter a negative 27% of the gross order in the wires-in commissions account in the non-product section of sales. That nets to 73% for sales purposes. This method keeps the full value in the product category in order to get accurate cost of goods sold (COGS) control.

This treatment of sales is the industry standard to which the various benchmark formulas apply.

DETERMINING PROFITABILITY

Once sales have been handled properly, COGS and expenses need to be checked.

For COGS, find out when the last physical inventory was taken. Normally, one will be done at the end of each fiscal year. You want to make sure that COGS accurately reflect the products that were sold and that inventory is not overstated.

On the expense portion of the business, you will want to check four items closely: depreciation, interest, facilities expense and owner/manager compensation.

If depreciation is over 3% of sales, it is probably due to an accelerated write-off of equipment. Change the accelerated amount to a normal annual amount of depreciation.

Take any interest off the expenses. A properly capitalized shop does not have to pay interest.

If the shop or the shop owner also owns the building, check the total cost of facilities expense. Is a fair market value being charged for rent? If not enough is being charged, adjust facilities expense up to approximately 8.5% of sales. (The average florist pays 8.5% of sales for facilities expense.)

The way in which the owner is compensated can have a significant effect on the profit of the business. Some shops pay the owner a salary. In others, the owner only takes a draw, depending upon the profitability of the business. Salaries show up as an expense but draws don't. Your goal is to get the owner compensation reflected at a standard level—not too high and not too low.

Start by identifying all expenses that are directly related to compensation to the owner. Look for salary and benefits, such as cars, health insurance, life insurance, club memberships, excess travel, excess entertainment, etc. Back all of these out of the expenses of the shop.

Next, add in a reasonable compensation for someone doing the owner's job. In a smaller shop that has less than $500,000 in annual sales, you can put in a figure equal to 10% of total sales. In larger shops (above $500,000 in sales) take $50,000 for the first $500,000 in sales and add 5% of the sales above $500,000.

After these adjustments are made, the net profit will reflect how the business is really doing for valuation purposes. To get a realistic view of how the business has done over time, look at the last three to five years and make the same adjustments.

HANDLING LIABILITIES

Every business has liabilities. They are found on the liability side of the balance sheet, and eventually they will have to be paid. By someone. Current liabilities are such things as payables, payroll and sales taxes. Long-term liabilities are all the loans the business has taken out to buy vehicles, other operating equipment or just for operating capital.

Buyers seldom want to take the liabilities because when a business is purchased, the new owner wants to know exactly what is being bought.

The value of the business is determined by the fair market value of the assets PLUS the value of how much the business can generate in annual profit.

Hidden liabilities are always a real possibility. Company debt about which the buyer wasn't informed. Or a legal liability arising out of an old, unresolved conflict with a vendor or customer.

Because of the risk of hidden liabilities, as a rule, buyers want to do "asset purchases" only. Instead of buying the whole business (the stock of the company)—liabilities and all—they just want to purchase the assets.

The former owner normally takes the responsibility to settle all the old liabilities out of the proceeds of the sale.

BUYER EXPECTATIONS

A buyer is not just making a purchase. He is making an investment. He wants a return on that investment.

In addition, if he is going to manage the shop himself, he expects a reasonable salary for his services. Remember, a salary doesn't substitute for a return on the investment.

Investors can normally get a 5% or higher return on an investment at virtually no risk or trouble. Simply deposit the money in a savings account or purchase certificates of deposit.

It stands to reason, therefore, that most potential purchasers will want a higher return for investing in something that has considerably more risk and trouble. Buying a flower shop certainly fits that description.

Most buyers of flower shops (or other small businesses) should expect a minimum return of 25% on their investment. That means, from an earnings perspective, you could expect to sell a flower business for no more than four times its actual net profit.

This ties back to that 10% to 40% of sales price range. An excellent profit in a retail flower shop is 10% of sales. Four times 10% is 40% of sales.

PROFESSIONAL HELP

Don't try to do a shop evaluation by yourself. Spending some money to get professional assistance is well worth it. There is usually a lot at stake in a valuation. It is important that it be done correctly.

