MOORE

COMPANY VALUATIONS: MAKING COMPLEX THINGS SIMPLE

Company Valuations: Making Complex Things Simple

Company valuation, by its nature, has an inherent degree of uncertainty. The outcome of a company valuation process is an estimate of the value a third party might be expected to pay for an asset.

Notwithstanding this uncertainty, there are established corporate finance principles and methodologies which enable valuations to be prepared on a sound theoretical basis.

Generally accepted valuation principles and concepts are in turn guided by International Valuation Standards as set by the International Valuation Standards Council ("IVSC"). The IVSC is an independent organisation committed to advancing quality in the valuation profession by building confidence and public trust in valuation by producing standards and securing their universal adoption and implementation for the valuation of assets across the world. The International Valuation Standards are standards for undertaking valuation assignments using generally recognised concepts and principles that promote transparency and consistency in valuation practice.

At Moore, we have the corporate finance experience and expertise to apply these principles to privately owned Irish companies and arrive at a practical solution for our clients. The outcome of our valuation process is a detailed report setting out the theoretical basis upon which our valuation is prepared as well as detailed workings to show how we arrive at our conclusion.

The need for valuations

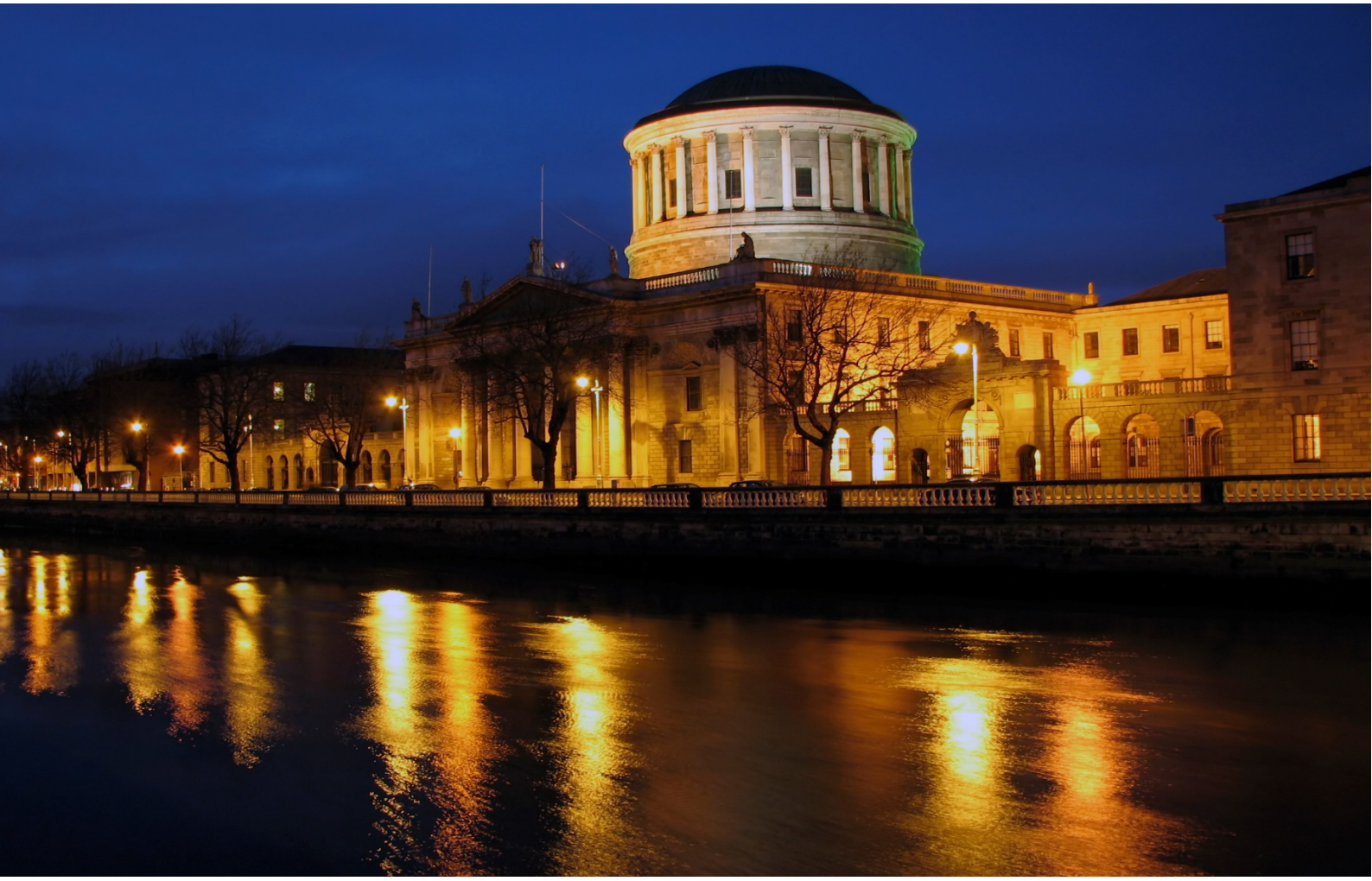
There are a number of scenarios where third party valuations are required:

