MOORE STEPHENS

Company valuations: Piecing it together

Corporate Finance

PRECISE. PROVEN. PERFORMANCE.

Company valuations: Piecing it together

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.

At Moore Stephens 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 place 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;
- Forecast 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;
- 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 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.

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

1. asset based method;
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 the underlying net assets, and where a relatively stable historic earnings pattern is demonstrated.

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

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.

"The outcome of our valuation process is a detailed report setting of the theoretical basis upon which our valuation is prepared."

Moore Stephens

Moore Stephens is a leading Irish owned provider of accountancy and advisory services for smart, commercially ambitious enterprises seeking the highest standards in client service and expertise. We are ranked in the top 10 Irish accountancy practices with 10 partners and over 100 staff. We have offices in Dublin and Cork and have grown steadily in the Irish marketplace since our foundation in 1970. We provide our clients with access to a range of core and specialist services including audit and tax compliance, business and personal tax planning, corporate finance, insolvency, corporate governance and forensic accounting. Our success stems from our industry focus, which enables us to provide an innovative and personal service to clients in niche markets. Specialist sectors include credit unions, healthcare, banking recovery and restructuring, agriculture and education, while maintaining our predominant foothold in the Irish SME sector. We recognise that Irish business will become increasingly export orientated in line with the national recovery plan. To address our clients' need for the highest quality international advice we have joined the Moore Stephens International Network.

Moore Stephens globally

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Contact information

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DPS18404 November 2018