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TRANSACTION ADVISORY SERVICES

Understanding Valuation Multiples

What they are, what moves them, and what a first-time seller should expect

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Introduction

Most owners arrive at a number before they arrive at an advisor. They search their industry, add "EBITDA multiple," and the first credible figure becomes the anchor for every conversation that follows.

If you are reading this before that anchor has set, you have an advantage most sellers give away. If you already have a letter of intent on your desk, the anchor is set, but the price in it is not the price you will receive, and most of what decides the difference is still ahead of you.

Either way, that anchor was almost certainly drawn from businesses nothing like the one you own.

Small business sales tracked by BizBuySell closed at 2.7x cash flow in the second quarter of 2026. Private equity deals between $10 million and $500 million, tracked by GF Data, averaged 7.2x earnings across 2025. Both numbers are correct. They measure different worlds. Anchor to the wrong one and you spend the next year either insulted by every offer you get or disappointed when the real ones arrive.

This paper covers what a multiple is, what moves it, and what you can still change before you go to market.

PART I

What a Multiple Is (and What it is Not)

What a multiple is not

First, let's start with what a multiple is NOT so we can clearly define what it is. A multiple is not a formula. You cannot look up your industry's number, multiply it by your earnings, and arrive at what your company is worth. It is the output of negotiations that already happened, not an input to a calculation you can run yourself.

It is not a fixed property of your industry or of your business. Two companies in the same trade, in the same town, earning the same profit, routinely sell at different multiples. Nothing about your sector entitles you to a number.

It is not a guarantee. Every published multiple describes a deal that closed under terms you cannot see, between parties whose reasons you do not know.

And it is not precise. The averages in this paper carry a decimal because that is what the underlying datasets computed. Your own outcome will not arrive at that resolution. Read 5.9x as "somewhere near six," because a single sale is a negotiated result, not a measurement.

What a multiple is, then, is shorthand. The rest of this section explains what it is shorthand for so you know how to interpret it.

What a buyer is buying

When someone buys your company, they are paying for the profit it will produce after they own it. The equipment, the building, the customer relationships, the crew: all of it matters, but only because it is the machinery that generates that profit.

So the obvious way to price a company is to forecast what it will earn going forward and decide what that cash stream is worth today. Professionals build models exactly like that, and the logic is sound. The practical problem is that nobody can truly forecast a private company’s earnings ten years out. Adjust performance in year six and the value moves by millions. The method is rigorous in structure and fragile in substance, which is why almost no private company sells purely on the strength of a forecast, especially one many years out.

The shortcut buyers use

A multiple is the market's workaround. Instead of predicting the future from scratch, you look at what buyers recently paid for companies like yours and reduce those prices to one ratio: purchase price divided by one year of earnings. Both halves of that ratio have more give in them than they appear to. Which earnings is settled shortly. Which year waits for Part III.

If comparable businesses trade around 6x earnings, that ratio already holds the judgment of hundreds of buyers and sellers who negotiated hard, walked away, came back, and landed there. Nobody sat down and calculated six. It emerged from a lot of people betting real money on their view of the future. Apply it to your earnings and you are borrowing their conclusion instead of building your own.

Real estate works the same way. Nobody thinks a square foot creates a house's value, but price per square foot lets you compare properties quickly and get close enough to start a real conversation.

What the number means

Read a multiple as **payback time**.

At 6x earnings, a buyer is saying they will wait six years to get their money back, assuming profits hold. At 10x, they will wait ten. Nobody waits longer unless they believe two things at once: that the earnings are dependable, and that they are going to grow.

That is the whole game. Once you see it, the rest of valuation stops feeling arbitrary.

Everything that raises your multiple makes future earnings more certain or more likely to grow. Contracts and recurring revenue. Enough customers that losing one is survivable. A management team that runs the place when you are not in the building. Books a stranger can verify without taking your word for anything. A growing market.

