

## **Enterprise / Equity Value Questions and Answers – Advanced (3 Questions)**

### **65. Are there any problems with the EV formula you just gave me?**

Yes – it's too simple. There are lots of other things you need to add into the formula with real companies:

1. Net Operating Losses: should be valued and arguably added in, similar to cash
2. Long-Term Investments: These should be counted, similar to cash
3. Equity Investments: Any investments in other companies should also be added in, similar to cash (though they might be discounted)
4. Capital Leases: Like debt, these have interest payments, so they should be added in like debt
5. (Some) Operating Leases: Sometimes you need to convert operating leases to capital leases and add them as well
6. Unfunded Pension Obligations: Sometimes these are counted as debt as well

So a more “correct” formula would be  $EV = \text{Equity Value} - \text{Cash} + \text{Debt} + \text{Preferred Stock} + \text{Noncontrolling Interest} - \text{NOLs} - \text{Longterm and Equity Investments} + \text{Capital Leases} + \text{Unfunded Pension Obligations}$

In interviews, usually is good enough to say  $EV = \text{Equity Value} - \text{Cash} + \text{Debt} + \text{Preferred Stock} + \text{Noncontrolling Interest}$

More advanced interviews will bother you about this

### **66. Should you use the book value or market value of each item when calculating EV?**

Technically, you should use market value for everything. In practice, however, you usually use market value only for the equity value portion because it's almost impossible to establish market values for the rest of the items in the formula – so you just take the numbers from the company's BS

### **67. What percentage dilution in Equity Value is “too high?”**

There's no strict rule here but most bankers would say anything over 10% is odd. If your basic Equity Value is \$100 million and the diluted equity value is \$115 million, you might want to check your calculations. It's not necessarily wrong, but over 10% dilution is unusual for most companies