Floral Finance Business Services is one industry resource for flower shop valuations. For more information, call 918-289-1574 or send an email to plgoodman@aol.com.

Ruining a Great Customer

Too Much of a Good Thing

It happens all the time. A florist gives "extra value" to keep a good customer happy. A few more flowers. Or an add-on at no additional charge. The thinking is the extra benefits will build the customer's loyalty.

What happens?

The customer ends up with unrealistic expectations. Any future "normal" arrangement or service won't be enough. The formerly happy customer becomes more demanding and less satisfied. Before long, she is looking for another florist.

The shop's reputation and bottom line suffer. It's the law of unintended consequences.

PLAYING FAVORITES

Special customers deserve special treatment. Everyone would agree with that principle.

The trick is to do it without creating unrealistic expectations or abandoning your pricing formula.

To protect yourself, start with one simple rule:

Give discounts instead of extra product.

This approach will accomplish several important goals:

- Special customers will get extra value.
- They will know they are receiving special treatment because they will see the discount.
- They will know they can't expect similar treatment from another florist.
- You will be able to follow your normal pricing formula, thereby maintaining control of your cost of goods sold (COGS).

WIRES-OUT DISMAY

Outgoing wire orders can be another problem with customers.

Here, it's not a lack of special treatment that creates ill will. The issue is the nature of the orders themselves.

Outgoing wire orders are filled by florists in other communities that may have very different pricing policies and cost structures.

Take the time to "teach" your customers what they can expect with outgoing wire orders.

A $60 arrangement prepared in another city may be larger or smaller than if you filled the order locally. Generally, florists in larger cities must charge more because their costs are higher. From lease rates to wage rates, everything is more expensive in a big city.

Don't expect a recipient to be "wowed" by the size or flower count of a $60 order you send to New York. It won't happen. The customer will need to spend more.

Education is the key. Take the time to "teach" your customers what they can expect with outgoing wire orders.

Find out their goals for the order. What sort of a statement do they want to make? What sort of impact do they want to achieve? Then, show what it will take to accomplish their objective. Realistic expectations will prevent a letdown.

Also, teach customers the value of "open orders." Allowing filling florists to use the flowers they have in abundance will yield better value for a given price.

THE VALUE

You may still have occasional complaints from your special customers. However, as long as you always give good value, these complaints will be few.

Go ahead and show special customers a little TLC. Just do it in a way that minimizes the potential pitfalls.

Signing a Lease

You're looking for a bigger place for your flower shop, trying to renegotiate your existing lease or selecting a site for a brand-new shop.

Of course, you're concerned about the space itself and the rental rate. But don't get distracted and ignore the terms of the lease you are asked to sign.

The lease document defines both parties' rights and responsibilities. Every line is important – even, and often especially, the ones in fine print. Ambiguities can cause trouble down the road. A few precautions at the front end will help you avoid embarrassing (possibly expensive) problems later on.

The following are the terms you should give extra attention to.

BUILDING SERVICES

As a florist with specific electrical and temperature requirements, building services is a crucial area.

Do the building services meet your needs? Will the electrical system support your refrigeration equipment? Do the hours when the landlord will supply heat and air conditioning square with your shop's hours?

If the landlord runs into financial difficulties, operating expenses will be the first cuts. Carefully review the minimum level of services the lease requires of the landlord. Make sure you're protected.

NEIGHBORS

This is a special concern for florists in strip centers or similar multi-store complexes.

The lease should prohibit the landlord from leasing nearby space to a tenant whose business would compete with your shop. Define this restriction broadly enough and specifically enough to be meaningful to you.

NON-DISTURBANCE

The landlord may decide to sell the building during your lease period. If so, the lease should specifically and automatically bind any new owner (or a bank if it forecloses on the property) to its terms.

You can't take the risk of a new owner coming in and renegotiating the favorable terms you obtained from the original landlord.

SUBLEASING

You sign a 5-year lease. In 2 years, you've outgrown the place. Or a health crisis makes the rent payments more than you can manage.

As the lessee, you're ultimately responsible for making sure the landlord gets paid. But the lease should allow you to sublease the space. The landlord may be able to require that any subtenant meet some minimum standard of reasonableness. But avoid anything more stringent than that.

