

Explain the CAGR

CAGR stands for Compound Annual Growth Rate. It is a financial metric that measures annual rate of return or growth of an investment finance on material over a specific period of time. The term CAGR values takes into account the compounding effect of growth from one period to the year 1.

The formula to calculate CAGR:

$$CAGR = \left(\text{End value} / \text{Beginning value} \right)^{1/n}$$

Where:

- End value is the final value at the even time or metric
- Beginning value is the initial value at the investment or metric
- Number of year in the time period and which the growth is measured.

For example:

If a company's revenue grows from £1,50,000 over 3 years the CAGR would be

$$CAGR = \left(\text{£1,50,000} / \text{£1,00,000} \right)^{1/3} - 1 = 14.5\%$$

This means the company's revenue grow at an average rate 14.5% per year over the 3-year period

CAGR is useful for

1. Evaluating investment performance

2. Comparing growth rate between companies or industries

3. Setting growth target or benchmark

4. Analysing historical growth trend

Remember CAGR is a smoothed rate of growth so it may not reflect the initial year's year fluctuations.