# DCF Valuation of Rollins Inc. (ROL) as a Middle-Market Add-On Target

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## Introduction

Private equity sponsors often pursue roll-up strategies, acquiring add-on targets in fragmented industries like pest control. To assist in determining whether an acquisition is a good investment, financial modeling—specifically the Discounted Cash Flow (DCF) method—becomes crucial in estimating a target company's intrinsic value. This paper applies a DCF model to Rollins Inc. (ROL), a company with stable recurring revenue, to assess its suitability as an acquisition target.

## Problem Statement

For investment bankers advising private equity firms, it's essential to quickly and accurately determine the fair value of potential targets. A well-structured DCF model provides a reliable and data-driven valuation that guides negotiations and enhances deal outcomes. The core challenge here is to develop a comprehensive model using actual financial data, project future cash flows, and calculate the company's intrinsic value through a discounted cash flow approach.

## Methodology

The DCF model evaluates the value of a company by projecting its Free Cash Flows to the Firm (FCFF) and discounting them using a Weighted Average Cost of Capital (WACC). Key assumptions, including growth rates and margins, are used to project future performance, with a terminal value representing the company's continued operations after the forecast period.

We begin by computing the FCFF for the next five years and then estimate a terminal value based on a perpetuity growth model. Finally, we discount both the FCFF and the terminal value to arrive at the company's Enterprise Value (EV).

## Assumptions

To project future cash flows and determine a reliable valuation, we set the following assumptions based on Rollins' financial history and industry norms:

| Assumption | Value |
|---|---|
| Revenue Growth Rate | 6% annually |
| EBITDA Margin | 22% |
| Tax Rate | 21% |
| CapEx as % of Revenue | 3% |
| Change in Working Capital | 1% of Revenue |
| WACC | 8.5% |
| Terminal Growth Rate | 2.5% |

Table 1: Key Financial Assumptions

## DCF Valuation Framework

The core of this valuation is based on projecting the Free Cash Flow to the Firm (FCFF) and the terminal value.

### Free Cash Flow to Firm (FCFF)

FCFF represents the cash that is available to all capital providers (debt and equity). We calculate it as:

$$\text{FCFF} = \text{EBIT} \times (1 - \text{Tax Rate}) - \text{CapEx} - \Delta\text{Working Capital}$$

where EBIT is Earnings Before Interest and Taxes, Tax Rate is the corporate tax rate, CapEx is capital expenditures, and $\Delta$ Working Capital is the change in net working capital.

### Terminal Value

The terminal value estimates the value of the business beyond the projection period, assuming perpetual growth at a constant rate $g$. We use the Gordon Growth Model:

$$\text{Terminal Value} = \frac{\text{FCFF}_{\text{Terminal Year}} \times (1 + g)}{\text{WACC} - g}$$

Here, $g$ is the terminal growth rate, typically aligned with long-term economic growth or inflation rates.

### Enterprise Value (EV)

The Enterprise Value is the sum of the discounted future FCFF over the projection period and the discounted terminal value:

$$\text{EV} = \sum_{t=1}^{5} \frac{\text{FCFF}_t}{(1 + \text{WACC})^t} + \frac{\text{Terminal Value}}{(1 + \text{WACC})^5}$$

This formula accounts for the time value of money, where future cash flows are worth less today, thus the discounting process is applied.

## Results

Using the assumptions and methodology above, the projections for Rollins Inc. over the next five years are as follows:

| Year | Revenue (M) | EBITDA (M) | FCFF (M) | Discounted FCFF (M) |
|---|---|---|---|---|
| 2025 | 3,592.03 | 790.25 | 409.67 | 377.58 |
| 2026 | 3,807.55 | 837.66 | 434.25 | 368.88 |
| 2027 | 4,036.01 | 887.92 | 460.31 | 360.38 |
| 2028 | 4,278.17 | 941.20 | 487.92 | 352.07 |
| 2029 | 4,534.86 | 997.67 | 517.20 | 343.96 |

Table 2: Free Cash Flow Forecast and Discounted Values

The projected **Enterprise Value (EV)**, after discounting future cash flows and the terminal value, is **$7.68 billion**.

## Sensitivity Analysis

The sensitivity analysis evaluates how changes in key assumptions, such as the Weighted Average Cost of Capital (WACC) and the terminal growth rate, impact the enterprise value. The analysis shows a range of **$6.2 billion** to **$10.1 billion** for the EV, depending on the variation in these assumptions. This demonstrates the importance of considering different scenarios when making investment decisions.

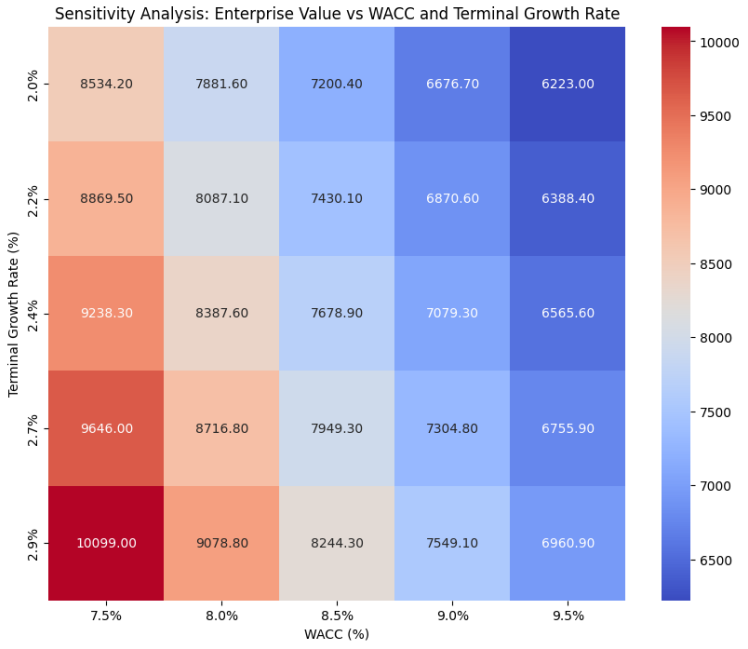


Figure 1: Sensitivity Analysis: Enterprise Value vs WACC and Terminal Growth Rate

## Conclusion

In this analysis, the intrinsic value of Rollins Inc. was calculated using a DCF model, providing a detailed financial picture of the company's potential worth. Key findings include:

- **Revenue Growth**: Rollins Inc. is projected to grow revenue at a steady **6%** annually, which supports a gradual increase in EBITDA and Free Cash Flow (FCF).
- **Enterprise Value**: The estimated **EV** of **$7.68 billion** represents Rollins' total worth, accounting for both short-term projections and long-term growth.
- **Equity Value**: After adjusting for **net debt**, the **Equity Value** of Rollins Inc. is **$7.72 billion**.
- **Sensitivity to Assumptions**: The analysis highlights the sensitivity of the valuation to changes in WACC and the terminal growth rate, with a range of **$6.2 billion** to **$10.1 billion** for the EV.

This analysis helps potential investors and acquirers make informed decisions by providing a robust valuation that incorporates realistic growth assumptions and accounts for market sensitivities.