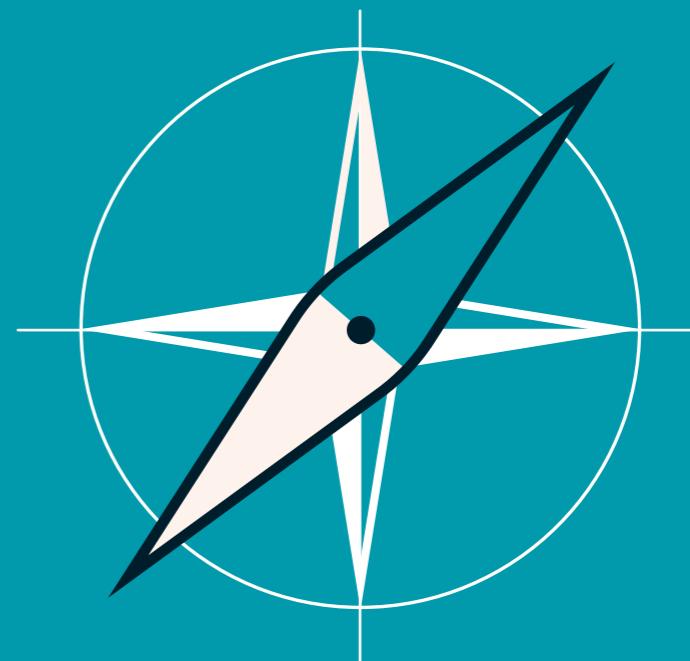


The Valuation Compass

Valuation as a guide for
corporate finance decisions



OWL PRESS

Jürgen Hanssens
Leentje Moortgat

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PREFACE

Given that the future is inherently uncertain, we do not believe the value of any business can be known with certainty at a given point in time, so our aim is to be generally right as opposed to precisely wrong.

– Wally Weitz

We start this book with a quote from Wally Weitz, the founder of Weitz Investment Management and a board member of Berkshire Hathaway since 2022. His words highlight one of the central challenges faced by every valuation practitioner: valuation is inherently forward-looking, yet no one possesses a crystal ball to predict the future with certainty. Consequently, uncertainty is a fundamental element embedded in every valuation exercise. As Weitz suggests, possessing strong valuation skills enables one to be generally right instead of precisely wrong when estimating a firm's value, even in the face of that uncertainty.

The aim of this book is to provide such foundational skills to students and (junior) valuation practitioners by combining practical insights with academic rigor. Yet, this book goes beyond simply introducing valuation techniques—it seeks to explain the reasoning, context, and application behind them.

- Part I provides a broad introduction to valuation, covering fundamental questions, such as why we conduct valuations, and introducing key valuation concepts. While many students and junior practitioners assume that valuation begins with an empty Excel sheet, we will see that valuation is more than just crunching numbers. A crucial first step in any valuation exercise is understanding the subject company—its business model, operations, and future prospects. These topics are at the heart of Part I of this book.
- Part II focuses on the quantitative side—“crunching the numbers.” Here, we introduce several valuation approaches, including intrinsic valuation methods (such as discounted cash flow (DCF) and adjusted present value (APV)), relative valuation techniques (comparable companies, or CoCos, and comparable transactions, or CoTrans), and book value-based approaches. We also discuss when certain discounts or premia may be appropriate. Since valuation proficiency improves through practice, we provide an online valuation case to help readers master the most commonly used techniques in real-world settings.
- Part III of this book builds a bridge to three key corporate finance decisions: the investment, financing, and payout decisions. In this part, we explore how valuation connects to and informs these strategic finance choices.

This book is accompanied by a dedicated website offering additional resources to complement the material presented here. On the website, readers will find supplementary information related to the book, updates and corrections to any remaining errors, an online valuation case, and curated links to external sources useful for conducting valuation analyses. The website can be accessed via the QR code below:



Two of these external data sources deserve special mention in this preface, as we refer to them frequently throughout the book:

- **Aswath Damodaran's data:** We make extensive use of data provided by Aswath Damodaran, Professor at NYU Stern School of Business and widely recognized as the “Dean of Valuation.” Each year, he publishes detailed datasets on a wide range of valuation metrics and ratios, such as equity risk premia by country and valuation multiples by industry and region. These data are often used by valuation professionals worldwide and are equally valuable for students. A direct link to Damodaran’s website is available on our webpage.
- **Vlerick M&A Monitor:** This annual survey, conducted by colleagues at Vlerick Business School, provides key insights into the Belgian mergers and acquisitions (M&A) market. The M&A Monitor is updated each year, and a link to the latest edition can always be found on our website.

