TP 4: Equity Valuation

Exercise 1:

PG paid an annual dividend of 1.61 Euros at the end of this year. You expect PG to increase its dividends by 7.6% per year for the next 3 years and thereafter by 3.3% per year. If the appropriate equity cost of capital for PG is 8.3% per year, use the dividend-discount model to estimate its value per share at the end of this year.

Moreover, would you buy the shares if their price on the market were 50 Euros?

Exercise 2:

The quoted stock price of a company is 150 Euros. Your own analyses are based on the following set of information:

- The dividend forecasts for the next 3 years are 10 Euros, 25 Euros and 15 Euros, respectively.
- The long-term growth rate is expected to be 4%
- The expected rate of return is 15%

Given that, would you buy, sell, or hold the stock?

Exercise 3:

Company A expects to have earnings this coming year of 3.18 Dollars per share.

Each year retained earnings will be invested in new projects with an expected return of 25.76% per year. Any earnings that are not retained will be paid out as dividends.

Company A plans not to distribute earnings as dividends for the next 2 years. The firm will distribute 48% of its earnings for the following 2 years. It will retain 22% of its earnings from that point onward.

Assume Company A's share count remains constant, and all earnings growth comes from the investment of retained earnings. If the equity cost of capital is 10.4%, what price would you estimate for Company A's stock?

Exercise 4:

You are asked to evaluate a company; it is totally financed by equity. A financial analyst sends you the following table and he informs you that the expected return is 10%. This company has 120,000 outstanding shares. In year 0, revenues were 85,000 euros. The net working capital is 5% of total revenues.

Year	1	2	3
Revenues	90,000	100,000	120,000
Earnings Before taxes	20,000	22,500	25,000
Earnings after taxes	13,400	14,850	16,500
Capex	8,000	10,000	12,000
Depreciation & Amortization	4,000	5,000	6,500

1. Compute the FCFs for each year.
2. Compute the enterprise value and the value per share of this company. The analyst suggested that the expected growth rate after the third year will be 5% and the company keeps its actual dividend policy (i.e. it distributes 40% of EAT).

Exercise 5:

Suppose that Company A had sales of 525 million Euros, EBITDA of 55.1 million, excess cash of 99 million, 6.2 million of debt, and 22 million shares outstanding. Use the multiple approach to estimate Company A's value based on the following data from comparable firms

	$\frac{P}{E}$	$\frac{\text{Price}}{\text{Book}}$	$\frac{\text{Enterprise Value}}{\text{Sales}}$	$\frac{\text{Enterprise Value}}{\text{EBITDA}}$
Average	15.01	2.84	1.06	8.49

1. Using the average enterprise value to sales multiple, estimate Company A's share price.
2. Using the average enterprise value to EBITDA multiple in the table above, estimate Company A's share price.