

‘I want this to be in good hands’: Sales price expectations of resigning entrepreneurs

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ABSTRACT

Resigning entrepreneurs may choose from a variety of exit routes, many of which include sales to another person, a group of individuals, or another firm. For those entrepreneurial exits, the agreement on a sales price is a core element in the business transfer process. The leaving entrepreneur's emotional pricing thereby affects his or her sales price expectations and subsequently the likelihood of a (successful) transfer, determines the satisfaction level with the succession of all parties involved, and has implications for financing of the deal. Based on loss aversion, we hypothesize how the economic situation of the firm, the type of exit route, and entrepreneurial tenure independently and interactively affect entrepreneurs' emotional pricing. In a first step, we test the hypotheses based on a sample of 1'354 owner-managers of Swiss SMEs who reflect on their exit intentions. In a second step, we mirror those results with findings of 455 recent ownership transfers of Swiss SMEs.

Keywords: entrepreneurial exit, emotional pricing, loss aversion, exit route

1. INTRODUCTION

Exiting the business is a major event for almost any entrepreneur with important implications for the firm owner, the firm, and all its stakeholders (DeTienne, 2010, Wennberg et al., 2011). The exit process itself comprehends a large number of considerations, choices, negotiations, and ultimately actions by the incumbent firm owner, for instance, selection of the preferred exit route. Many entrepreneurs ultimately decide to sell the business, for instance to family members, employees, external individuals, or other firms (Dehlen et al., 2012, Howorth, Wright and Westhead, 2007).

For any selling of an entrepreneurial firm, the sales price and related expectations are crucial (Granata and Chirico, 2010), as they determine important “exit outcomes” (Van Teeffelen and Uhlaner, 2013: 2)—not only the speed of the transaction process and the satisfaction of all parties involved, but also whether the transfer of the business takes place at all (Geerts, Herrings and Peek, 2004, Howorth, Westhead and Wright, 2004): If the entrepreneur's expectations regarding the sales price are too high, potential successors might be alienated and ultimately withdraw from the transfer negotiations. As a consequence, the

pool of potential successors diminishes with increasing price expectations, and, in the extreme case, no adequate succession candidate will remain to take over the business (Dehlen et al., 2012). Low sales price expectations of the entrepreneur, on the other hand, might entail low actual transaction prices and, as a consequence, endanger the entrepreneur's retirement provisions.

Applying a rational point of view, one would expect the entrepreneur's sales price expectations to equal the respective firm's real value, yet this view neglects an important emotional, apparently "irrational" aspect of pricing. A large body of theoretical and empirical research indicates that exiting entrepreneurs are often not only concerned about the amount of their harvested value but also the quality of exit and the future prospects of "their baby" (Cardon et al., 2005, DeTienne, 2010, Sharma and Irving, 2005). In a qualitative, case-based study, Eisenhardt and Graebner (2004) provided evidence that entrepreneurial US-based high tech firms were not sold to the bidder with the highest offer but rather to prospective buyers who "fit" best with the company's values and culture. Exiting owners appear to care for the firm's future prosperity, even after the ownership transfer has occurred. Scholars attribute this desire to the entrepreneur's emotional attachment to the firm (DeTienne, 2010) and argue that this attachment, in turn, affects the emotional value that owners associate with the business (Astrachan and Jaskiewicz, 2008, Zellweger and Astrachan, 2008). Empirical work carried out in the family business context indeed shows the importance of emotional aspects in exit contexts (DeTienne and Chirico, in press) and reveals that long times of exposure to the business affect the owner's minimum acceptable sales price when considering transferring the business to family-external individuals (Zellweger et al., 2012).

Despite the relevance of this emotional pricing component in the context of entrepreneurial exits, we still lack a profound understanding of this phenomenon. To date, it remains largely unclear how extensive this emotional pricing component is and how it is determined. With our study, we thus aim to answer the following research questions: *How do*

(1) prior firm performance, (2) familiarity to the successor (as reflected in different exit paths), and (3) entrepreneurial tenure independently and in interaction affect entrepreneurs' emotional pricing components (measured as deviation of expected sales price from real firm value, as assessed by the owner-manager)? We build our hypotheses on arguments of loss aversion and test them based on survey answers of 1'354 Swiss entrepreneurs who have already given thought to their own future exit from their business. To link those intentions to data on actual entrepreneurial exits and respective transaction prices, we also probe several of the hypotheses based on a sample of 455 transfers of SMEs that occurred within the last decade in Switzerland.

Our research advances literature on entrepreneurial exits in multifold ways. This study draws the focus of entrepreneurial exit research to emotional pricing, an important yet so far underinvestigated element of many exit processes. Our empirical findings indicate that loss aversion plays a crucial role for any sales price considerations. The empirical results of this study support the notion that entrepreneurs indeed care about the post-exit well-being of their firm and adapt expected sales prices in order to avoid losses—be it the loss of the firm, the firm's values or information about the firm. Thus, we do not only provide empirical evidence on typical extents of emotional pricing for sales price considerations, but we also identify several drivers that entail heterogeneity in resigning owners' sales price expectations. Moreover, by providing empirical evidence on specific heights of discounts offered in family-internal and family-external transfers, we also contribute to family business research.

2. THEORETICAL FOUNDATIONS

2.1 Entrepreneurial Exits

All entrepreneurs once have to exit their business, but they differ with regard to why they resign—for instance, due to age and health reasons or because of financial motives—(DeTienne, 2010) and how they resign (Wennberg et al., 2010). When exiting their business, incumbent owners can either discontinue the business (liquidation), issue shares to the public

(IPO), or sell the business to family members (family buy-out, FBO), to employees (management buy-out, MBO), to external individuals (management buy-in, MBI), or to other firms. As the goal of this study is to investigate the emotional aspects of owners' considerations when selling the firm to another party, we will henceforth focus on the last four exit paths. This approach is also in line with empirical findings that show that those exit choices are by far the most dominant ones for small and medium sized enterprises (DeTienne and Chirico, in press, Howorth et al., 2004). Although entrepreneurial exits constitute a dyadic setting that involves the buyer's as well as the seller's perspective, our focus lies on the selling party, which so far remains underinvestigated in current entrepreneurship research (Graebner and Eisenhardt, 2004, Wennberg et al., 2010).