In the development of this book, generative AI tools, most notably ChatGPT (version ChatGPT-5), were employed to support the authors throughout various stages of the writing process. Specifically, these tools were used to assist in the refinement of language and style, and to facilitate the structured development of illustrative cases, pedagogical examples, and graphical representations. All outputs produced with AI assistance were rigorously reviewed, verified, and, where neces-

sary, substantially revised by the authors to ensure accuracy, coherence, and academic integrity. At no stage were generative AI tools used as autonomous content creators or as substitutes for the authors’ professional judgment.

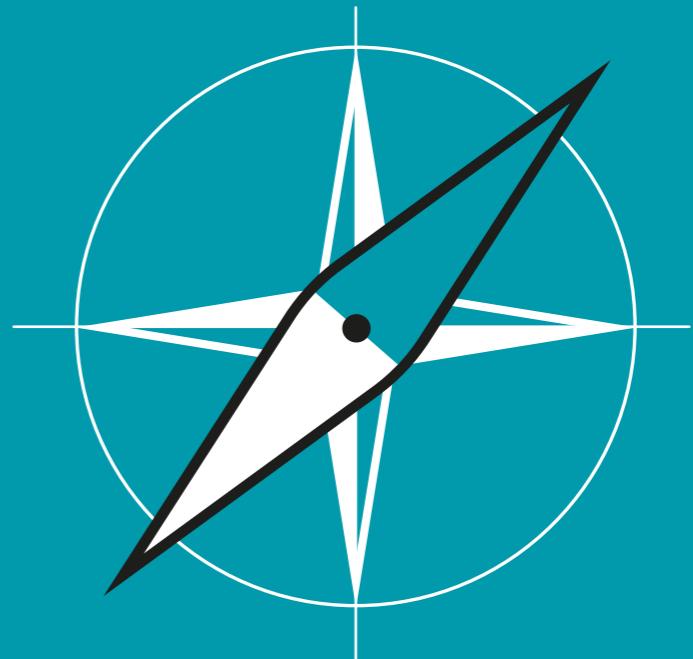
To conclude, we hope that this book helps readers to gain a deeper understanding of company valuation and that it illustrates how valuation serves as a compass for the three central corporate finance decisions.

Jürgen Hanssens
Leentje Moortgat
Ghent, 2025

PART I

THE BASICS OF VALUATION

Valuation – What's in a name?



When students—or junior M&A and valuation practitioners—think about valuing a company, they often imagine crunching numbers: starting with a blank Excel sheet, building complex models, and producing a single number for the firm’s value. Numbers are, of course, crucial in any valuation, but they form only part of the process—and they are not the starting point. So what is the starting point?

In the first part of this book, we lay out the basics of valuation by addressing key questions such as: *Which company are we valuing? Are we estimating the enterprise value (EV) or equity value? What is the valuation date?* We can only choose the most appropriate valuation method after answering these questions.

Everything starts with understanding the context for the valuation. Put differently: before analyzing numbers, we need to understand the company’s story. That begins with asking: *Why are we valuing this company? Is it the target of an acquisition? Are we valuing it from the buy side or the sell side? Or do we need to perform the valuation for other purposes, such as tax or accounting?*

Once we get an answer to these questions, we must dig deeper. We ask: *What are the company’s main activities? What is its business model, and how does the company make money? What is its risk profile? What are its strengths and weaknesses? Who are its competitors? In which market does the company operate? What is the company’s investment strategy?* Answers to such questions help us assess the firm’s potential and its capacity to create value.

Because valuations are forward-looking, they always involve uncertainty. A sound valuation therefore produces not a single figure but a range of possible values. This approach avoids what Aswath Damodaran calls the “Bermuda Triangle of valuation.” Chapter 1 of this book explores the valuation fundamentals in greater detail.

