



What Affects Enterprise Value?

Got Revenue Growth?



What Affects Enterprise Value?

*“You’ve said before that raising debt or equity, repaying debt, repurchasing shares, issuing dividends, etc., do not impact **Enterprise Value**.*

*So then what **does** impact Enterprise Value? When would it actually increase or decrease?”*

What Affects Enterprise Value?

- **FIRST OFF:** This person's statement is not completely correct
- **IN THEORY,** capital structure changes such as raising debt and equity will not affect Enterprise Value...
- **IN REALITY,** there will still be some impact because the company's discount rate, or WACC, will change
- **However,** these changes will make a *relatively* small impact on Enterprise Value over small ranges (e.g., 10% debt to 20%)
- **Equity Value** will be affected far more by these types of changes



What Affects Enterprise Value?

- **Definition of Enterprise Value:** The value of the company's **core business operations** to **ALL the investors** in the company



- What is “The value of the core business operations”?

- **ANSWER:** The sum of the Present Value of a company's Unlevered Free Cash Flows, plus the Present Value of its Terminal Value



- **DCF Analysis:** Gives you a company's *implied* Enterprise Value



- **So:** If something affects the company's Unlevered Free Cash Flows, its Terminal Value, or both, it will affect Enterprise Value as well



What Affects Enterprise Value?

- **MOST COMMON:** The market expects higher or lower revenue growth from the company, or higher or lower margins
- **Example:** The company wins a major contract with a new customer
- **Example:** The company's expansion strategy into Southeast Asia succeeds more quickly than expected
- **Example:** The company closes down an unprofitable division, boosting its margins
- **Example:** The company negotiates a better supplier contract, boosting its margins



What Affects Enterprise Value?

- **Other Items:** Changes in expectations for Capital Expenditures, Working Capital, and non-cash adjustments such as D&A could also affect Enterprise Value...



- **BUT:** The impact is fairly small next to differences in revenue growth and operating margins

