Valuing private companies: the inputs

Equity Investments

1 A story: two firms making metal parts

- A listed firm: price every second, audited accounts
- Calder: founder owns it all and runs it
- No screen price, so the value must be built
- Step one: spot how Calder differs

IN THE LESSON

- Picture two firms that make metal parts.
- One is a big listed company.
- Its shares trade every second, an auditor signs its accounts, and a hired team runs it.
- The other is Calder Fabrication, a small private firm.
- Ruth Calder founded it, owns every share, runs the factory herself, and pays herself whatever she likes.
- Nobody can buy a slice of Calder on a screen.
- Now an analyst, Sam Okoye, is asked what Calder is worth.
- Sam cannot look up a price.
- Sam has to build the value from the inside, and the first step is to notice how this firm differs from a listed one.

2 Two kinds of difference

Company-specific

Younger and smaller →
Owner is the manager → Weaker information

Share-specific

Hard to sell → Transfer restricted → Control concentrated

IN THE LESSON

- Here is the first picture.
- The differences fall into two groups, and it helps to keep them apart.
- The top row is about the company itself.
- A private firm is often younger and smaller, so it has less depth of management.
- The owner is often the manager too, so profit is shaped by the owner's wishes, often to save tax rather than to look good.
- And the financial information is weaker, sometimes reviewed rather than audited.
- The bottom row is about the shares.
- They are hard to sell, because no active market exists.
- Transfers may be restricted by agreements.
- And ownership is concentrated, so who controls the firm matters a great deal.

3 Company-specific differences

- Earlier stage of life, smaller size
- Thin management; owner is also the manager
- Accounts less reliable, often unaudited
- No short-term market pressure
- Tax saving often beats showing profit

IN THE LESSON

- Let us go through the company side one item at a time.
- Early stage and small size mean the firm is riskier: losing one customer can hurt a great deal.
- Thin management means the business may depend on one person, the founder.
- The accounts may be reviewed but not audited, so the numbers deserve more checking.
- On the bright side, a private firm does not face the quarterly pressure of the stock market, so it can plan for the long run.
- But the owner often wants to pay as little tax as possible, so reported profit can be low on purpose.
- The analyst must undo that before using the numbers.

4 Share-specific differences

- Illiquid: no active market for the shares
- Transfer restricted by agreements
- Concentrated ownership, so control matters
- All of this raises the required return

IN THE LESSON

- Now the share side.
- Liquidity means how quickly you can sell at a fair price.
- A listed share sells in seconds.
- A share in Calder may take months to sell, if a buyer can be found at all.
- The shareholders agreement may also forbid sales to outsiders without the board's consent, which is a restriction on transfer.
- And because a few people own everything, whoever holds the majority can steer the business, set pay and decide on dividends.
- That is why control becomes an important issue.
- Investors dislike being stuck, so they ask for more return to hold such shares.
- A higher required return means a lower value.

5 Why a higher required return hurts

Chart: Value per $1 of cash flow vs Required return (%)

- 9%: 16.7
- 13%: 10.0

IN THE LESSON

- Let us see how much the required return matters.
- Look at the picture.
- The bottom axis is the required return, in per cent.
- The side axis is the value of a business that pays one dollar of cash next year and grows at three per cent for ever.
- The curve slopes down.
- At a required return of nine per cent, which suits a large listed company in our example, the value is sixteen point seven.
- Move right to thirteen per cent, which is more like a small private firm, and the value falls to ten.
- Same business, same cash, very different worth.
- That drop is why the differences on the last slides are not decoration.

6 Example 1: the same cash, two required returns

Cash flow and value in $ million

Cash flow next year	growing 3% for ever	**1.00**
Value at 9%	1.00 ÷ (9% − 3%)	**16.67**
Value at 13%	1.00 ÷ (13% − 3%)	**10.00**
Fall in value	(16.67 − 10.00) ÷ 16.67	**40%**

IN THE LESSON

- Here is the same idea in numbers.
- Take a business whose cash flow next year is one million, growing at three per cent a year for ever.
- Level One taught you the value of such a stream: next year's cash flow divided by the required return minus the growth rate.
- At nine per cent, one divided by six per cent gives sixteen point six seven million.
- At thirteen per cent, one divided by ten per cent gives ten million.
- The value fell by forty per cent, only because the return rose.
- And here is the trap for this outcome.
- Do not take a listed company's multiple or discount rate and apply it to a private firm without adjusting for size, liquidity and the quality of the information.