2.2 Sales Prices and the Entrepreneurial Exit Process

Agreement on the respective sales price is at the core of each entrepreneurial exit process since it can be decisive for the success of the intended exit (Scholes et al., 2007) and it affects the level of satisfaction with the succession process (Niedermeyer, Jaskiewicz and Klein, 2010). However, determining an adequate sales price for private firms in general, and small and medium-sized firms in particular, is complex (Baik, Kang and Morton, 2007). No commonly agreed approach to calculate the value of an unlisted firm exists, and researchers and practitioners can choose from a variety of methods—such as multiples, income-based approaches, and asset-based approaches (Feldman, 2005, Pratt, Reilly and Schweihs, 2000)—with diverging outcomes in order to calculate the respective firm's assumed real value.¹

In the remainder of this paper, we will assume that the resigning owners have at minimum basic knowledge about the real value of their firm, regardless of what this figure is in absolute terms (and regardless of how well the real value perceived by the owner fits the real value of the firm as assessed by experts). This assumption is reasonable since we focus

¹ Each of those approaches to determine the firm's real value brings along several advantages and disadvantages. In the remainder of this paper, we will use the term real value without specification of a certain calculation method applied.

on resigning owners that have already thoroughly engaged in considering their exit and as there are methods such as the multiples approach (Granata and Chirico, 2010) that allow owners to assess their SME's rough value without requiring substantial effort or knowledge.

However, we continue to argue that the real value of the firm (respectively, what the owner believes that is the real value) is unlikely to equal his or her intended sales price—i.e. his or her sales price expectations—because of an emotional pricing component, which needs to be taken into account. Empirical evidence reveals that privately held firms are often traded with a discount in the two-digit percentage area as compared to similar publicly listed companies (Cooney, Moeller and Stegemoller, 2009, Officer, 2007). While part of this discount might be attributable to malevolent valuations of buyers (Granata and Chirico, 2010), another part of this discrepancy between the sales price and the firm's real value can be attributed to the selling incumbent, who, due to his or her emotional attachment to the firm, aims to achieve sales prices that are either above (“emotional cost”) or below (“emotional benefits”) the actual value of the firm (Astrachan and Jaskiewicz, 2008, Zellweger and Astrachan, 2008, Zellweger et al., 2012). Research thus indicates that diverging price expectations might exist that stem from the owner's emotional attachment to the firm and the desire to pass on the firm to a successor who ensures a prosperous future for the firm (DeTienne and Chandler, 2010, Graebner and Eisenhardt, 2004).

2.2.1 Fear of Ultimate Firm Failure—Performance Level and Emotional Pricing

Individuals that sell items, such as traders (Odean, 1998) or condominium owners (Genesove and Mayer, 2001), often have emotional pricing considerations, which result in deviation of sales price expectations from the objects' real values. Behavioral theory, in particular prospect theory and its focus on loss aversion (Kahneman and Tversky, 1979) has previously been proven successful to explain such discrepancies among expected rational and observed irrational behavior by assuming a bounded rationality of decision makers such as sellers. In line with those arguments, previous work indicated that gain or loss framing is influential in

entrepreneurial exit decisions (Gimeno et al., 1997). For instance, Wennberg and colleagues (2010) created and tested a framework that uses arguments of prospect theory to predict how different contextual situations render harvest sale, harvest liquidation, distress sale, or distress liquidation more probable.

Building on and extending those studies, we expect that loss aversion affects emotional pricing considerations of resigning entrepreneurs. In particular, we propose that inferior financial performance of the firm relative to competitors increases an owner-manager's fear of ultimate firm failure and thus enhances his or her willingness to sell the firm at a substantial discount compared to the firm's real value. Several authors have previously pointed to the important role of the firm's economic performance and in particular performance relative to the entrepreneur's aspiration level for various aspects of the entrepreneurial exit process (e.g., DeTienne and Chirico, *in press*, Wennberg et al., 2010).

When the performance of the firm is low as compared to peers, the owner-manager is assumed to be in a "distress" situation (Wennberg et al., 2010) and in a mode of loss framing. In such a situation, avoidance of liquidation might emerge as a salient goal of the owner, because—depending on personality and culture—discontinuation of the business might be perceived as ultimate failure and loss by the resigning entrepreneur (Bane and Neubauer, 1981, Ucbasaran et al., 2010). We argue that, trying to avoid this type of loss, other goals such as achieving sales prices close to or even above the firm's real value are likely to fade from the spotlight. This is in line with previous research that highlights that decision makers in organizations are "sequentially attentive" and follow goals one after another (Greve, 2008). Consequently we argue that the owner, who is reluctant to realizing the perceived loss, is willing to accept any successor and any sales price as long as the business is likely to be continued.

When firm performance is above the owner's aspiration point, however, the resigning entrepreneur is likely to be in a mode of gain rather than in a mode of loss. In such a

situation, continuance of the firm is not at stake according to the owner's own perception and hence the urgency to find a successor is decreased. Considerations about potential financial gains are thus more likely to play a crucial role in the entrepreneurial exit process and the incumbent owner might feel encouraged to find a successor who is willing to pay a sales price, which is close to or even above the firm's value. Ceteris paribus, we thus expect that framing as loss or gain affects entrepreneurs' sales price expectations. In sum, we propose:

H1: The worse the financial performance of the firm, the larger the emotional pricing component, in particular the lower the entrepreneur's sales price expectations relative to the firm's real value (i.e. larger emotional discounts under bad performance).

Loss aversion is not bound to the fear of ultimate firm failure as discussed in this section. Yet loss aversion can also relate to other aspects of perceived loss, such as loss of control of or information about the firm. Thus we assume that two other aspects—familiarity between buyer and seller as well as emotional attachment to the firm—also affect the resigning owner's level of potential losses and thus his or her emotional pricing.