Everything that lowers it does the opposite. The business depends on you personally. One customer is forty percent of revenue. Demand collapses when the economy turns. The financials need explaining. Each one shortens how long a buyer will wait, because each one raises the odds that next year looks nothing like this year.

This is why two companies with identical profit sell for very different prices, and why the seller of the cheaper one rarely sees it coming.

Four different earnings figures

This is where deals get mispriced, because "earnings" hides four measures, and which one applies to you depends mostly on your size.

Revenue gets used when a business has little or no profit. Early-stage software companies get priced this way, as do businesses bought mainly for their customer list. For a profitable operating company it tells a buyer almost nothing, since two companies with the same sales can have wildly different margins.

Seller's Discretionary Earnings (SDE) applies to smaller owner-operated businesses. Start with profit, then add back everything you personally take out: salary, benefits, the vehicle, personal expenses running through the business. A buyer stepping in to run the company themselves captures all of it.

EBITDA, earnings before interest, taxes, depreciation, and amortization, applies once a company is big enough to run on hired management. The critical difference from SDE is that EBITDA does not add back your compensation. It assumes the business pays market rate to whoever runs it. A buyer at any real scale is not planning to sit in your chair, so they need to know what the business earns after paying someone competent to do your job.

Adjusted EBITDA is EBITDA minus what will not repeat or does not reflect ongoing economics. The legal settlement that happened once. The above-market rent you pay yourself for your own building. The relative on payroll who does not work there.

MEASURE	TYPICALLY APPLIED TO	THE DISTINCTION THAT MATTERS
Revenue	Businesses with little or no profit	Says nothing about profitability
SDE	Owner-operated Main Street businesses	Adds the owner's compensation back
EBITDA	Companies run by hired management	Assumes a market-rate salary for your role
Adjusted EBITDA	Middle market transactions	Normalized for what will not recur

Table 1. The four earnings measures, and where each one belongs.

The market observes that line consistently. The IBBA and M&A Source Market Pulse, a quarterly survey of business brokers and M&A advisors, reports that Main Street deals price on SDE while lower middle market deals price on EBITDA. If someone quotes you an SDE multiple for a company an institutional buyer will purchase, something has gone wrong in that conversation.

The gap is not academic. Your company can show one number on the tax return, a higher number as SDE, and a different one again as adjusted EBITDA. Apply the wrong multiple to the wrong measure and the answer is off by a wide margin, usually toward disappointment.

Compare like with like

A multiple is one number divided by another: a price on top, a year of earnings on the bottom. When you measure your company against a published multiple, you are comparing two of those ratios. The comparison only holds if both were built the same way.

Two things can quietly differ.

What counts as earnings. The multiples you find were almost certainly built on adjusted EBITDA, with a market salary charged for the owner's job and one-time items stripped out. Apply one of those multiples to the profit on your tax return and you are dividing by a different number than the market divided by.

What counts as price. Some sources report the whole value of the business, including debt the buyer takes on. Others report only what reached the shareholders. A multiple built on one does not transfer to the other.

Get either wrong and the answer moves by millions without anything about your business having changed.

Go back to price per square foot. It only tells you something if both houses measured square feet the same way. Count the finished basement in one and not the other and the comparison quietly stops working, even though both numbers look equally precise.

This is also why two credible sources can disagree about what your industry is worth. Usually they are not disagreeing about your industry at all. They built their ratios differently.

PART II

Why Your Number Is Not the Number You Found Online

Size moves the multiple more than industry does

This is the least intuitive finding in the market, and among the best documented.

GF Data tracks private equity transactions between $10 million and $500 million, drawing on deals reported by more than three hundred sponsor firms. Through the first nine months of 2025, platform acquisitions in the $10 million to $25 million range averaged 5.9x EBITDA. Deals in the $100 million to $250 million range averaged 10.0x. Both figures come out of the same dataset over the same period, measured the same way, which leaves size as the only thing separating them.