7 Matching Calder's features to their effect

Name the feature, then name the effect

Calder's feature	Where it bites
Founder runs the firm	Key person
Small, one factory	Size
Accounts not audited	Information
No market; family sale limits	Liquidity, transfer

IN THE LESSON

- Let us finish this part by matching Calder's features to what they do.
- The founder runs the firm, which is key person risk.
- One small factory means size risk, so a higher required return.
- Unaudited accounts mean the information is less trustworthy.
- No market means illiquidity.
- Family limits on sales mean the shares are hard to transfer.
- Every row pushes the required return up or calls for a discount.
- When you read a case, do this matching first.
- Name the feature, name the effect, and then decide where in the valuation it belongs: in the cash flows, in the discount rate, or in a discount applied later to the value of the shares.

8 Three people ask for a value

- Buyer: what should we offer?
- Tax office: what was it worth?
- Court: what damage was done?
- The reason decides the right answer

IN THE LESSON

- Suppose three people come to Sam in the same week.
- A buyer wants to know what to offer for Calder.
- The tax office wants to know what Calder was worth for a tax return.
- A court wants a number to settle a dispute between shareholders.
- Same firm, three questions.
- A listed share has a market price that anyone can look up, so nobody has to ask.
- For a private business, a value only exists because someone needs one, and the reason they need it shapes the right answer.
- So the first job is always to ask why the value is wanted.

9 Why a private business gets valued

Why someone asks for a value

Transaction → Compliance → Litigation

IN THE LESSON

- Here are the three families of reasons.
- First, transaction related.
- This is a deal: raising venture capital, preparing a listing, called an I P O, buying or selling a company, or reorganising one in bankruptcy.
- Second, compliance related.
- Rules demand a number, such as testing goodwill for impairment in the financial statements, or estate and gift tax.
- Third, litigation related: damages claims, disputes between shareholders, and divorce settlements.
- Read the boxes from left to right and ask which one your case belongs to.
- That one question decides which definition of value you should use and how much detail the work needs.

10 Calder in each box

- Transaction: venture capital, IPO, deals, bankruptcy
- Compliance: goodwill tests, estate and gift tax
- Litigation: damages, shareholder disputes, divorce
- Each audience has its own rule for value

IN THE LESSON

- Let us bring Calder into each box.
- Transaction: a venture investor considers putting money in, and needs to know what share to ask for.
- Or Ruth decides to sell, and a buyer needs an offer price.
- Compliance: Ruth dies, and her estate must report the value of her shares for tax, or a buyer must test the goodwill it booked for impairment.
- Litigation: two cousins who each own a quarter fall out, and a court must set a fair price for one cousin's stake.
- Notice that each case has an audience that will check the work, and each audience has its own rule about what counts as value.

11 Four definitions of value

Say which definition applies before you start

Definition of value	Typical use
Fair market value	Tax
Fair value	Reporting
Investment value	One buyer
Intrinsic value	Analyst

IN THE LESSON

- Now the four definitions of value.
- Fair market value is the price between a willing buyer and a willing seller, both well informed, neither forced.
- Tax authorities usually want this one.
- Fair value for financial reporting follows the accounting standards.
- Investment value is the worth to one particular buyer, including that buyer's own synergies and plans.
- And intrinsic value is the value an analyst computes from the fundamentals of the business, once the facts are known.
- They can all differ for the same company, so the analyst must say, at the start, which definition applies.
- The trap is using one buyer's investment value on a tax filing that calls for fair market value.

12 Example 2: one company, two correct values

$ million, a made-up illustration

Fair market value	any typical buyer	**15.0**
Dunmore's synergies	worth this to Dunmore only	**3.0**
Investment value	15.0 + 3.0	**18.0**
Value for the tax return	fair market value	**15.0**

IN THE LESSON

- Here is an illustration with round, made up numbers.
- Sam values Calder on a fair market basis, using the cash flows and risks any typical buyer would face, and gets fifteen million.
- Then a larger competitor, Dunmore, studies Calder.
- Dunmore can close one of its own factories after buying, and those savings are worth three million to Dunmore only.
- So Dunmore's investment value is eighteen million.
- If the estate's tax return used eighteen million, it would overstate the value by three million, and the estate would pay too much tax.
- The right number for the tax return is fifteen million.
- Same company, two correct numbers, each for its own purpose.