Once we identify the company at the center of our valuation, we must distinguish between price—easily observable for listed firms—and value. We also need to decide whether to estimate the company’s total value (EV) or just the value of its equity. In addition, we must determine the valuation date and assess an appropriate target level of net working capital (NWC). Chapter 2 addresses these key decisions.

After developing a deeper understanding of the subject company (“the story”), we can turn to valuation methods (“the numbers”). Chapter 3 introduces different techniques, contrasting how practitioners categorize valuation methods with how academics do so (following Damodaran’s framework), and showing how these perspectives connect. Finally, we discuss how to select the most appropriate valuation approaches.

We conclude this introduction with an important piece of advice, inspired by Damodaran’s perspective on valuation:

Valuation is not an art, nor a science. It is a craft.

- **Why is valuation not an art?** If valuation were an art, only those with an innate gift could master it, while others would remain incapable of valuing a company. Yet countless textbooks and courses on valuation prove otherwise. Valuation can be taught and learned—so it is not an art.
- **Why is valuation not a science?** Scientific laws are universal and yield the same outcome regardless of circumstance. If you drop a pencil, it will always fall at its terminal velocity, whether you are the buyer or seller of that pencil. Valuation, however, relies on assumptions. Different perspectives and choices inevitably lead to different outcomes. For that reason, valuation cannot be a science.
- **Why is valuation a craft?** A craft, like playing the piano, is a skill that you learn by doing it. The more you do it, the better you become. Valuation follows the same principle: skill comes from application. We therefore encourage you to actively practice what you learn throughout this book.

CHAPTER 1

INTRODUCTION

As I often remind our analysts, 100% of the information you have about a company represents the past, and 100% of the value depends on the future.

– Bill Miller

INTRODUCTION

Despite increasing emphasis on environmental, social, and governance (ESG) factors, many companies still prioritize maximizing shareholder value as their primary goal. Rooted in classical corporate finance theory, this traditional focus often elevates short-term financial returns over broader societal and environmental responsibilities. Although ESG initiatives are shaping business strategies more and more, the pursuit of shareholder wealth continues to dominate—and can sometimes overshadow—measures of true corporate success.

To maximize shareholder value, companies make three types of financial decisions:

- **Investment decisions:** Which assets should the firm acquire? Which projects or investments promise the highest returns? How can we maximize returns on our investments?
- **Financing decisions:** How should we fund our operations? What share should come from internal resources, and how much can we raise through external debt or equity?
- **Payout decisions:** How much of our profits should we distribute to shareholders? Should we pay dividends, repurchase shares, or retain earnings to finance future growth?

The outcomes of these decisions appear in the balance sheet and income statement. However, as renowned value investor Bill Miller noted, accounting statements reflect the past, while valuations focus on the future. Therefore, understanding how a firm's investment strategy, financing choices, and payout policy will generate value going forward is essential.

In this first chapter, we establish a solid foundation for understanding the company to be valued, equipping us to better predict its potential to create value in the future. First, it is crucial to understand the situations in which valuing a company matters, a topic we explore in Section 1.1. Next, to clarify the concept of “value,” we examine different valuation standards (Section 1.2) and bases of value (Section 1.3).

In Section 1.4, we then explore the building blocks of valuation, providing insights into the firm's investment, financing, and payout decisions, as well as its long-term strategy for creating value. Finally, we highlight common pitfalls in any valuation exercise—what Aswath Damodaran calls the “Bermuda Triangle of valuation”—discussed in Section 1.5.

1.1 THE NEED FOR VALUATION

Valuation plays a crucial role in corporate finance, strategic planning, and regulatory compliance. It is a fundamental component in a wide range of contexts, from routine financial reporting to complex transactional and legal processes. This section provides a comprehensive overview of the key situations in which valuations are required, bridging theoretical foundations with practical applications. Rather than being a standalone exercise, valuation is embedded across the corporate, legal, and financial spectrum. Whether used for compliance, strategic guidance, or dispute resolution, valuations enable stakeholders to make informed, data-driven decisions grounded in economic reality.