FIGURE 1 / AVERAGE PLATFORM MULTIPLE BY ENTERPRISE VALUE

GF Data, platform acquisitions, first nine months of 2025. Both figures drawn from the same dataset over the same period.

The reason is certainty again. A larger company has outgrown the risks that make a smaller one fragile. More customers, so losing one is survivable. Managers with real authority, so your departure is not an existential event. Systems rather than habits, reporting rather than bookkeeping, enough market presence that a competitor cannot simply take the work. A buyer paying 10x is not being generous. They are paying for earnings they can forecast.

So if your company earns $2 million and you are comparing yourself to a competitor that earns $20 million, you are not in the same market. You will not get the same multiple, and the gap will be wider than you expect.

What industry tells you

Industry matters, but not because buyers have favorites. It is shorthand for three characteristics, and those characteristics drive price.

How reliably earnings turn into cash the buyer keeps. Two companies can report the same EBITDA and deliver very different spendable cash. One reinvests constantly in equipment, carries heavy inventory, and waits ninety days to get paid. The other collects monthly in advance and owns almost nothing. The second is worth considerably more per dollar of reported earnings, because more of those dollars arrive.

How predictable next year's revenue is. A business with maintenance contracts or a service book that renews starts each year with much of its revenue already committed. A business that starts every January at zero does not. Predictability is what buyers pay the most for, because it directly shortens payback risk.

Whether the sector supports consolidation. This one rarely surfaces in an owner's own research, and it matters enormously. Some industries are thousands of small operators serving local markets with no dominant player. Those attract buyers whose entire strategy is assembly: buy many small companies, combine them into something large, and sell the combination. That creates a durable form of buyer demand that does not exist in sectors already run by a few national players.

Residential HVAC shows all three at once. Demand is non-discretionary, since heating and cooling fail regardless of the economy. Maintenance agreements make revenue predictable. And the sector remains fragmented, which has drawn serious institutional capital. Blackstone's 2026 agreement to acquire Champions Group carried an implied enterprise value near $2.5 billion on roughly $140 million of EBITDA, about 18.5x, according to Bloomberg's coverage. Altas Partners' acquisition of Redwood Services implied roughly 17x.

Those are platform-scale numbers, and no individual contracting business should read them as its own. But they explain why a company building such a platform can rationally pay a strong price for an operator far too small to command that multiple alone. A dollar of earnings is worth more inside a large, professionally managed platform than inside a single shop. The buyer is paying for your earnings and for what they become once absorbed.

Where the crowd overshoots

When enough well-funded buyers chase the same kind of company, sale processes get genuinely competitive. Several bidders appear, you can run a real auction, and the price gets set by the most aggressive buyer rather than the typical one. That premium is real, and if you own a company in a sector attracting capital right now, you may well capture it.

Be clear about what that premium is and is not. Part of it reflects real economics: better cash conversion, better predictability, a genuine consolidation opportunity. Part of it reflects nothing but the number of bidders in the room this year, which is a function of capital cycles rather than of your business.

Not every repricing is a fad. The market's rerating of recurring-revenue businesses over the past fifteen years was a correct read of genuinely different economics. Telling a permanent repricing from temporary crowding is hard in advance, and neither side does it reliably.

What is certain: when your price depends on how many buyers are looking at your sector this year, that part of your value is not something you built and not something you control.

What the buyer is betting on

How a buyer arrives at their number explains most of what happens next.

Institutional buyers do not evaluate companies in isolation. They work from a thesis about a sector: that home services generate recurring maintenance revenue, that specialty contractors serving data center construction are riding a durable buildout, that a particular kind of distributor has pricing power its owners have never used. The thesis is what justified raising the capital in the first place.

Your company gets priced against that thesis. The multiple you are offered reflects the buyer's assumption that your business has the characteristics the thesis requires. Early on, before anyone has examined your records in detail, that assumption rests on a management presentation, a financial summary, and a conversation.