2.2.2 Loss of Firm, Control, and Information—Exit Route and Emotional Pricing

Besides the relative performance level of the business, firm owners' emotional pricing might also depend on the familiarity to the firm's buyer (Teeffelen, Uhlaner and Driessen, 2011) and thus on the targeted type of exit path. Sales of an entrepreneurial firm can include transfer to family members, firm employees, family- and firm-external individuals, or other firms (Dehlen et al., 2012) and all those exit types are distinct modes of business transfer with idiosyncratic characteristics (Parker, Storey and Van Witteloostuijn, 2010) and different levels of "closeness" or familiarity between buyer and seller.

Business exits might not only be associated with a fear of cessation of the firm as ultimate failure but also with a potential loss of control and influence over the firm by the resigning entrepreneur. Empirical evidence reveals that owners' perceived sense of responsibility for their firm does not terminate at the time of transfer; yet the entrepreneurs do

indeed care about their firm's potential future and hence pay attention to whom they transfer their business to (e.g., Dehlen et al., 2012, Graebner and Eisenhardt, 2004). This notion is supported by a large body of empirical evidence carried out in various contexts, which highlights that retired CEOs continue to influence their former companies after resignation in order to shape the firm's future (Ahrens, Woywode and Zybura, 2012, Quigley and Hambrick, 2012, Sharma, Chrisman and Chua, 2003). Moreover, firm owners with transgenerational intentions (Chua, Chrisman and Sharma, 1999) are known to strive for family-internal succession, that is transfer to most familiar individuals, in order to avoid the loss of legacy, tradition, and socio-emotional wealth (Gómez-Mejía et al., 2007, Zellweger et al., 2012).

We argue that the incumbent owners' emotional pricing varies, depending on the type of potential successor, since the familiarity between seller and buyer affects the incumbent owner's anticipated losses associated with the business transfer. First, the resigning entrepreneur's level of trust in the successor's capabilities to shape the firm's future in a positive way varies (Howorth et al., 2004, Morris and Williams, 1997, Teeffelen et al., 2011). The level of trust in a person depends on the history of exposure to that person and typically grows over time (Johnson-George and Swap, 1982). As a consequence, human beings, *ceteris paribus*, have greater trust in individuals that are closer and more familiar to them, such as family members, as opposed to strangers (Luo and Chung, 2005). If entrepreneurs know and trust the person, whom they plan to transfer the business to, they will be more confident that this individual will continue the business operations in a desired and successful way and thus avoid ultimate firm failure.

Second, the closer the incumbent's ties to the successor, the higher is the likelihood that the former owner remains "informed" about the business activities and might even possess the opportunity to influence the business development post-exit, for instance through advising activities (Osborne, 1991). Increased familiarity with the successor thus decreases the incumbent owner's anticipated level of loss of control and influence.

Summarized, transferring the business to a familiar individual allows incumbent owners to minimize their perceived losses associated with firm transfer. Analogous to the chain of arguments provided in section 2.2.1, we expect that the resigning entrepreneur is willing to offer a rebate for this mitigation of losses, which is assumed to be reflected in a discount of sales price for the respective successor. In other words, the entrepreneur is willing to accept lower sales prices in case he or she can be confident that the firm is continued in a desirable way and that there are ongoing possibilities for him or her to remain informed about the company and influence it even post-exit. Thus, we formally propose:

H2: The more familiar the successor is to the incumbent, the larger the emotional pricing component, in particular the lower the entrepreneur's sales price expectations relative to the firm's real value.

2.2.3 Loss of Firm, Control, & Information—Entrepreneurial Tenure & Emotional Pricing

We further argue that the anticipated loss associated with firm exit is not only driven by factors relating to the firm (2.2.1) and the dyadic relationship between buyer and seller (2.2.2) but is also shaped by characteristics of the entrepreneur, in particular his or her emotional attachment to the business.

The ties of the entrepreneur to the firm change over time (DeTienne, 2010). With increasing entrepreneurial tenure within the firm, the owner-manager's emotional attachment to the business increases (Dehlen et al., 2012, Zellweger et al., 2012) and the more he or she cares about what will happen to the business after his or her exit (Cardon et al., 2005). As noted earlier, in chapter 2.2.2, emotional value and attachment is assumed to render the incumbent owner reluctant to realize losses in terms of potential firm failure, absence of continuing information, or lack of possibilities to influence the business development.

Thus, as over time emotional attachment to the firm increases, the entrepreneur might change his or her exit preferences and related business transfer criteria (Dehlen et al., 2012). More specifically, non-financial considerations, and thus the emotional pricing component, are expected to become more dominant in the exit process, when entrepreneurs have owned

the firm for an extended period of time. In other words, owners who have possessed their firm for a long time perceive it as more important to avoid any losses—in terms of failure, lack of influence or control—instead of maximizing financial gains when transferring the business to a successor. Thus, we expect the long-tenured, resigning firm owner to search for the best suitable successor and to be a priori willing to give a substantial discount to this individual. Formally, we propose:

H3a: The longer the owner's entrepreneurial tenure within the firm is, the larger the emotional pricing component, in particular the lower the entrepreneur's sales price expectations relative to the firm's real value.

Besides this hypothesized direct influence, we expect a moderating effect of entrepreneurial tenure on emotional pricing. As argued above, entrepreneurial tenure enhances the owner's emotional attachment to the firm (Dehlen et al., 2012). Strong emotional attachment, in turn, is likely to increase the threat of loss, which the entrepreneur perceives when the performance of the firm falls below his or her aspiration level or when the business is transferred to an unfamiliar person. As a consequence, entrepreneurs are likely to feel even more encouraged to avoid such anticipated losses at any price and sell the business below its real value, when his or her tenure within the firm is high. Formally,

H3b. Entrepreneurial tenure within the firm strengthens the hypothesized relationship between firm performance and emotional pricing.

H3c. Entrepreneurial tenure within the firm strengthens the hypothesized relationship between familiarity of the successor and emotional pricing.

3. METHODS

3.1 Sample

To test our hypotheses we collected survey responses from CEOs of SMEs based in Switzerland, defined as firms with less than 250 employees. For this purpose, we obtained addresses of 36'699 CEOs of privately held Swiss SMEs from the D&B database. Thereby we a priori excluded businesses active in agriculture, forestry, petroleum refinement,

electricity and gas supply, water treatment, financial services, insurance, and public administration (NOGA codes 01, 02, 19, 35, 36, 64, 65, 66, 84) due to idiosyncratic characteristics of those sectors.