- **Mergers, acquisitions, and disposals:** Valuations are indispensable in merger and acquisition (M&A) scenarios. Whether a company is seeking to acquire a target, divest a business unit, or contribute assets to a joint venture or special purpose vehicle (SPV), a sound valuation informs negotiation strategy, pricing decisions, and the identification of key value drivers and synergies.
- **Fairness opinions:** In transactions involving publicly listed companies or transactions where minority shareholders' rights are a concern, fairness opinions provide an independent assessment of whether the terms of a proposed deal are financially reasonable. These valuations are typically prepared for boards of directors to support decision-making in the context of M&A activity, restructuring proposals, or share buybacks. In legal disputes or arbitration, fairness opinions can also serve as evidence in defending the integrity of a transaction.

- **Financial reporting and accounting standards:** Under international accounting standards, valuations are often mandatory to ensure transparency and accuracy in financial reporting. Key valuation applications in this context include:
 - **Purchase price allocation (PPA):** Following an acquisition, International Financial Reporting Standards (IFRS) 3 requires the allocation of the purchase price to the identifiable assets and liabilities of the acquired business, including the recognition of residual goodwill.
 - **Goodwill impairment testing:** Required annually or when impairment indicators arise, as per International Accounting Standards (IAS) 36 and other accounting standards, such as U.S. Generally Accepted Accounting Principles (GAAP). These tests assess whether the carrying value of goodwill or other assets exceeds their recoverable amount.
 - **Fair value measurements:** IFRS 13 mandates fair value assessments for many assets and liabilities, calling for the use of market-based or income-based valuation techniques.
- **Tax and legal purposes:** Valuation plays a central role in tax planning, compliance, and legal restructuring. Authorities often scrutinize valuations in these contexts, particularly in cross-border or intra-group transactions. Common scenarios include:
 - **Group reorganizations:** Valuations are necessary during mergers, demergers, carve-outs, spin-offs,¹ or capital restructurings.
 - **Transfer pricing analysis:** To support defensible pricing in intercompany transactions.
 - **Management incentive plans:** Especially relevant in private equity (PE) settings, where incentive instruments, such as stock options or free shares, require careful valuation for both tax and accounting purposes.

¹ Carve-outs and spin-offs are separation transactions in which a portion of a business is separated from the parent company. Valuation is required in both cases to allocate assets, liabilities, and equity between the two entities. In a carve-out, the parent company sells a portion of its business (often a subsidiary or division) to outside investors—often through an initial public offering (IPO)—while often retaining partial ownership. This transaction generates cash for the parent company. In a spin-off, the parent company distributes shares of the subsidiary to its existing shareholders, creating a new, fully independent company.

- **Strategic planning and business analysis:** Valuations are frequently undertaken to support strategic decision-making, often in the context of internal performance assessments, investment planning, or market positioning. Such valuations typically focus on identifying key value drivers, understanding business performance under various scenarios, and modeling the impact of strategic initiatives.
- **Raising capital and financing:** In the context of raising equity or debt financing—especially for startups—valuations help determine the company's worth and guide discussions with investors. They are also used to assess loan-to-value ratios and inform lending decisions by financial institutions.
- **Restructuring and litigation support:** Valuation services are integral to corporate restructuring, insolvency proceedings, and legal disputes. Independent valuations support asset disposals, spin-offs, or recapitalizations, especially when mandated by regulators or courts. In contentious settings, valuation professionals may also act as court-appointed experts or provide advisory services in shareholder disputes, contract breaches, or supplier/customer disagreements.
- **Valuation of complex financial instruments:** Valuations are essential for pricing complex or derivative financial instruments, which may include management incentive schemes, embedded financial products, or structured debt instruments. These valuations often require advanced methodologies (e.g., Monte Carlo simulations), option pricing models (e.g., Black-Scholes), or other stochastic modeling techniques.

Example: Solvay splits into Syensqo and Solvay

In December 2023, the Belgian chemical group Solvay completed its split into two independent, publicly listed companies: Solvay and Syensqo. The new Solvay now focuses on producing essential chemicals such as soda ash, peroxides, silica, and other basic chemicals, while Syensqo concentrates on specialty materials and advanced solutions for innovation-driven sectors.