13 What the analyst should concentrate on

- Stage: start-up or mature business
- Are management's forecasts reliable?
- Size of the interest: control or minority
- Confirm the definition of value first

IN THE LESSON

- Beyond the purpose, there are three areas where the analyst should put effort.
- First, the stage of the business.
- A start-up with no profit needs a different method from a mature firm with steady cash flow.
- Second, the reliability of management's forecasts.
- In a private firm the forecast often comes from the owner, who may be hopeful, so test it against history and the industry.
- Third, the size of the interest being valued.
- A hundred per cent stake gives control, but a ten per cent stake gives almost no say, and its value per share can be very different.
- Keep these in mind, and always begin by confirming the definition of value.

14 Accounts written for the owner

- Owner's pay is set by the owner, not the market
- Rent paid to the owner's own company
- Personal bills run through the business
- Restate profit as a buyer would see it

IN THE LESSON

- Here is a story.
- Ruth pays herself eight hundred thousand a year to run Calder, although a hired manager of the same skill would cost three hundred thousand.
- She rents the factory from a company her family owns, at a price above the market.
- She also puts her car and her travel through the business.
- None of that is dishonest, but none of it will carry over to a new owner.
- A buyer will hire a manager at the market wage, and will pay the market rent.
- So before any multiple or discount rate is used, the analyst must restate profit as a buyer would really receive it.
- That restated figure is called normalised earnings.

15 Normalised earnings

Normalised = reported + pay and rent above market + personal and one-off costs − non-operating income

Reported earnings	Profit in the accounts
Pay and rent above market	Add back the excess
Personal and one-off costs	Costs that will not recur
Non-operating income	Value these separately
Normalised earnings	What a buyer expects

IN THE LESSON

- Here is the recipe as a formula.
- Start with reported earnings before tax.
- Add back any pay to the owner above the market wage, and any rent above the market rent, because a buyer would not bear those costs.
- Add back personal costs and one-off costs, since they will not recur.
- Subtract income from non-operating assets, such as a spare piece of land, because those assets are valued on their own and must not be counted twice.
- The adjustments can go both ways.
- If the owner underpays herself, or rents the factory below the market rate, you subtract instead.
- The aim is always the same: the earnings a typical buyer would expect to continue.

16 Example 3: Calder's first three adjustments

Earnings before tax, $ million

Reported income	per the accounts	**1.40**
Owner pay above market	0.80 − 0.30	**+0.50**
Rent above market	0.30 − 0.18	**+0.12**
Personal costs	car and travel	**+0.07**
Running total		**2.09**

IN THE LESSON

- Now the numbers for Calder.
- Reported income before tax is one point four million.
- Adjustment one: Ruth is paid zero point eight million, but the market wage is zero point three.
- The excess, zero point five, is added back.
- Adjustment two: Calder pays zero point three million rent to a family company, but the market rent is zero point one eight.
- The excess, zero point one two, is added back.
- Adjustment three: personal car and travel costs of zero point zero seven million were run through the business, and they are added back.
- The running total is one point four plus zero point five plus zero point one two plus zero point zero seven, which is two point zero nine million.

17 Example 4: one-offs, spare land and tax

Earnings before tax, $ million

Running total	from the last slide	**2.09**
One-off legal settlement	add back	**+0.20**
Rent on spare land	value the land separately	**−0.05**
Normalised, before tax		**2.24**
After tax at 25%	2.24 × 0.75	**1.68**

IN THE LESSON

- Continue with Calder.
- Adjustment four: last year Calder paid a legal settlement of zero point two million after a one-off contract dispute.
- It will not repeat, so add it back.
- Adjustment five: Calder owns a spare plot of land and earns zero point zero five million of rent from it.
- The land is not part of the operating business, so take the income out of earnings.
- The analyst will value the land on its own and add that value to the total.
- The result: two point zero nine plus zero point two minus zero point zero five is two point two four million of normalised earnings before tax.
- At a tax rate of twenty five per cent, that is one point six eight million after tax.

18 Reported against normalised

Earnings ($ million)

Reported	**1.40**
Normalised	**2.24**
After 25% tax	**1.68**

Calder's earnings, before and after normalising

IN THE LESSON

- Here are the key figures as bars.
- The left bar is what the accounts showed, one point four million before tax.
- The middle bar is normalised earnings before tax, two point two four million, sixty per cent higher.
- The right bar is the normalised figure after twenty five per cent tax, one point six eight million.
- An analyst who skipped the adjustments would have valued a business earning one point four when a buyer would really see two point two four.
- Notice that most of the gap came from the owner's pay and the rent, the two items that cases like to test.