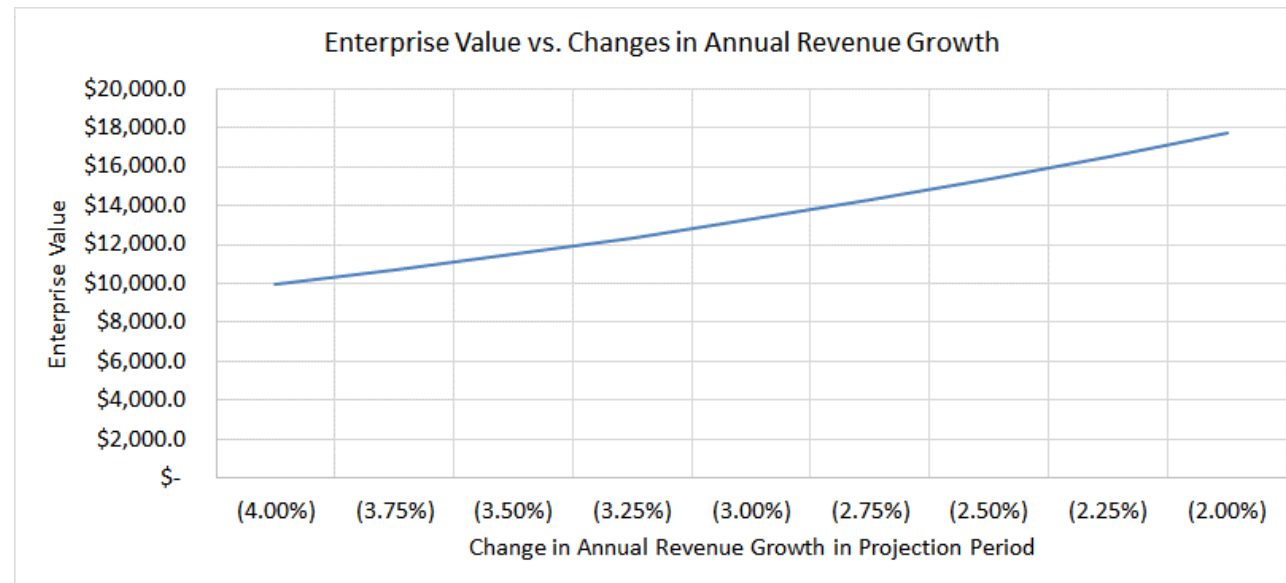
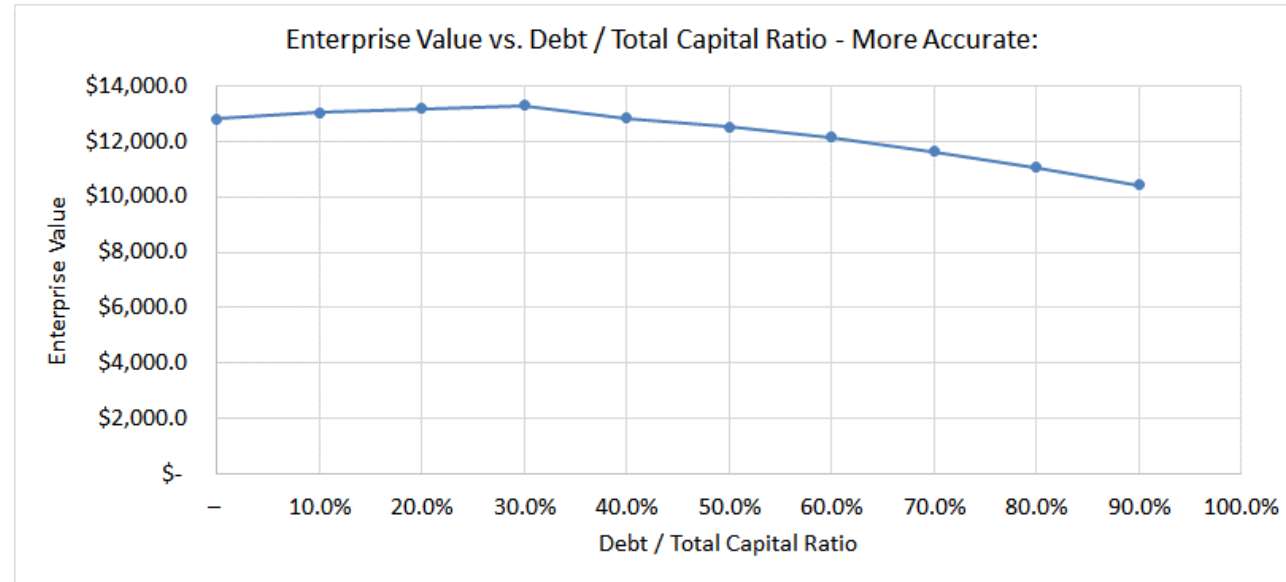


- **Also:** These items tend to stay in fairly narrow ranges over time, whereas revenue growth and operating margins can swing around wildly