The transaction was structured as a spin-off: no new capital was raised, and existing Solvay shareholders received shares in the newly created Syensqo. This allowed investors to gain direct exposure to both businesses without additional investment.

The strategic rationale behind the split was to unlock value by clearly separating two very different business profiles. Essential chemicals are capital-intensive, cyclical, and cash-generative, whereas specialties are higher-growth, innovation-driven, and require distinct capital allocation and risk strategies. By splitting the group, management aimed to increase transparency, sharpen strategic focus, and give investors the flexibility to invest in one or both profiles.

At the time of the transaction, shareholder support was overwhelming, with 99.53% of the shareholders voting in favor of the spin-off at the extraordinary general meeting.

This comprehensive overview clearly indicates that valuation needs are spread across the business life cycle. Valuations can occur pre-deal, during the deal execution, and post-deal:

- **Pre-deal:** Transaction fairness opinions, pre-deal PPAs, etc.
- **Deal execution:** Asset valuation in carve-outs, equity value assessments, etc.
- **Post-deal:** Impairment testing, financial instrument valuation, and annual reporting, etc.

1.2 VALUATION STANDARDS

Given the diverse contexts in which valuations are conducted—ranging from transactions and financial reporting to taxation and legal proceedings—clear and consistent guidance is essential to ensure transparency, comparability, and professional integrity. To address this need, various standard-setting bodies have developed valuation standards tailored to specific asset classes, industries, and jurisdictions. These frameworks aim to establish best practices within the valuation profession and offer a shared language for stakeholders across the financial landscape. Below are some of the most widely recognized and applied valuation standards:

- **The International Valuation Standards (IVS) issued by the International Valuation Standards Council (IVSC):** The IVS are widely recognized and globally used by valuation professionals to estimate the value of assets for financial reporting and regulatory purposes and to determine the value of a company in the context of a transaction.
- **The International Private Equity and Venture Capital (IPEV) Valuation Guidelines issued by the IPEV Board:** The IPEV guidelines set out recommendations on the valuation of private capital investments.
- **The Uniform Standards of Professional Appraisal Practice (USPAP) issued by The Appraisal Foundation:** Real estate appraisers in the United States (U.S.) have to adhere to the USPAP. The USPAP can also be used to estimate the value of companies.
- **The Royal Institution of Chartered Surveyors (RICS) Valuation—Global Standards (Red Book) issued by the RICS:** The Red Book can be considered the leading standard for real estate valuations globally and is widely adopted, especially in the United Kingdom (UK) and Europe.
- **The European Valuation Standards (EVS) issued by The European Group of Valuers' Associations (TEGoVA):** The EVS are mainly used in the real estate and property sectors in European countries.

- **The American Society of Appraisers (ASA) Business Valuation Standards issued by the ASA:** These standards specifically focus on the valuation of companies and are mainly followed by business appraisers in the U.S.

- **The International Financial Reporting Standards (IFRS) and Generally Accepted Accounting Principles (GAAP) issued by the IFRS Foundation and Financial Accounting Standards Board (FASB):** These are accounting standards that also include guidelines for valuations that are performed for financial reporting purposes. The focus of these guidelines is on the fair value measurement of assets and liabilities.

As a result, there is no universally mandated valuation standard. Business appraisers are often not required to follow any specific framework, and adherence to one or more standards is typically left to the appraiser's discretion. In practice, enforcing these standards is challenging, as most valuation reports are not publicly available, making it difficult for standard-setting bodies to monitor compliance. Additionally, the inherently diverse nature of valuations—varying by purpose, context, and methodology—further limits the ability of these bodies to issue detailed technical guidance that applies uniformly across cases.

