Value for SME transfer: user value instead market value

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Abstract

The concept of value is in the centre of valuation process. He is developing with the concept of market. A conception of market value which is practiced on a large scale, as a value in exchange is based on the assumption of stability of the market of a valuation subject (a SME) and does not correspond well with condition of non-stable market. The paper seeks to present another kind of value which is more suitable for modern market of SME transfers referred both to the sale and to the acquisition of small or medium-sized enterprises.

Although rather many statements of imperfection of value concept in modern condition of mortgage crisis are exist, all propositions lay in the frame of traditional definition of market value as a value in exchange. This paper is the attempt to propose a new kind of value, user value, in the frame of value in use.

Traditional valuation methodology has combined in USA after the 1930s in the midst of the Great Depression crisis. Later it has became world recognized. That methodology has reflected in valuation standards, elaborated by RICS and Appraisal Foundation. On that base the system of the

International Valuation Standards, IVS, has been generated and gradually began to find the increasing recognition both among appraisers of the various countries and representatives of adjacent trades, first of all bookkeepers. On that base many countries complete national valuation standards. The main purpose of all these standards was to fix uniform traditional approaches to appraisal, developed for centuries of activity in condition of the stable economy, characteristic for the leading countries of the world during the preceded period.

All the same time it became gradually clear, that valuation activity in condition of emerging markets has new, additional essential features which were not noticed in traditional valuation manuals. So-called "White document" let out in 2001, the comment to IVS, devoted to a valuation in the emerging markets, draws attention to necessity of use of the standard of market value and describes difficulties of valuation activity in these conditions, not giving recommendations on their overcoming.

But, as it was found out in the further, some elements of economy of emerging markets are shown in quite stable and economically developed countries in the separate markets during separate time. At last, rather recent scandals with Parmalat company in Europe, Enron company in the USA, and, finally, present financial crisis have shown, among other, that absence of the account of features of a valuation in these situations attracts sometimes to a catastrophic consequence. It is time to think on the basic concepts. One of them is a concept of a value.

Methodology of valuation most widespread now is based on the assumption of stability of the market of a valuation subject (a SME). This assumption has consequence the concept of the market value, in particular, in the definition of International Valuation Standards. A decade ago most valuations are performed on the base of market value.

This is a conception of a value in exchange, where a willing seller and a willing buyer decide to change a valuation subject for a calculated sum of money on the valuation date on the base of well-done marketing. Market value is the most probable selling price between a willing buyer and a willing seller under normal (*i.e.* stable) market conditions and assumes a sale to the most probable purchaser. For reach a market value "buyer and seller each acting prudently, knowledgeably, and for self-interest", "both parties are well informed or well advised, and acting in what they consider their best interests."

It is evident, that market value definition means an information transparency of the market of a valuation subject, enabling its appropriate research for achievement of good awareness on consequences of the imagined transaction of an exchange. Moreover, market value is often identified with equilibrium price, arising on crossing of curves of a supply and demand which calculation requires, generally speaking, presence in the market of the so-called perfect competition. Differently, it is reasonable to draw a conclusion, that calculation of market value is possible only for the equilibrium (steady) transparent competitive market.

An importance of broadening concept of market value has noted from the very beginning of market value definition existence. Nevertheless some time ago it seems that the approximation of a market value looks strange only for emerging markets with its non-transparency and, as consequence, impossibility of performance conditions resulted in definition of market value.

Last half-decade changes the situation. Thinking on the reasons of poor-quality valuation since times of scandals with Enron company etc. up to modern mortgage crisis many analytics have come to conclusion, that, apparently, the stable markets exist only in imagination, as a model. In the contemporary world prices are not established by what has gone before or even what exists now, but by buyers' and sellers' future needs and expectations.

Whether for this reason, or on the basis of intuition, more and more valuers' clients (owners, buyers, investors) are interested not in a present condition of the market, but its future. Making a decision of SME transfer they wish to know the future incomes of use of a SME (valuation subject). Differently, a willing seller and a willing buyer have typically ignored market value, but are interested in value in use.

The concept of the value in use (or use value in US) is well-known. The value in use is a value of concrete property at concrete use for the concrete user and consequently not connected with the market. In book keeping a value in use is the value of calculated future cash flows discounted to a present situation which presumably will arise from continuation of use of an active and from its sale in the end of its term of useful services.

Nevertheless often a potential investor is not interested in value in current use, but value in the most profitable use (highest and best use). We shall name this kind of value as the "user value". It can be defined as follows. User value is a current value of the future incomes of valuation subject in highest and best use.

Being based on this definition, it is simple to fix an algorithm of calculation of the user value. At the first stage it is necessary to define the highest and best use of a valuation subject. Further, it is necessary to forecast the incomes from this use, including return of the capital by sale in the end of use. At last, to predict changes of capitalization rate in the market of valuation subject and to discount future incomes to the valuation date.

As it shows, in conditions of changing markets the using by the appraiser of the user value as the basis of a valuation often meets greater understanding of clients, than calculation of the market value.