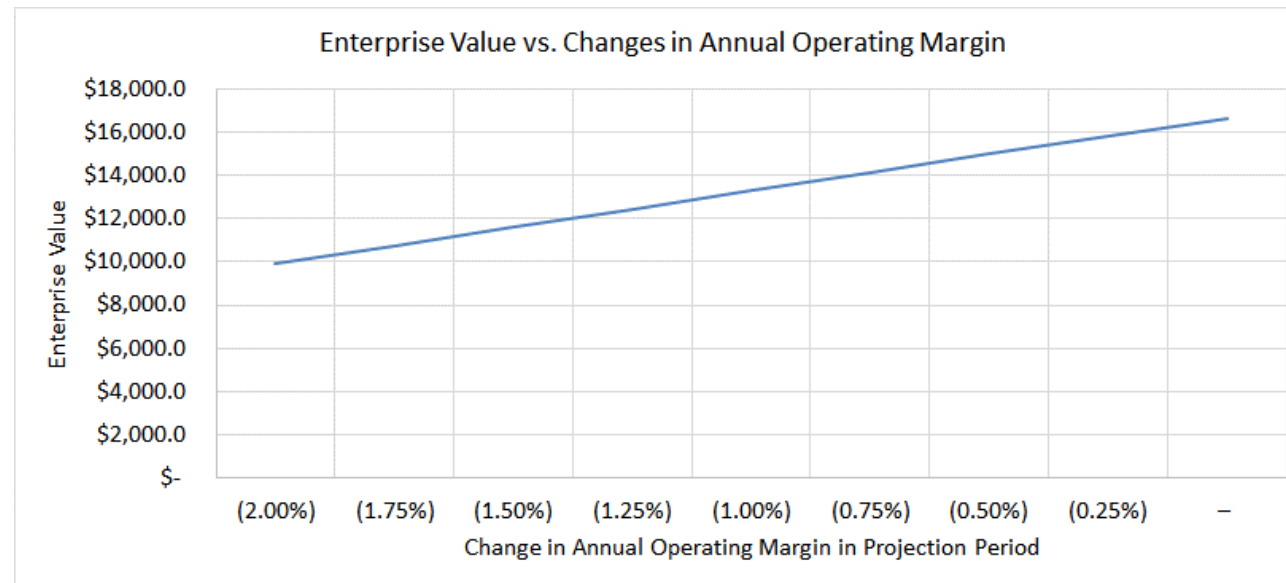
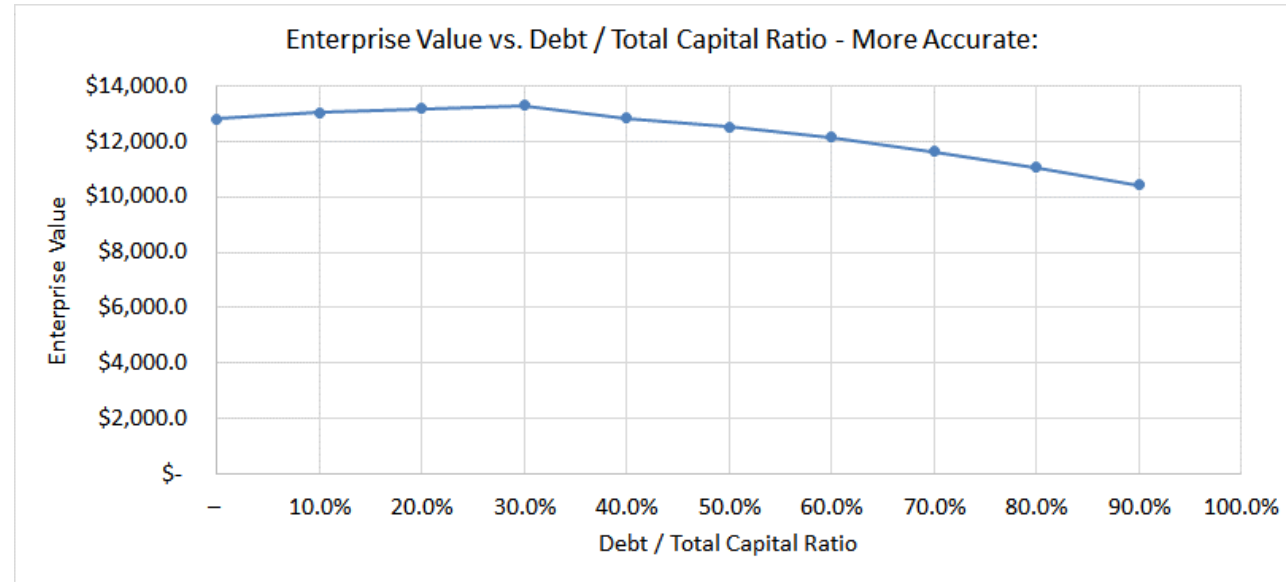


- **Excel:** Let's see how much each of these impacts Enterprise Value...

What Affects Enterprise Value?



What Affects Enterprise Value?



Recap and Summary

- **Financing Changes:** *In theory*, changes such as more/less debt or equity will not affect Enterprise Value



- **Operational Changes:** *In theory*, only operational changes such as higher/lower revenue growth and margins will affect Enterprise Value



- **REALITY:** Financing changes will still affect Enterprise Value, but by **FAR LESS** than operational changes



- **Examples:** You'll see small changes when going from a 10% debt / total capital ratio to 20%...



- **But:** MUCH bigger changes if revenue growth goes from 10% to 20%