19 Whose eyes? And what to trust

- Owner, financial buyer or strategic buyer?
- Strategic buyers may add synergies
- Management forecasts may be optimistic
- Surplus assets are valued separately

IN THE LESSON

- One more decision: whose eyes are you using?
- The existing owner may keep her habits.
- A financial buyer, such as a fund, wants only the earnings the business can produce on its own.
- A strategic buyer, such as a competitor, can add synergies like shared factories or combined purchasing, and so may pay more.
- Decide the perspective before you adjust, and say it in your report.
- Next, forecasts.
- In a private firm the forecast often comes from the owner, who knows the business but may be hopeful.
- Test it against past results and the industry.
- Last, non-operating assets like the spare land are valued separately and added in.

20 Mistakes so far

- 1. Missing excess owner pay or rent
- 2. Not cutting earnings for an underpaid owner
- 3. Synergies inside a tax-filing value
- 4. A listed rate pasted onto a private firm

IN THE LESSON

- Time for a short list of mistakes.
- One: missing the excess owner pay or rent.
- If Ruth takes too much, earnings are understated, and so is the value.
- Two: forgetting that the adjustments can go the other way, so an underpaid owner or a cheap rent should reduce earnings.
- Three: using a strategic buyer's investment value, with its synergies, for a tax filing, which calls for fair market value.
- Four: applying a listed company's discount rate straight to a private firm without adjusting it.
- Keep that last one in mind, because the discount rate is our next topic.

21 Adjusting the discount rate

- Size premium, though the evidence is debated
- Higher cost of debt raises the WACC
- Use a sustainable debt mix, not today's
- Optimistic forecasts: fix them directly
- Key-person premium is subjective

IN THE LESSON

- Cash flows are half of a valuation.
- The other half is the rate you discount them at.
- A listed company's rate is built from market data, and a private firm has none.
- So the analyst adjusts.
- First, size.
- Small firms have historically been riskier, so analysts often add a size premium, though the evidence is debated and it can overlap with other premiums.
- Second, the cost of debt.
- A private firm borrows on worse terms, so its debt costs more, which pushes up the W A C C.
- Third, leverage.
- Use a sustainable target mix of debt and equity, not whatever the owner happens to have today.
- Fourth, optimistic forecasts.
- Fifth, key person risk.

22 Example 5: the cost of debt and the debt mix

Cost of equity 15.6%, tax rate 25%

Calder's debt, after tax	8% × (1 − 0.25)	**6.0%**
Peers' debt, after tax	6% × (1 − 0.25)	**4.5%**
WACC, 70/30 target mix	0.7 × 15.6 + 0.3 × 6.0	**12.72%**
WACC with peers' debt	0.7 × 15.6 + 0.3 × 4.5	**12.27%**
WACC at today's 50/50 mix	0.5 × 15.6 + 0.5 × 6.0	**10.80%**

IN THE LESSON

- Let us see the debt effect in numbers.
- Calder's bank charges eight per cent, but listed peers borrow at six.
- After twenty five per cent tax, Calder's cost of debt is six per cent.
- Suppose the cost of equity is fifteen point six per cent; the last section shows where that comes from.
- The sustainable mix is seventy per cent equity and thirty per cent debt.
- The W A C C is zero point seven times fifteen point six plus zero point three times six, which is twelve point seven two per cent.
- Pasting in the peers' cheaper debt would give twelve point two seven.
- Using today's fifty fifty mix would give ten point eight, which looks lovely but is not sustainable.

23 Whose risk does the rate carry?

Discount rate (%)

Buyer's own	**9.00%**
Calder, peer debt	**12.27%**
Calder, real debt	**12.72%**

Use the target's risk, not the buyer's

IN THE LESSON

- Look at three bars.
- The left one, nine per cent, is the rate Dunmore, the buyer, uses for its own projects.
- The middle one, twelve point two seven, is Calder's W A C C if you borrow the peers' cheap debt.
- The right one, twelve point seven two, is Calder's with its real cost of debt.
- The lesson for an acquisition is that the rate must reflect the risk of the target, not the buyer.
- Dunmore is large and safe, but Calder's cash flows are small and exposed.
- Discounting Calder at nine per cent would flatter it badly.
- Each bar tells you whose risk the rate is carrying.