1.3 BASES OF VALUE

Just as multiple valuation standards exist—each developed by different standard-setting bodies—there are also various definitions of value, each suited to specific purposes and contexts. Selecting the appropriate definition is critical, as it directly shapes the valuation outcome. A valuation only holds meaning when interpreted within the context of its underlying basis of value. Below we define some of the most commonly used bases of value, as outlined by the International Valuation Standards (IVS) effective January 31, 2025:

- **Market value**, which is defined as “the estimated amount for which an asset and/or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm’s-length transaction, after proper marketing and where the parties had each acted knowledgeably, prudently and without compulsion.”
- **Investment value**, which is defined as “the value of an asset to a particular owner or prospective owner for individual investment or operational objectives.”
- **Synergistic value**, which is “the result of a combination of two or more assets or interests where the combined value is more than the sum of the separate values. If the synergies are only available to one specific buyer then synergistic value will differ from market value, as the synergistic value will reflect particular attributes of an asset that are only of value to a specific purchaser.”
- **Liquidation value**, which is defined as “the amount that would be realized when an asset or group of assets are sold from a liquidation sale, with the seller being compelled to sell as of a specific date.”
- **Fair value**, which is defined under IFRS 13 as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.”

The precise value definition will affect the estimated value. Therefore, a valuation should only be used for the purpose it was generated.

1.4 BUILDING BLOCKS FOR VALUATION

A comprehensive business valuation entails a thorough analysis of various interrelated components that collectively determine a company’s value. These essential building blocks can be categorized into operational, financial, and asset-based factors, each making a distinct contribution to the overall valuation process. Figure 1.1 represents these building blocks, which we will examine in more detail.

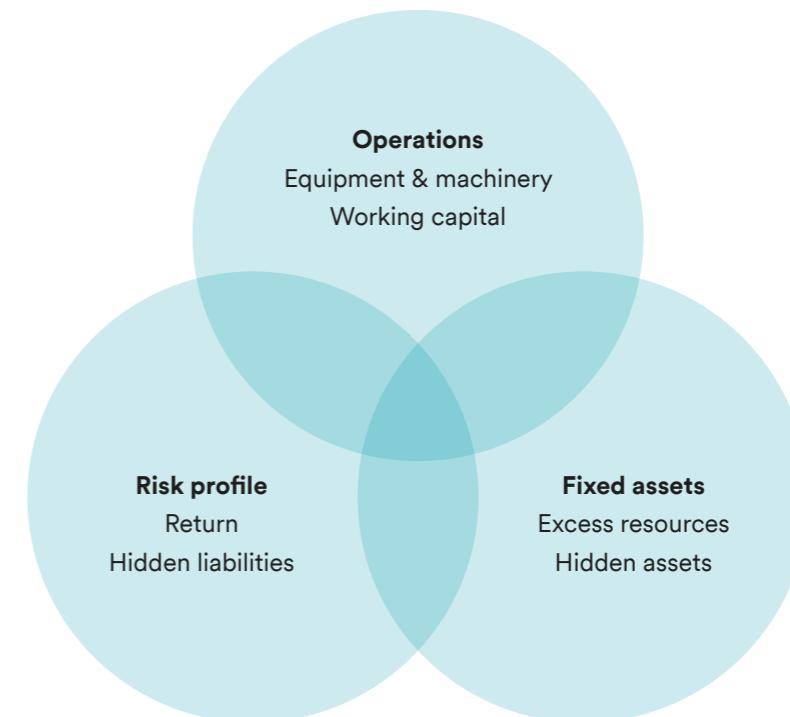


FIGURE 1.1
Building blocks for valuation.

Operational aspects form the foundation of value creation. Key considerations include: the company’s core operations, which reflect its day-to-day activities and operational efficiency; equipment and machinery, representing the physical assets that support production or service delivery; and working capital, which indicates the company’s liquidity position and short-term financial health.

In this context, a fundamental question for any business appraiser is: What sets the company apart from its peers? This competitive advantage may be rooted in operational factors, including a distinctive product or service, proprietary expertise, a favorable market position, exclusive contracts or intellectual property (IP) rights, or the availability of skilled labor, among others.