Diligence is where the assumption gets tested.

Take an electrical contractor approached by a buyer chasing data center exposure. The opening valuation reflects that thesis. Then diligence examines the backlog and finds two data center projects in a book that is otherwise general commercial construction, with the data center work carrying no better margin than the rest. Nothing was misrepresented. The buyer's assumption was simply broader than the facts supported.

The pattern repeats. An HVAC business priced on service revenue that turns out to be mostly new-construction installation. A services business priced on relationships that belong to the founder personally.

Where the gap lands

When diligence finds that gap, the intuitive expectation is that the buyer cuts the multiple. That is usually not what happens.

The headline multiple survives, because it was set against sector comparables and the buyer's investment committee approved it on that basis. What changes is the number the multiple gets applied to, and the terms under which it gets paid.

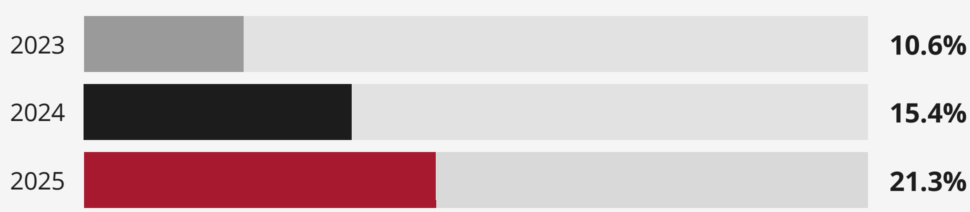
Earnings move first. Add-backs you proposed get rejected. Expenses you called one-time turn out to recur. Costs the business will carry under new ownership, like market compensation for your role or the systems investment deferred for years, get built into the run rate. Adjusted EBITDA drops, the price drops with it, and the multiple never moves.

Structure absorbs the rest. Cash at closing shifts into an earnout that pays only if the business performs. The buyer asks you to roll part of your proceeds into equity in the new entity. Escrow and holdback provisions expand. Each one cuts what you receive at closing and pushes risk back onto you, without touching the number in the press release.

This is why sellers describe deals in terms that do not match their bank statements. The multiple was 7x. The proceeds were nowhere near 7x the earnings anyone discussed at the outset.

This is measurable. Axial, a transaction platform serving the lower middle market, publishes an annual analysis of deals that died after a signed letter of intent. Across 75 failed transactions in 2025, the leading cause was diligence findings outside formal earnings analysis, at 25.3%. Second was earnings quality discrepancies, at 21.3%, meaning reported earnings diverged materially from what buyers found on examination.

FIGURE 2 / EARNINGS QUALITY AS A SHARE OF FAILED DEALS



Axial Dead Deal Report. Share of transactions that failed after a signed letter of intent where earnings quality was the cited cause.

The trend matters more than the ranking itself. Earnings quality accounted for 10.6% of failed deals in 2023, 15.4% in 2024, and 21.3% in 2025. The broader diligence category rose over the same period. Buyers are examining earnings more closely every year and finding more that changes their view.

PART III

What You Can Change

Who the buyer is changes the number

The same company shown to different buyers produces different outcomes, for structural reasons rather than negotiating ones.

An **individual buyer** purchasing a business to run personally is constrained by financing. They are usually using an SBA loan, and their ceiling is what the cash flow can service. They may pay a fair multiple, rarely a premium one, and their diligence focuses on whether the business can carry its own debt.

A **financial buyer**, meaning a private equity firm or similar, is underwriting a return over a defined holding period. They are disciplined, thorough in diligence, and able to move quickly. Their price comes from a model, and the model has limits they will not cross no matter how much they like the business.

A **strategic buyer**, an operating company in your industry or an adjacent one, is the only category that can justify paying more than the business is worth standalone, because they may capture cost savings or revenue a financial buyer cannot. Premium outcomes usually originate here. Strategics are also slower, more bureaucratic, and more likely to walk for reasons that have nothing to do with your company.