In January 2013, we mailed a physical cover letter and an eight-page questionnaire to the 36'699 identified CEOs. Depending on the postal code, the language of the letter and the questionnaire was German, French, or Italian. During a seven-week data collection phase, we retrieved 2'362 completed surveys, resulting in a response rate of more than² 6.4%, which is slightly lower than that of other studies targeting entrepreneurs or top managers (Cruz, Gómez-Mejía and Becerra, 2010, Dehlen et al., 2012, Schulze et al., 2001). The relatively low response rate was likely to be caused by the length of the questionnaire (30 min) that was attributable to the comprehensive nature of the questionnaire, which was embedded in a large project studying Swiss SMEs. In order to check for non-response bias, we compared the responses of early and late responders, thereby assuming that the latter ones resemble non-responders (Oppenheim, 1966). Our results revealed no significant differences regarding any of the variables included in the model.

We excluded any surveys that fulfilled at least one of the following criteria: (a) respondent was not the owner-manager of the respective company (6 cases), (b) companies with more than 500 employees (18 cases), (c) missing information on sales price expectation, for instance because the CEO had not contemplated his exit yet³ (919 cases), and/or (d) CEO indicated IPO (11 cases) or liquidation (54 cases) instead of sales as his or her intended exit strategy. Our final sample contained 1'354 survey responses ("prospective sample").

For a post-hoc test of our hypotheses based on actual transactions, we rely on a subsample of 523 respondents who additionally provided information on their own takeover

² Numbers of letters, which could not be delivered, for instance because of wrong addresses, are not included in the calculation.

³ We included a filter question in order to assess whether the CEO has already contemplated his or her exit strategy.

in the role as successor within the last 10 years (“retrospective sample”). After removing cases with missing data regarding the dependent variable (actual sales price in percentage of real value), our final sample size was 455.

In line with other studies on privately held firms, our study is based on a key informant approach (Kellermanns et al., 2008, Kumar, Stern and Anderson, 1993, Seidler, 1974) as we assume that the CEO is most informed about the information to be gathered in the questionnaire. To assess the degree to which our sample is representative of the total population of Swiss SMEs, we compared the descriptive characteristics of CEOs and firms in our sample with the characteristics of the samples used in comparable studies. The average age of the firms in our sample (44 years) is lower than the average age of the firms in a sample with Swiss family businesses studied by Zellweger and colleagues (2012) (67 years) and older than the average age of the firms in a sample of startups included in the 2007 Global Entrepreneurship Monitor’s (GEM) report on Swiss firms (17 years) (Volery et al., 2007). This is reasonable as our focus is on established family- as well as non-family firms. The average age of the owner-managers in our sample (57 years) is higher than the average ages of the owner-managers of the Swiss firms (46 years) in the GEM reports and of the firms studied by Zellweger and colleagues (2012) (51 years). This can also be explained as our sample is based on answers of entrepreneurs who have already thought about their entrepreneurial exit, considerations that often occur towards the end of one’s professional career. Our descriptive data (Table 1) reveals that the average tenure of CEOs in our sample is 22 years. Our sample consists of 84% family firms. The average size of companies in our sample is 36 employees.

Next, we assessed the likelihood of common method bias, which can stem either from drawing on the same source to obtain the independent and the dependent variables or from specific item characteristics that enhance respondents’ tendency to answer the survey questions in a distorted, for instance socially desirable, way. When collecting our data, we

took several ex ante procedural steps in order to mitigate the risk of this type of error. First, we designed the questions in the simplest possible way. Second, the questionnaire that we used was embedded in a comprehensive survey on the economic relevance of entrepreneurial exits within Switzerland. Taken together, the design of the survey and the particular order of the questions within the questionnaire did not reveal any indication of the expected correlations to the respondents. Therefore, it is unlikely that the respondents “edit[ed] their responses to be more [...] consistent with how they [thought] the researcher want[ed] them to respond” (Podsakoff et al., 2003; p. 888). Third, we assured the respondents of the strict confidentiality of their responses, an ex-ante measure that is known to reduce the probability of social desirability bias in respondents’ answers (Podsakoff et al., 2003a). In order to verify ex-post that our procedural efforts to reduce common method variance were effective, we followed the suggestions of Podsakoff and Organ (1986) and performed a single-factor test. An exploratory factor analysis of all of the variables used in this study revealed six factors with Eigenvalues greater than one, jointly accounting for 63% of the total variance, with the first factor accounting for less than 17% of the total variance. In sum, those results of the post-hoc analysis, together with various ex-ante precautions indicate that common method variance is unlikely to distort the results of our study (Podsakoff et al., 2003).

3.2. Variables

3.2.1 Dependent Variable—Emotional Pricing

To assess the emotional pricing component, we asked the respondents to indicate for how much money—as compared to real value—they aim to sell their firm. The respondents of our survey could choose one of eight categories: 0% (1), 1-20% (2), 21-40% (3), 41-60% (4), 61-80% (5), 81-99% (6), 100% (7), more than 100% (8). We chose to ask for relative data on sales price expectations as opposed to asking for absolute numbers, an approach chosen for instance by Zellweger and colleagues (2012), because relative data is considered less sensitive. As a consequence, respondents of the survey are more likely to provide

comprehensive and correct relative data on this specific topic. Moreover, relying on absolute instead of relative numbers would not increase the richness and/or correctness of our collected data, in particular as, due to a lack of information on financial data of Swiss SMEs, there is no possibility to calculate firm values for our sampled data externally.

3.2.2 Independent Variables

Financial performance. As our theory builds on loss aversion and the CEO's perception of how well the firm performs, we used a subjective measurement of firm performance. We asked respondents to indicate their assessment of the financial performance of their own firm as compared to competitors over the last three years. We used a 4-item, 7-point Likert-scale ranging from "much worse" to "much better." Respondents were asked to assess the performance in terms of profit, revenue growth, growth of market shares, and growth of profitability. To analyze the data, we used the mean of the four items as indicator for financial performance.