- Share transfers – solicitors and or tax practitioners often require valuations to support share transfers as part of restructuring;
- Legal proceedings – shareholder disputes often generate the need for a company valuation;
- Merger/acquisitions – in any corporate takeover, share valuation is an integral part of a deal. Sound valuations are a key requirement;
- Equity placement – potential investors in an equity placement will often require a share valuation;
- Debt restructuring – in debt restructuring, the underlying company value is a key negotiation tool and share valuations play a central role in this process.

Our approach

Our approach involves a number of key steps:

- Financial analytics – we prepare a comprehensive review of the historical accounts of the company;
- Forecasting stress testing – we prepare a scenario "stress test" of forward looking statements of the company;
- Sector analysis – we complete a review of market sector financial ratios of the sector in which the company operates. This involves reviewing price earning ratios, costs of capital, beta factors and other market sector metrics;



- We prepare our valuation and present our draft report;
- Asset valuation often involves accounting and corporate finance concepts that may be abstract and complex. The purpose of the valuation engagement, the complexity of the asset being valued, and the user's requirement all influence the level of reporting detail needed, and also, the level of supplementary explanations and contexts to ensure the report is readable.
- Moore uses its professional judgment to ensure that the report is narrated with an appropriate level of detail and context to suit the reader's needs, guided by the overarching objective that the report must be, above all, readable by he or she who reads it.
- Following discussion and engagement with the company board, we finalise our report.

Our principal methodologies

The primary corporate finance principles upon which valuation methodologies are based can be summarised as follows:

- the value of a share is usually determined by the income flows that shareholders expect to receive from its ownership; and
- income flows that occur at different points in the future need to be discounted to reflect the time and value of money.

Valuation of private unquoted companies is more difficult as there is an absence of a developed market for the share transactions. In addition, there is generally a lower quality and quantity of information relating to the company. Furthermore shares in unquoted companies are subject to more risk, as unlike quoted companies, they do not operate in a corporate governance environment with rigorous operational and reporting demands.

"Making simple things complex is easy. Making complex things simple takes skill."

Market value is commonly derived by applying (or more) of the following valuation methodologies:

1. asset based methods;
2. capitalisation of earnings methods; and
3. discounted cash flows methods.

Asset based methods

Asset based methods are commonly used:

- when the company has substantial surplus assets, such as a property holding company or
- a special purpose company where it has fulfilled its purpose and is left with residual assets;
- when a business is operating at a loss or at a low return that is not consistent with the level of net assets employed; and
- when liquidation is anticipated or the future prospects of the company are extremely doubtful.

Capitalisation of earnings methods

Earnings based approach estimates a sustainable level of future earnings for a business ("maintainable earnings") and applies an appropriate multiple to those earnings, capitalising them into a value for the business. This approach is appropriate where the earnings of a business are sufficient to justify a value exceeding the value of underlying net assets, and where a relatively stable historic earnings pattern are demonstrated.