Which one is right depends on what you want. Maximum price, speed to close, continuity for your employees, and a clean personal exit are not the same objective and do not point to the same buyer.

The headline price is not your proceeds

Structure determines what you actually receive, and it varies with size.

The IBBA and M&A Source Market Pulse tracks this quarterly. In the second quarter of 2026, sellers received between 83 and 92 percent of deal value as cash at closing on average, with seller financing under 10 percent of most transactions. That is a favorable environment by historical standards.

The averages hide the pattern that matters. Cash at close runs highest at the smallest end, where SBA financing supplies the buyer's capital, and again at the larger end, where institutional buyers write big equity checks. The middle is where seller notes, earnouts, and rollover equity show up most, because that is where the gap between what a buyer will fund and what a seller expects is widest.

Timelines have stretched. In the second quarter of 2026, Main Street deals averaged six to ten months from engagement to closing, while lower middle market deals averaged eleven to twelve. The $2 million to $5 million segment jumped the most, from nine months to eleven and a half.

Two things follow. Your proceeds depend on structure at least as much as on the headline multiple, so you cannot judge an offer by its multiple alone. And the process runs long enough that the business has to keep performing throughout, since slipping results during diligence are themselves a documented deal killer.

Which twelve months count

The default is trailing twelve months (TTM). GF Data and most comparable sources report against TTM adjusted EBITDA, and buyers start there for the same reason they use a multiple at all: it is the only period that already happened.

The period is negotiable, though, and three situations move it.

Revenue that is already committed. When next year sits in signed contracts, subscriptions, or a maintenance book with documented renewals, a forward figure is not a forecast as much as it is arithmetic on commitments already in hand, and buyers will underwrite it because the uncertainty they are pricing has been resolved.

A deal negotiated late in the year. Trading in November against a period that ended in September means the reference number is stale. A buyer may accept a projected full year or an annualized run-rate instead. This cuts both ways. A strong fourth quarter argues for the projection. A weak one means the buyer waits for the year to close and reprices against it, which costs you months.

A step change readily present in the results. A new contract, a second location, an acquisition completed mid-year. Once the change has been in the numbers for six months, annualizing it is a smaller leap than forecasting it, and buyers will often meet you there.

Getting a forward basis accepted is not the same as getting paid at closing, but it is also not a discount. Total consideration is the numerator: cash, earnout, and any equity you roll. A multiple applied to forward earnings with part of the value contingent is still that multiple on those earnings. What a buyer declines to do is pre-pay for performance that has not happened yet.

That distinction matters more than it sounds. Without a contingent mechanism, most buyers would not credit the forward number at all. They would underwrite the trailing period and your growth would go unpaid. The earnout is how a forward year gets valued, not the price of asking for one.

What does change is control. At closing you stop running the business, and the buyer takes over the decisions that determine whether the target gets hit: accounting treatment, integration choices, whether the investments your forecast assumed get made at all. The earnout's measurement terms end up mattering as much as the multiple you negotiated.

One further complication is worth knowing. Published data does not treat contingent consideration consistently. Some sources count the maximum potential earnout in the numerator, some probability-weight it, some capture only what was paid at closing. If your deal is earnout-heavy and you are measuring it against published multiples, you may be comparing numerators that were built different ways. That is the same problem as comparing like with like, now with your own transaction on one side of it.

Two things follow. A budget is not evidence and a signed contract is, so documentation decides which period you can credibly argue for. And the period definition and the earnout measurement terms belong in the letter of intent, where you still have leverage, not in diligence, where you have less.

The preparation window

Almost everything that sets your multiple is a property of the business, not of the negotiation. By the time you have a letter of intent, the number is mostly fixed. The window where you can still move it runs twelve to twenty-four months before you go to market.