24 Example 6: fix the forecast, not the rate

Growth 3%, WACC 12.72%, value in $ million

Realistic forecast 1.80	1.80 ÷ 9.72%	**18.52**
Hopeful forecast 2.00	2.00 ÷ 9.72%	**20.58**
Hopeful, rate plus 3 points	2.00 ÷ 12.72%	**15.72**

A rate premium is a blunt tool: fix the forecast

IN THE LESSON

- Now the optimistic forecast.
- Management says the cash flow next year will be two million.
- Sam's check against history says one point eight.
- Kieran, a junior analyst, suggests keeping two million and adding three points to the discount rate instead.
- Test it, with growth of three per cent.
- Realistic: one point eight divided by twelve point seven two minus three, which is nine point seven two per cent, gives eighteen point five two million.
- Keeping two million at the same rate gives twenty point five eight, too high.
- Adding three points to the rate gives fifteen point seven two, too low, because a rate premium cuts value far more than the forecast error did.
- The clean fix is to correct the forecast.

25 Specific premiums and double counting

- Key-person and customer premiums are subjective
- Risk already in the cash flows? No premium
- Size premium and marketability discount can overlap
- Acquisition: use the target's risk

IN THE LESSON

- Last, the company-specific premiums.
- If Calder depends on its founder, or one customer buys half of its output, an analyst may add a premium.
- These are subjective, so write down the reason and the size.
- Then comes the big discipline: count each risk once.
- If the forecast already shows a lost customer, a premium on top counts the risk twice.
- A size premium and a later discount for lack of marketability can also overlap, because small firms are often illiquid as well.
- The trap is counting the same risk twice.
- And remember, in an acquisition the discount rate belongs to the target's risk, never the buyer's.

26 Three recipes for the required return

- CAPM needs a beta; Calder has no share price
- Borrow a beta from guideline public companies
- Expanded CAPM adds premiums for what beta misses
- No usable beta? Build the return up

IN THE LESSON

- Now the last piece: the return that shareholders require on the equity itself.
- You may remember the C A P M from Level One.
- The required return equals the risk-free rate plus beta times the equity risk premium.
- The difficulty is beta.
- Beta is measured from share prices, and Calder has none.
- There are three ways forward.
- One, borrow a beta from listed guideline companies and use the plain C A P M.
- Two, borrow the beta, then add premiums for what it misses: the expanded C A P M.
- Three, when no suitable beta exists, skip beta entirely and use the build-up approach.
- Let us take each in turn.

27 The CAPM and the expanded CAPM

CAPM: r = rf + β × ERP
Expanded: r = rf + β × ERP + size + specific

Risk-free rate	Return on a safe asset
Guideline beta	Borrowed from listed peers
Equity risk premium	Market's extra return
Size premium	Extra for small firms
Company-specific premium	Risk unique to this firm

IN THE LESSON

- The first formula covers the C A P M and its expansion.
- Plain C A P M is the risk-free rate plus beta times the equity risk premium.
- The beta is taken from guideline public companies.
- It can miss two things: the extra risk of being small, and risk special to this company.
- So the expanded C A P M adds a size premium and a company-specific premium to the plain answer.
- If the guideline beta already captures the risk of the industry, do not add an industry premium.
- An industry premium appears only when the beta does not reflect the industry.
- The trap here is leaving the size premium out of the expanded model.

28 The build-up approach

Build-up: r = rf + ERP + size + industry + specific

Risk-free rate	Return on a safe asset
Equity risk premium	Implicit beta of one
Size premium	Extra for small firms
Industry premium	If the industry differs
Company-specific premium	Risk unique to this firm

IN THE LESSON

- The build-up approach starts with the risk-free rate and adds layers.
- Add the equity risk premium on its own, with no beta.
- This works because it assumes an implicit beta of exactly one: the firm is as risky as the market.
- Then add a size premium.
- Add an industry premium if the industry is riskier or safer than the market.
- And add a company-specific premium.
- The biggest slip is multiplying the equity risk premium by a beta in the build-up method.
- There is no beta in this recipe.
- You build the return one layer at a time, and because every premium involves judgement, you should document where each one came from.