Income approach

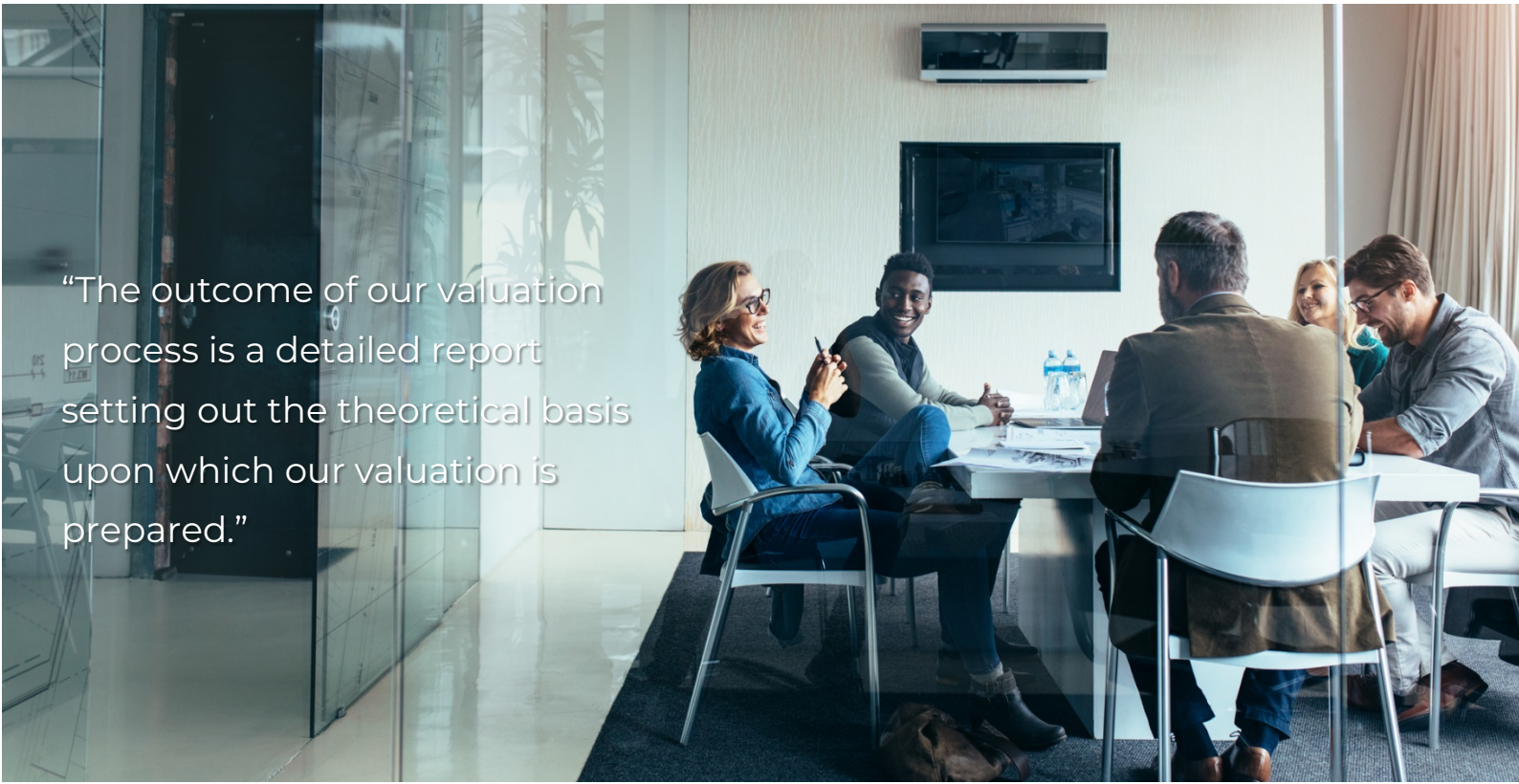
The income approach provides an indication of value by converting future cash flow to a single current value. Under the income approach, the value of an asset is determined by reference to the value of income, cash flow, or cost savings generated by the asset.

Discounted cash flows ("DCF") methods

DCF is based on the premise that the value of a business is the net present value ("NPV") of its future cash flows. It requires forecasting of cash flows over a suitable period of time, analysis of these future cash flows, the capital structure and cost of capital (discount rate), and an assessment of the residual value of the business remaining at the end of the forecast period.

Our final deliverable is a comprehensive report addressed to the Board which will contain:

- a standalone executive summary;
- a detailed analysis of our valuation approach;
- an analytical review of the key financial drivers of the company;
- a detailed breakdown of the application of our approach to the client company; and
- a clear conclusion.



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For more information on how our global services and sector expertise can help your business thrive in over 100 countries, just get in touch.

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