**Discounted Cash Flow Questions and Answers – Basic (32 questions)**

1. **Walk me through a DCF**

A DCF values a company base d on the present value of its cash flows and the present value of its terminal value

First, you project out a company’s financials using assumptions for revenue growth, expenses and working capital. Then you get down to free cash flow for each year, which you then sum up and discount to a NPV, based on your discount rate – usually the WACC

Once you have the present value of the cash flows, you determine the company’s terminal value, using either the multiples method or the Gordon growth method, and then also discount that back to its NPV using WACC

Finally, you add the two together to determine the company’s enterprise value

1. **Walk me through how you get from revenue to free cash flow in the projections**

Subtract COFS and operating expenses to get to operating income (EBIT). Then multiply by (1 – tax rate T), add back depreciation and other non-cash charges, and subtract capex and the change in working capital

Note: This gets you to Unlevered Free Cash Flow since you went off EBIT rather than EBT. You should confirm that this is what the interviewer is asking for

1. **What’s an alternate way to calculate free cash flow aside from taking net income, adding back depreciation, and subtracting changes in operating assets / liabilities and capex?**

Take cash flow from operations and subtract capex and mandatory debt repayments. That gets you to levered cash flow. To get to unlevered cash flow, you then need to add back the tax-adjusted interest expense and subtract the tax-adjusted interest income

1. **Why do you use 5 or 10 years for DCF projections?**

That’s usually about as far as you can reasonably predict into the future. Less than 5 years would be too short to be useful, and over 10 years is too difficult to predict for most companies

1. **What do you usually use for the discount rate?**

Normally you use WACC though you might also use cost of equity depending on how the DCF is set up