Exit path. To operationalize the familiarity of the future successor to the entrepreneur, we asked for the type of planned exit route. We thereby assume that family members are closest and family- and firm-external individuals (MBI, sales to firm) are least close. More specifically, we asked the respondents to whom they plan to transfer the ownership of their firm at the time of their exit. Respondents could choose among the following answers, which were later dummy coded: Sales to family member(s) (FBO), sales to employees (MBO), sales to external person(s) (MBI), sales to other business (sales to firm), others (liquidation, IPO—those were excluded from the analysis, as described in 3.1). We dummy coded those variables with "still unknown/unsure" as reference category.

Entrepreneurial tenure. To assess the tenure of the CEO, we asked the respondent to indicate in what year he or she joined the respective firm (year of entrance). The variable "tenure" is calculated by subtracting the year of entrance from the year when this study was

conducted (2013). It is important to note that this variable accounts for the entire professional tenure of the CEO within the firm and is not restricted to his or her time as CEO.

3.2.3 Moderator Variables

To calculate the moderator variables, we first centered the variables by subtracting their respective means (Aiken and West, 1991, Li and Tang, 2010) and subsequently calculated the interaction of tenure and financial performance as well as with the four exit route dummies.

3.2.4 Control Variables

We included six control variables into our analysis that possibly affect the entrepreneur's emotional pricing. First, we included a dummy variable that indicates whether the business is a family business (=1, otherwise 0). In family firms, emotional attachment to the business is particularly high (Zellweger et al., 2012), which in turn might impact the entrepreneur's sale price expectations. Second, we control for industry-induced effects applying a dummy variable (=1 for tertiary and 0 for secondary sector). Third, we included firm size into our model, measured as the number of full time employees. When financial performance is below aspiration level, entrepreneurs of larger firms might be even more anxious about finding any buyer due to the financing issues inherent in the transfer of larger businesses to one or more individuals (Dehlen et al., 2012). Fourth, we control for the year of the company's foundation as this might further affect the entrepreneur's emotional attachment to the firm (Dehlen et al., 2012). Fifth, we control whether the firm is part of the entrepreneur's personal pension plan. Entrepreneurs who view the firm as important component of their old-age provision might be inclined to have higher sale price expectations. Lastly, we control for the entrepreneur's gender (male = 0, female = 1)

3.3. Analyses and Results

3.3.1 Descriptive Data

Table 1 presents descriptive statistics as well as a correlation matrix for all of the variables used in the models reported. In general, the correlations are only low to moderate.

Furthermore, we examined the variance inflation factors of our estimation variables; the variance inflation factors range from 1.01 to 2.07, with an average of 1.24, and are thus below the generally established threshold of 10 (Hair et al., 2006, Tabachnick and Fidell, 1996).

Insert Table 1 about here

Moreover, a frequency analysis of our data reveals first insights on the extent of the emotional pricing component (see Table 2 for numbers and an explanation of underlying assumptions). On average, owner-managers intend to sell their firm at a discount between 11% (sales to another firm) and 50% (FBO). Prospective discounts for MBOs and MBIs are 26% and 17%, respectively. Compared to those prospective considerations, data from our sample used for the post-hoc test reveal that the actual emotional pricing component is lower for FBO (42%), similar for MBOs (26%), and higher for MBI to familiar people (36%), MBI to strangers (26%), and for sales to firms (22%). Those findings will be interpreted and discussed in the discussion section (chapter 4).

Insert Table 2 about here

3.3.2 Results of Linear Regression

We tested our hypotheses based on OLS regression with the entrepreneur's emotional pricing component as dependent variable (see Table 3). Model 1 contains only the control variables, in Model 2 the independent variables (financial performance, exit route choice, CEO tenure) are added. Throughout the Models 3 to 7, we included the moderators (interaction of CEO tenure with financial performance as well as exit route choices).

Model 1 reveals a negative and significant effect of family business status on expected sales price ($\beta = -0.088$, $p < 0.01$) and a positive and significant effect of year of company foundation ($\beta = 0.066$, $p < 0.1$) and pension plan ($\beta = 0.112$, $p < 0.001$). Those results show that, in general, CEOs of family firms have lower sales price expectations. This can be

attributed to the prevalence of FBO as preferred exit choice in this type of firm (compare results of model 2). The higher the year of company foundation—that is the younger the firm—the higher is the sales price expectation. One could argue that this is in line with our argumentation above that a long history of the firm increases emotional attachment. Moreover, in accordance to our argumentation above, the firm being part of the pension plan leads to higher sales price expectations. Model 1 has an F-value of 4.564 and an adjusted R^2 of 0.022.

According to Model 2, financial performance has a positive and significant ($\beta = 0.076$, $p < 0.01$) effect on sales price expectations, thus supporting H1. FBO ($\beta = -0.411$, $p < 0.001$) and MBO ($\beta = -0.078$, $p < 0.05$) exert a negative and significant effect on sales price expectations (relative to “unknown/unsure” as baseline category), whereas sales to another firm exerts a positive and significant effect ($\beta = 0.074$, $p < 0.05$). Sales to another firm- and family-external person is positive yet non-significant ($\beta = 0.027$, $p > 0.1$). Hypothesis 2 is thus largely supported: As compared to the base category (“successor type unknown/unsure”), individuals that are close to the entrepreneur receive a discount to the real value, whereas “anonymous” buyers will have to pay an additional amount of money. CEO tenure exerts a negative and significant effect on sales price expectations ($\beta = -0.081$; $p < 0.05$), thus confirming H3a. Model 2 further shows that the control variables family business and foundation year lose their significance as soon as the independent variables are added. In model 2, the F-Value is 21.171 and the adjusted R^2 is 0.201.

In Models 3 to 7, the interaction effects are added, yet none of those variables is significant. Thus hypotheses 3b and 3c are rejected. The F-value (15.206) and adjusted R^2 (maximum 0.200) reveal that this model is not superior as compared to Model 2.