29 Example 7: three answers for Calder

rf 4%, ERP 5.5%, beta 1.2, size 3%, industry 1%, specific 2%

Plain CAPM	4.0 + 1.2 × 5.5	**10.6%**
Expanded CAPM	10.6 + 3.0 + 2.0	**15.6%**
Build-up	4.0 + 5.5 + 3.0 + 1.0 + 2.0	**15.5%**
Gap, expanded v build-up	15.6 − 15.5	**0.1 points**

IN THE LESSON

- Let us compute all three for Calder.
- The risk-free rate is four per cent.
- The equity risk premium is five point five.
- The guideline beta is one point two.
- The size premium is three, the industry premium one, and the company-specific premium two.
- Plain C A P M: four plus one point two times five point five, which is six point six, gives ten point six per cent.
- Expanded: add size three and specific two, giving fifteen point six.
- The beta comes from the same industry, so no industry premium.
- Build-up: four plus five point five plus three plus one plus two gives fifteen point five.
- The expanded and build-up answers agree within a tenth of a point.

30 Three routes, side by side

Required return (%)

Plain CAPM	**10.6%**
Expanded CAPM	**15.6%**
Build-up	**15.5%**

Rate for Calder's equity under each method

IN THE LESSON

- Here they are side by side.
- The plain C A P M bar is ten point six per cent.
- It has only the risk-free rate and the beta scaled premium.
- The expanded bar, fifteen point six, adds size and specific risk.
- The build-up bar, fifteen point five, reaches nearly the same place by a different route.
- An analyst who stopped at the plain C A P M would use a rate five points too low, and would overvalue Calder.
- Earlier we used the fifteen point six figure as the cost of equity in the W A C C, so the numbers in this lesson tie together.

31 Traps in the required return models

- 1. Multiplying the ERP by a beta in the build-up
- 2. No size premium in the expanded CAPM
- 3. Industry premium on top of an industry beta
- 4. Treating judgement premiums as facts

IN THE LESSON

- Four traps to remember.
- One: multiplying the equity risk premium by a beta in the build-up method.
- The build-up has an implicit beta of one, so the premium goes in whole.
- Two: leaving the size premium out of the expanded C A P M, and so ending up with a rate that is far too low.
- Three: adding an industry premium on top of a beta taken from the same industry, which counts the industry risk twice.
- Four: treating the premiums as facts.
- The size premium, the industry premium and the company-specific premium all involve judgement, so state your reasons, and do not stack premiums without thinking.

32 Recap: the pieces of the inputs

Normalised = reported ± adjustments
Expanded: r = rf + β × ERP + size + specific
Build-up: r = rf + ERP + size + industry + specific

Normalised earnings	Earnings a buyer expects
WACC at target mix	Own debt, target mix
Expanded CAPM	Has beta, size, specific
Build-up	No beta; implicit beta one

IN THE LESSON

- Let us pull it together.
- Normalised earnings are reported earnings, adjusted for pay and rent above market, personal and one-off costs, and non-operating income.
- The W A C C for a private firm uses its own cost of debt and a sustainable target mix, and it reflects the target's risk.
- The expanded C A P M is the risk-free rate plus beta times the equity risk premium, plus the size premium and the company-specific premium.
- The build-up approach is the risk-free rate plus the equity risk premium, size, industry and specific premiums, with no beta.
- And always begin by asking why the value is wanted and which definition of value applies.

33 Try three quick questions

1. Reported income 1.00m; owner paid 0.60m, market wage 0.25m. Normalised income?
   Answer: 1.00 + 0.35 = 1.35 million.
2. Build-up: rf 3%, ERP 5%, size 2.5%, specific 1.5%. Required return?
   Answer: 3 + 5 + 2.5 + 1.5 = 12%, no beta.
3. Which definition of value fits an estate tax filing?
   Answer: Fair market value, not a buyer's investment value.

IN THE LESSON

- Now try three quick questions yourself.
- Pause after each one.
- Question one.
- A private firm reports income of one million.
- The owner is paid six hundred thousand, and the market wage is two hundred and fifty thousand.
- What is normalised income, ignoring other items?
- Add the excess, three hundred and fifty thousand, to get one point three five million.
- Question two.
- Build-up approach: risk-free rate three per cent, equity risk premium five, size premium two point five, specific premium one point five.
- What is the required return?
- Add them all: twelve per cent, with no beta.
- Question three.
- Which definition of value fits an estate tax filing?
- Fair market value, not a buyer's investment value.