Most sellers reach the market without having used it. The Pepperdine Private Capital Markets Report, an annual survey of more than five hundred participants across private capital markets, found that 64 percent of sellers did no formal exit planning before going to market, and only 26 percent met with any advisor beforehand. Pepperdine also found that about a third of investment banking engagements never close, with the most cited cause being a valuation gap between buyer and seller. Where deals died on price, the gap was most often only 11 to 20 percent.

That last number deserves your attention: the difference between a closed deal and a wasted year is often smaller than what ordinary readiness work can move.

What moves the number, roughly in order of impact:

Make yourself replaceable. If the business cannot run for a month without you, every buyer prices that in and some walk away entirely. Building real management depth takes years, which is exactly why it belongs at the start of the window rather than the end.

Fix concentration. A customer at forty percent of revenue is a risk the buyer inherits, and they will price it. You cannot fix this in ninety days. You can often improve it substantially in eighteen months.

Make your earnings verifiable. This is the difference between financials that support a conclusion and financials that need your narration. Every add-back you plan to claim needs documentation a stranger can follow without you in the room. Given what the Axial data shows about earnings quality disputes, ambiguity is getting more expensive every year.

Write down what lives in people's heads. Procedures, pricing logic, vendor terms, and customer history that exist only as habit are risks to a buyer. Written down, they become assets that transfer.

Time it on purpose. Buyers look at trailing twelve month performance. Going to market on a declining trend invites a discount that has nothing to do with the long-term health of your business.

Closing

The multiple you get is mostly an expression of how confident a buyer is in your earnings. Size, sector, and the state of the capital markets set a range. Where you land inside that range comes down to how much of your performance a stranger can verify and how much of it depends on you.

One last observation, offered as judgment from practice rather than a finding from data. Owners in hot sectors often read the attention as validation, and treat unsolicited offers as a sign the sale will be easy. The opposite is closer to true. Heavy interest brings more buyers and more sophisticated diligence, and it pulls every asset in the sector to market, including the ones least ready to be examined. Being in a market buyers want helps you set the opening price. It protects you not at all once the examination begins.

Appendix: Sources and How to Read Them

These figures come from populations that are not interchangeable. If you are researching your own company's value, know what each source measures.

> GF Data (Association for Corporate Growth). Private equity sponsored transactions with enterprise values between $10 million and $500 million, reported by more than three hundred sponsor firms. Stated as total enterprise value over trailing twelve month adjusted EBITDA. The most directly relevant source for lower middle market companies. Headline data is free; the searchable database requires a subscription.
>
> IBBA and M&A Source Market Pulse. Quarterly survey of business brokers and M&A advisors covering Main Street businesses from $0 to $2 million and lower middle market businesses from $2 million to $50 million. Roughly 300 to 350 respondents per quarter. Reports multiples, deal structure, and timelines by size band. This is advisor-reported survey data, not audited transaction records.
>
> BizBuySell Insight Report. Broker-reported small business transactions, median sale price around $350,000. Multiples are reported against SDE and against revenue. Relevant to Main Street businesses and misleading if applied to anything larger.
>
> Pepperdine Private Capital Markets Report (Graziadio Business School). Annual survey across lenders, private equity, investment bankers, brokers, appraisers, and business owners. Strongest on cost of capital, process outcomes, and seller preparation. Free, and available earlier to survey participants.
>
> Axial Dead Deal Report. Annual analysis of lower middle market transactions that failed after a signed letter of intent. The 2025 edition covers 75 transactions. A small sample from one platform's deal flow, and the only public dataset that categorizes why deals die.
>
> NYU Stern industry data (Professor Aswath Damodaran). Updated each January. Enterprise value multiples by industry for publicly traded companies. Frequently cited in articles about private company valuation, where it does not belong. Public company multiples reflect large, liquid, professionally managed businesses and substantially overstate what a private company will receive.
>
> *One caution on all transaction data: reported multiples come from completed deals. Businesses that went to market and failed to sell appear in none of these datasets, and that population is large. Published multiples describe the sellers who succeeded.*