 Insert Table 3 about here

3.3.3 Robustness Test

A robustness test using ordinal regression confirmed most of the findings presented in chapter 3.3.2., which is based on OLS. In particular, the independent effects of firm performance ($p < 0.001$) and CEO tenure ($p < 0.01$) remained significant. FBO ($p < 0.001$) and MBO ($p < 0.001$) settings also exert a significant effect on the CEO's emotional pricing component, yet the effects of MBI and sales to another firm were insignificant in this model. Among the control variables, perceiving the firm as part of the pension plan also remained significant ($p < 0.01$).

3.3.4 Post Hoc Test (Retrospective Analysis)

The results showed above can be perceived as intended behaviors (Ajzen, 1991). However, theory of planned behavior has been constantly challenged and criticized by researchers because planned behavior does not always turn into actions and thus intentions might not be a reliable predictor of actual behavior (Armitage and Conner, 1999). As this might substantially limit the contribution of our findings, we decided to perform a post-hoc test, which scrutinizes some of our findings based on a sample of recent entrepreneurial exits. As described in the section on data collection, we identified 523 actual entrepreneurial exit processes in our overall sample, 455 of which provided information on actual sales prices (measured as ratio of sales price to real value of the firm). Based on this sub-sample we performed another set of OLS regression.

For details on the data collection process, please refer to chapter 3.1. Regarding the measurement of the dependent variable—actual sales price—, we used the same scale as described in the methodology section (3.2); yet we asked about *actual* buying prices (relative to real firm value) rather than *expected* selling prices. Regarding the independent variable “financial performance,” we relied on a single item, 5-point Likert scale: The respondent was asked to assess the firm's performance in comparison to its peers *at the time of transfer*. Due to potential retrospective biases we chose 5 rather than 7 points in the Likert-like scale and we also referred to a single- as opposed to multi-item measure. Regarding the closeness of

successor and incumbent at the time of transfer, i.e. the actual chosen exit route, we asked the respondent about his or her relationship to the predecessor at the time of transfer:

Respondents could choose among the following options: (1) child, (2) spouse, (3) other relative, (4) employee, (5) friend, (6) business partners (7) no relationship. Options 1, 2, and 3 were summarized as FBO.

We used the year of the firm's foundation, a family firm dummy, industry, size of the firm (measured as number of full time employees), and gender of the incumbent as control variables. For a detailed description of the operationalization of the control variables, please see the respective paragraph in the methodology section (3.2).

The descriptive statistics (Table can be obtained from first author) again reveal only low to moderate levels of correlation. The highest VIF value is 1.414 thus indicating a low risk of multicollinearity. To test the effect of financial performance and exit route choice on actual sales prices, we ran a set of OLS regressions (Tables can be obtained from first author). Model 1 only contains the control variables. Industry ($\beta = -0.139$; $p < 0.01$), size ($\beta = -0.102$, $p < 0.05$), and gender ($\beta = -0.138$; $p < 0.01$) exert a negative and significant effect on sales prices. Those results reveal that larger firms are sold at a discount, a finding, which might point to financing issues when selling larger firms to individuals. Moreover, our findings indicate that women entrepreneurs give larger discounts to successors as compared to their male counterparts. Adjusted R^2 of Model 1 is 0.039, the F-value is 4.404. In Model 2, the independent variables are added. Financial performance at the time of transfer does not exert a significant effect ($\beta = -0.005$; $p > 0.1$). This finding contradicts hypothesis H1 (see discussion for explanation). In our model, the reference category for exit route choice is the family buy-out. All other exit route choices exert a positive and significant effect: MBO— $\beta = .206$, $p < 0.001$; MBI to friend— $\beta = 0.106$, $p < 0.05$; MBI to unknown individual— $\beta = 0.207$, $p < 0.001$; sales to another firm— $\beta = 0.185$, $p < 0.01$. Those findings further support hypothesis 2. The adjusted R^2 is 0.082, the F-value is 4.689 and thus higher than in Model 1.

4 DISCUSSION

In our survey-based study, we investigate emotional pricing of Swiss entrepreneurs in the context of owner exit in SMEs. Our findings show that emotional aspects induce owners to offer their firm at a substantial discount. Indeed, the average expected sales price is slightly more than 70% of the firm's real value, hence indicating emotional pricing of 30% of the firm's value. By providing detailed and specific information on those emotional pricing values (see in particular Table 2), our findings contribute to the ongoing discussion whether emotional attachment of selling owners leads to increased ("premium") or decreased ("discount") sales prices (Astrachan and Jaskiewicz, 2008, Zellweger and Astrachan, 2008).

Our results are in line with previous findings that private firms are often traded at a discount (Granata and Chirico, 2010, Officer, 2007). So far, this discount has often been attributed to an undervaluation of private firms by buyers, e.g., due to perceived lack of professionalism of firms owned by a family, and those individuals' negotiations skills (Granata and Chirico, 2010). Our specific study design, which surveys intentions of owners that plan their exit, however, enables us to show that (part of) those discounts are rooted in the seller's side, in particular his or her loss aversion, not the buyer's side. A comparison of the prospective and retrospective findings on emotional pricing reveals that for unfamiliar buyers (MBO, MBI) the actual discounts are indeed higher than the intended ones. We thus conclude that both, the owners' emotional aspects as well as negotiation skills of successors, reduce the actual transaction price of the firm.

Our study also advances theory on entrepreneurial exits. We build on and extend previous valuable attempts to explain choices of exiting entrepreneurs by loss aversion (Sandri et al., 2010, Wennberg et al., 2010). Combining prospect theory (Kahneman and Tversky, 1979) and emotional aspects of key decision makers has already been proven to be powerful in other organizational contexts (Ariely, Huber and Wertenbroch, 2005). Our approach is novel in that we consider a broad range of possible losses associated with

entrepreneurial exits such as loss of the firm, loss of control and influence, and loss of information stream.

