

Valuing Cafes and Restaurants

The hospitality industry is one of NZ's biggest industries, with sales of \$6.5 billion per annum and providing 100,000 jobs through almost 15,000 outlets!

Cafes and restaurants are a unique blend of manufacture, service, and retail. They encompass a wide range of concepts and menus ranging from "fast food" to "fine dining" with new trends constantly appearing.

They are a simple business but not an easy one.

Cafes and restaurants are among the most difficult businesses to value. There is no formula. Each needs to be considered on its own merits. One problem is that they are cash businesses and a high percentage do not show profits over and above the owner's time. We suspect that many financials do not show the true earnings.

As always, all three approaches should be considered (asset-based, earnings-based, and market-based) and various methods applied. Capitalised Earnings or DCF can produce results that bear no relationship to the realities of the market. Asset-based approaches may be equally dangerous. Set-up costs can be very high, but much of these can be leasehold improvements with little recovery if the business fails. It does not matter how flash the set-up if it doesn't generate sufficient income.

The **market approach** is the most accurate for café and restaurant valuations as it is based upon actual transaction data and reflects current market activity. We find the most appropriate approach is the **multiple of sales** – but the approach needs to be used with great caution. We have data on hundreds of actual sales but you need to be careful that you are comparing "apples with apples". Our statistics provide us a guide – but there is a very long list of **value modifiers** to apply to each business. As with all valuations it is critical to obtain **full information** before reaching an opinion.

Value modifiers include:

- Lease
- Financial Accounts
- Historic profits
- Concept
- Hours of operation
- Rental
- Menu
- Location
- Sales trends
- Gross profit
- Plant condition
- Parking
- Labour supply
- Licensing
- Owner profile
- Food/liquor ratio
- Zoning
- Competition
- Finance
- Potential
- Accommodation

Arriving at an accurate opinion of value for a hospitality business will involve many subjective judgements – that's valuation, as opposed to calculation.

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