SQUARE FOOTAGE

Most, if not all, of your rent will be based on the space's square footage. But do you understand what you're really paying for?

"Usable" space is the square footage within the walls that define your shop. But the rent may be based on "rentable" space. This is the usable space plus an allocation for common areas.

One building may add 11% to the usable space before rent is calculated. Another may add only 7%. Do the math. See which deal will give you more for your money.

FIXTURES & IMPROVEMENTS

If you plan to build in a refrigerator or make other improvements, what rights do you have to this property at the end of the lease?

Often, all leasehold improvements belong to the landlord.

ESCALATION CLAUSES

It's not uncommon for the lease to allow the landlord to pass along certain increased operating costs during the lease term. Make sure you understand how much, how often and when your rent might rise as a result.

AMBIGUITIES

If there is any term in the document you don't understand, get it clarified. Before you sign.

FAMOUS FINANCIAL WORDS—ANONYMOUS

"A salesman is one who sells goods that won't come back to customers who will."

"A nickel goes a long way now. You can carry it around for days without finding a thing it will buy."

"A sign in a secondhand store: We buy old junk. We sell antiques."

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INQUIRIES & ANSWERS

Letters

PAYABLES

"My accountant keeps saying I turn in the wrong payables list every month. Can you give a clear explanation of 'payables'?"

Certainly.

A payable results when you purchase something in one month but don't pay for it that month. The expense is something that is yet to be paid.

The timing and recording of payables are where the confusion usually lies.

Suppose, for example, you buy $3,000 worth of flowers in March and charge the purchase. In April you get the invoice, which requires payment before the end of the month.

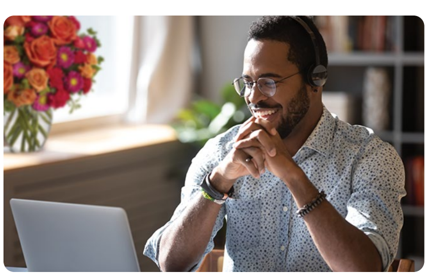
Isn't that an April payable? Not from an accountant's point of view. It is a March payable. The month the purchase was made is the month assigned to the payable.

EMAIL MARKETING

"Are there some general guidelines about email marketing?"

Try these:

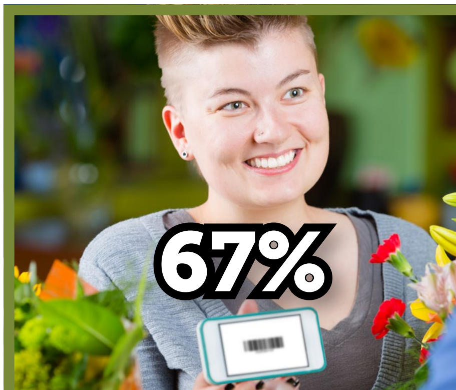
1. Only send emails to persons who have requested or signed up for your emails.
2. Be consistent in when you send emails. Pick a schedule, and stick to it.
3. Send business-to-business (B2B) emails Tuesday through Thursday. The best times of the day are 9–10 a.m. and 1–2 p.m.
4. Send business-to-consumer (B2C) emails Tuesday through Thursday from 6–9 p.m. or between Friday evening and Sunday afternoon.
5. Put your company name in the "From" line. Familiarity with the sender is the number one reason someone will open an email. Once you pick a name, keep it.



6. Don't use all caps or multiple exclamation marks in the subject line or body. Doing so will trigger spam filters.
7. Build your distribution list at every opportunity. Place a sign-up form at the checkout counter. Ask every caller if you may add them to your list.

NORMS

COUPONS



Two-thirds of American households use coupons—87% of which help the user save money and 30% of which introduce a new product or service.

Almost half of all American households use coupons on food or grocery products. That's easily the most common type of coupon.

Nearly 50% of American adults say a coupon is likely to draw them to a store they don't normally frequent.

Email marketing is the fastest growing coupon trend. Emails with coupons get opened 50% more frequently than those without.

Source: Experian Marketing Services

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