In particular, we argue that entrepreneurs do not fully act as *homo oeconomicus*, yet are driven by bounded rationality (Cyert and March, 1963), in particular loss aversion (Kahneman and Tversky, 1979). Under bad financial performance, entrepreneurs might fear to be unable to find a willing (and capable) successor for their underperforming firm. As they are reluctant to realize the ultimate loss of the firm, i.e. liquidation, the owner-managers lower their sales price expectations (measured in percentage of real value; H1). This hypothesis finds strong and significant support based on our analysis on planned behavior of resigning entrepreneurs, however, the effect becomes insignificant when we look at actual, past transactions. In line with critics on theory of planned behavior (Armitage and Conner, 1999), this might indicate substantial deviations of planned and actual entrepreneurial behavior. Another possible explanation points to methodological issues: The assessment of the firm's performance at the time of transfer might be distorted, for instance by the applied assessment by an outsider, by retrospective bias (Janson, 1990), or by self-serving bias (Bradley, 1978). Our findings related to hypothesis 1 extend prior work in the field of entrepreneurial exits (Wennberg et al., 2010) and provide a more nuanced understanding of the performance—entrepreneurial exit relationship. Moreover, they indicate that owners' performance attainment discrepancies, which have been shown to affect firm behavior in several contexts (e.g., Chrisman and Patel, 2012) are also relevant in situations of entrepreneurial exit.

Furthermore, our results—from both samples—reveal a strong dependence of sales price expectations on the chosen exit route. We argue that the “closer” or more familiar the successor is to the resigning entrepreneur, the larger the discount that this person receives. Specifically, our results (from the retrospective sample; for prospective discounts see Table 2) show that family members receive the largest discount (sales price on average 58% of real value), followed by firm transfers to friends (70% of real value). Other family-external

individuals who take over the company (MBO, MBI to unknown person) have to pay 74% of the firm's real value on average. Firms taking over the entrepreneur's former business have to pay most as they, on average, only achieve 22% discount. Besides the relevance for studying valuation of SMEs, those findings might also draw the scholarly attention to the following aspect: Given the substantial differences of emotional pricing components between sales to firm-external "friends" and sales to "strangers" —both exit routes typically considered as MBI—, a more detailed investigation of the relationship between seller and owner is required for further studies. Indeed, roughly 50% of all MBI cases in our sample referred to business transfers to family- and firm-external "friends" rather than "strangers."

We further hypothesized that entrepreneurial tenure, which goes along with growing emotional attachment to the firm, substantially affects the entrepreneur's sales price expectations (Zellweger et al., 2012) and positively moderates the effects of financial performance and exit path choice. While our findings based on the entrepreneurs' expected sales prices support the direct influence (H3a), we had to reject the interaction hypotheses (H3b, H3c). Our findings regarding hypotheses 2 and 3 support the notion that not only sales price matters for the resigning entrepreneur but also "soft factors," as such our study can be interpreted as indirect, quantitative support of Graebner and Eisenhardt's (2004) case-based propositions that the resigning owner is more concerned about whom the business is transferred to as compared to sales price maximization. Entrepreneurs, who exit their businesses, care about the future of their former business and thus search for a "fit" of firm and successor.

Our results further show that there are no significant differences regarding sales price expectations depending on the ownership type (as long as one controls for exit route). While industry has no significant effect in the sample based on intended prices, the effect becomes significant for data on actual transfers. In service industries discounts are typically higher than in production. One could explain this observation by the higher proportion of immaterial

as opposed to physical assets in service firms. Size exerts a negative and significant effect for actual sales prices:⁴ The larger the business, the lower the sales price as compared to real value. One possible explanation for this observation, which is also reflected in anecdotal stories of Swiss practitioners, is that owners of SMEs, particularly in rural areas, are challenged by low “supply” of willing and capable successors, who are able to finance the transaction. This challenge grows with the real value of the firm. Lowering the sales price might thus be seen as a potential remedy to ultimately find a successor. As expected, entrepreneurs, who perceive their business as component of their pension plan, are less willing to give a discount to their successor. Moreover, our regression analysis shows that *prospective* pricing emotional considerations do not depend on the gender of the resigning entrepreneur, while *retrospective* sales prices do: Female entrepreneurs provide larger discounts than male ones.

In general, our results contribute to the emerging stream of research that investigates the entrepreneurial exit process. In particular, we study a topic—emotional pricing—that has implicitly been noted in several studies (Graebner and Eisenhardt, 2004, Scholes et al., 2007), but has received little explicit, empirical investigation so far. Valuation of the entrepreneurial firm is an important component of the entrepreneurial exit process (Astrachan and Jaskiewicz, 2008, Granata and Chirico, 2010, Zellweger and Astrachan, 2008), as it determines the satisfaction with the exit process (Niedermeyer et al., 2010) as well as the probability of a (successful) exit process.

Our findings also carry about important practical implications. They reveal the importance of “familiarity to the resigning entrepreneur,” a finding, which might guide incoming entrepreneurs in their search process. Investing in building up longer-term relationships with the entrepreneur might ultimately pay off financially for the succession

⁴ One caveat here is that size of the firm was measured as of 2013, not the time of transfer.

candidate. For the resigning entrepreneurs, awareness of how the perceived financial performance distorts the sales price expectations is of certain value. Entrepreneurs, who are aware of this bias, might re-set and in particular raise their sales price expectations.

4.2 Limitations and Avenues for Future Research

As any empirical work, our study comes along with various limitations, which offer guidance for further research. First, the main part of our investigation is based on self-reported intentions of entrepreneurs rather than actual events. However, planned behavior is not necessarily converted into the respective activities. To mitigate limitations that arise from this issue inherent in any study based on planned behavior (Armitage and Conner, 2001), we tested several of the hypotheses based on a smaller sample of recent actual ownership transfers. While those results corroborate many of our findings, we still encourage further research to study the phenomenon in a longitudinal way that captures the owners' intentions before the entrepreneurial exit as well as the actual transaction prices. For such a study, it would also be interesting to include further dependent variables such as likelihood of firm transfer or incumbent's and successor's satisfaction with the ownership transfer.

A second limitation lies in the operationalization of our dependent variable. We asked our respondents to indicate their expected transaction price as percentage of real value. Implicit in this question is the assumption that owners know the real value of their business. Some scholars (Zellweger et al., 2012) try to overcome this issue by asking for absolute numbers related to the minimum sales price and comparing those numbers to figures on the firm's balance sheet items. However, as financial information on privately held Swiss firms is scarce, such a measure might also be distorted by incorrect responses. A further drawback of such a measure is that questions on absolute numbers regarding the financial structure of the firm are considered as highly sensitive. The response rate might thus be substantially lowered.

