



Summarizing 'Corporate Valuation' ...



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Basic FCF Model

- Value of Firm
 - Use CF of Firm and WACC as discounting rate
- Value of Equity
 - Use CF to Firm's Equity and Cost of Equity as discounting rate
- Modifications for ...
 - Firms in trouble
 - Estimate cash flow until they turn positive
 - Cyclical Firms
 - FCF are usually smoothed out
 - Firms with unutilized assets
 - Get the value of these assets externally and add

FCF Model ... Complications

- Firms with patents and product options
 - Get the value of these externally and add [or] better, real options pricing model
- Firms in the process of restructuring
 - Adjust CF to reflect business restructuring and discount rate to reflect financial restructuring
- Firms involved in acquisitions
 - (a) incorporate in FCF's; and (b) incorporate in risk
- Private firms:
 - Take riskiness of comparable firms that are publicly traded [or] relate the measure of risk to accounting variables

Why Estimates Usually Go Wrong?

Sources of uncertainty (by Aswath Damodaran)

- Our estimates of value can be wrong for a number of reasons (divided into three groups):
 1. Estimation uncertainty: Errors while converting raw information into inputs and use these inputs in models (common in valuing young technology company)
 2. Firm-specific uncertainty: The path that we envision for the firm can prove to be hopelessly wrong. (common in situations of information asymmetry for us vis-à-vis market participants)
 3. Macroeconomic uncertainty: Macroeconomic environment can change in unpredictable ways (common in mature cyclical or commodity company)

Good Responses to Uncertainty

Healthy responses to uncertainty would include:

- Better valuation models
- Valuation ranges
- Probabilistic statements
- The principle of parsimony helps

Unhealthy responses to uncertainty would include:

- Passing the buck
- Giving up on fundamentals (and going for day dreaming or technical analysis)

Limitations of Valuation

- Valuing alternate assets
- Valuing control
- While one can always state that ... in the long run market always prices assets based on their intrinsic value
 - ... finally, it is also a question of Demand and Supply
 - And hence there can be temporary asset mis-pricing due to liquidity issues
 - Also slightly longer time frame mis-pricing is created by a few market participants (using information asymmetry and large complexity) → typically you make things opaque) → RIL
 - Finally, Corporate Valuation is very successful over the long-run

Corporate Valuation

- How much of Corporate Valuation did we cover?
- Our focus was on connecting theoretical knowledge to practical aspects through ... Comprehensive Project, Illustrations, Examples, and Mini Case Studies.
- Two things left ... DTL, Valuing Infant Inds,
- However, (within time and other constraints) we covered quite a range ... in terms of 'firm size', 'industry type', 'valuation model', 'risk-return' profiles, ...
- Why was this course tailored in this way? ...