From a financial perspective, the company's risk profile is a critical determinant of value, as it reflects uncertainties related to the industry landscape, competitive positioning, and the quality of management. The expected return on investment, which depends on this risk profile, incorporates both profitability and growth potential, making it another key driver of valuation. It is essential to distinguish between expected returns and historical performance, as past results may have been achieved at the expense of future growth. Therefore, normalizing historical financial data is a vital step in the valuation process. Typical adjustments include management and director remuneration, non-recurring or extraordinary items, and rental expenses that diverge from prevailing market conditions. In addition, appraisers must consider hidden liabilities, such as contingent obligations or underreported debts. These may not be immediately apparent on the balance sheet but can significantly affect the company's enterprise value (EV).

Example: €345 million fine for TikTok owner

Big Tech companies such as Alphabet, Google, and Meta face intense scrutiny from European regulators, and ByteDance, TikTok's Chinese parent company, is no exception. In 2023, following a lengthy investigation, European authorities fined ByteDance €345 million for violating the EU General Data Protection Regulation (GDPR).

From a valuation perspective, such fines are generally treated as non-recurring, exceptional expenses and are typically excluded from normalized EBITDA, which aims to capture the company's sustainable earnings. Normalization adjustments usually remove one-time revenues and expenses that do not reflect ongoing operations.

In May 2025, ByteDance faced another GDPR-related fine, this time of €530 million. Although the fine remains under appeal, the same logic applies: it can be classified as an exceptional item and excluded from normalized EBITDA.

However, the recurrence of such fines raises a key analytical question. If regulatory penalties of this scale become frequent rather than isolated, they may represent an inherent cost of doing business. In that case, consistently excluding them from normalized EBITDA could overstate the company's true earnings power.

On the asset side, both tangible and intangible resources are relevant. Fixed assets—including real estate, infrastructure, and long-term equipment—represent durable investments that underpin operations. Excess resources, such as surplus cash or underutilized assets, can enhance value if correctly identified and appropriately valued. Hidden assets, such as IP, brand equity, and customer relationships, may also hold substantial value, even if they are not explicitly recognized in financial statements.

Together, these elements create a structured framework for assessing a company's value. Each building block must be carefully evaluated and integrated into the broader valuation approach to arrive at a fair and realistic estimate of a company's economic worth.

1.5 VALUATION MYTHS

Valuation standards and definitions of value aim to provide structure and consistency, but valuation is far from an exact science. Beneath its technical façade, valuation relies heavily on professional judgment, assumptions, and contextual factors. Consequently, several common misconceptions persist about what valuation can truly accomplish. To clarify these misunderstandings, renowned valuation expert Aswath Damodaran identifies a series of widely held myths that reveal how valuations are often approached and interpreted. These myths remind us that every model rests on uncertainty and that rigorous, critical thinking is essential for meaningful valuation analysis.

Myth 1: A valuation is an objective search for “true” value.

Valuation outcomes cannot be classified as simply “right” or “wrong,” because valuation is inherently subjective. Analysts make numerous assumptions, both when building forecasts—such as projecting future sales growth or EBITDA (earnings before interest, taxes, depreciation and amortization) margins—and when applying those forecasts in a valuation model—such as when estimating the discount rate. Different analysts may hold differing views on a company’s future prospects, resulting in varying valuation outcomes. Buy-side and sell-side analysts may also disagree on the company’s expected cash flows and risk profile. Consequently, a valuation is not a precise measure of a company’s “true” value but an estimate shaped by the assumptions and professional judgment of the analyst conducting it.

Myth 2: A good valuation provides a precise estimate of value.

No one can predict the future, while each valuation strongly depends on the assumptions made about what will happen in the future. Small changes in these assumptions (e.g., sales growth rate, discount rate, etc.) can have a significant impact on valuation outcome. As a result, valuers typically come up with a valuation range instead of a point estimate when performing a valuation, which they graphically represent in a valuation football field (further discussed in Chapter 6 – Relative valuation).

Myth 3: The more quantitative a model, the better the valuation.

The KISS principle (keep it simple, stupid) often applies to valuation. While quantitative models can handle large amounts of data, adding complexity can reduce transparency and obscure key assumptions. Complex models also tend to rely on more assumptions than simpler ones—and each assumption carries the risk of being wrong. Therefore, the quality of assumptions matters more than the complexity of the model. A strong valuation analysis links narrative to numbers and clearly explains the assumptions behind the model. In short, while financial modeling is important, valuation is far more than just mathematics.