Reverse causality might be a concern regarding hypothesis 2 and 3b. One could also argue that the level of expected target price affects the targeted exit path. For instance, entrepreneurs aiming to achieve a high sales price might opt for sales to an external person rather than family-internal succession. We tried to partly mitigate this risk by inserting a control variable for the owner's future financial dependence on the firm and its proceeds. However, further research is required.

The geographical focus of our sample is limited to Switzerland. While the low levels of "noise" that come along with such a design can be assessed as strength of the study, it is also a weakness because of the limited generalizability. Cultural and country-specific aspects such as individualism (Wagner, 1995) or tax regulation (Colli, Perez and Rose, 2003) might affect the targeted transaction prices. To overcome this issue, we suggest replicating this study in other cultural and geographical contexts.

5. CONCLUSION

Entrepreneurs have certain ideas about the expected sales price of their firm. Those expectations differ substantially from the market price value and they are strongly influenced by emotional factors, in particular loss aversion: Framing of the exit, familiarity of incumbent and successor, and emotional attachment all exert influence on the expected sales price, and, at least partially, also on actual sales prices. A profound understanding of what drives resigning owners' emotional pricing in entrepreneurial exit processes is important for research as well as practice.

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TABLES

TABLE 1: MEANS, STANDARD DEVIATIONS AND PEARSON CORRELATIONS

	Mean	S.D.	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17
1 Emotional Pricing	5.16	2.08	1.000																
2 Family Business	0.84	0.36	-.089	1.000															
3 Industry	0.44	0.50	.029	-.072	1.000														
4 Size (# employees)	35.71	55.97	-.043	-.025	-.149	1.000													
5 Year foundation firm	1969.05	34.46	.086	-.115	.198	-.292	1.000												
6 Retirement plan	0.51	0.50	.110	.067	-.001	-.075	.054	1.000											
7 Gender	0.05	0.22	-.021	-.001	.121	-.082	.107	.047	1.000										
8 Financial performance	4.59	1.10	.051	-.018	-.043	.076	.048	-.004	.017	1.000									
9 FBO	0.41	0.49	-.415	.296	-.052	.085	-.123	-.018	.018	.058	1.000								
10 MBO	0.16	0.37	.058	-.290	-.001	-.050	.065	.005	-.055	.039	-.364	1.000							
11 MBI	0.10	0.30	.141	-.003	.115	-.127	.104	.034	.035	-.105	-.273	-.142	1.000						
12 Sales to firm	0.09	0.29	.195	-.141	-.009	.021	.072	.036	-.026	.027	-.267	-.138	-.104	1.000					
13 Tenure	22.83	12.01	-.148	.130	-.087	.105	-.383	.078	-.051	-.057	.191	-.045	-.041	-.011	1.000				
14 Tenure x Fin. Perf.	-.75	13.65	.037	.021	-.012	.005	.031	.010	-.033	.075	-.040	.023	.009	-.021	-.153	1.000			
15 Tenure x FBO	1.13	6.08	-.009	-.006	.031	.078	-.146	.002	-.035	-.038	.092	-.054	-.031	-.056	.177	.028	1.000		
16 Tenure x MBO	-.20	4.44	.022	.043	.007	.033	.030	-.028	.011	.024	-.054	-.063	.030	.016	-.005	.058	-.427	1.000	
17 Tenure x MBI	-.15	3.20	.026	-.042	-.092	.002	.053	.019	-.022	.011	-.041	.034	-.105	.016	-.098	-.051	-.291	-.124	1.000
18 Tenure x sales to firm	-.04	3.46	.016	.003	-.050	-.022	.048	-.035	.011	-.023	-.057	.016	.015	-.011	-.004	.003	-.311	-.136	-.088

All correlations with absolute value above .047 are significant at $p < 0.05$

TABLE 2: EMOTIONAL PRICING PER EXIT PATH

	FBO	MBO	MBI	SALES TO FIRM
Prospective Sample - Average Discount	50%	26%	17%	11%
Retrospective Sample – Average Discount	42%	26%	Friend: 30% Stranger: 26%	22%

Note – this table is based on the following assumptions: The categories in the questionnaire were translated into emotional pricing values as follows: Category ‘1’: 0%, ‘2’: 10%, ‘3’: 30%, ‘4’: 50%, ‘5’: 70%, ‘6’: 90%, ‘7’: 100%, ‘8’: 100%. Because of the last assumption, the displayed discounts are likely to exaggerate the actual discounts. However, “‘8’: 100%” is the best available assumption as we lack data on any requested premiums. Moreover, only 4.2% of all cases (48 in total) fall into this category

TABLE 3: OLS REGRESSION FOR EMOTIONAL PRICING INTENTIONS

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7
Family Business	-.088**	.026	.025	.029	.026	.026	.026
Industry	.012	.008	.008	.004	.008	.008	.008
Size	-.019	-.001	-.001	-.003	-.001	-.001	-.001
Founding Year	.066+	-.004	-.004	.000	-.003	-.004	-.004
Retirement Plan	.112***	.106***	.105***	.105***	.105***	.105***	.106***
Gender	-.036	-.028	-.028	-.027	-.028	-.028	-.028
Financial Performance		.076**	.076**	.077**	.076**	.076**	.076**
FBO		-.411***	-.411***	-.412***	-.412***	-.411***	-.411***
MBO		-.078*	-.078*	-.075*	-.079*	-.078*	-.078*
MBI		.027	.027	.028	.027	.028	.028
Sales to Firm		.074*	.074*	.077*	.077*	.074*	.074*
Tenure		-.081*	-.080*	-.088**	-.081*	-.081*	-.081*
Tenure x Fin. Perform.			.142				
Tenure x FBO				.047			
Tenure x MBO					-.007		
Tenure x MBI						.004	
Tenure x Sales to Firm							.000
R ²	0.028	0.210	0.210	0.212	0.210	0.210	0.210
Adj. R ²	0.022	0.201	0.200	0.202	0.199	0.199	0.199
Observations	967	967	967	967	967	967	967

+p<0.1; *p<.05; **p<.01;
***p<.001