

# BASIC PRINCIPLES OF FINANCIAL VALUATION DISCOUNTING

## DCF Practical Example

James P. Weston

Professor of Finance

The Jones School, Rice University

# DCF PRACTICAL EXAMPLE

A water well in the desert. How much is it worth to sell or acquire?

If the well is dry?

Connected to an active source of water?

# DCF PRACTICAL EXAMPLE: WATER WELL

How much water is there?

Infinite

How much does it produce?

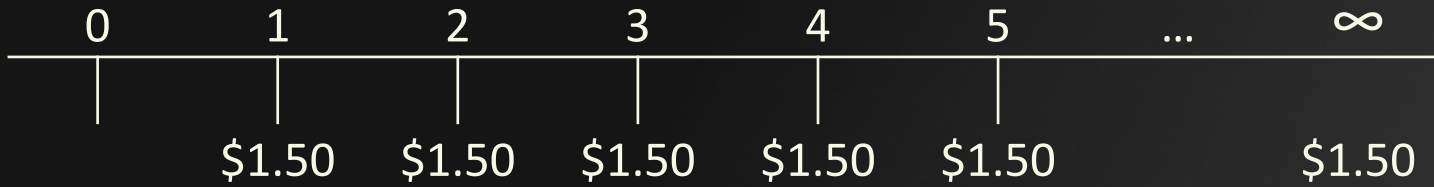
1 gallon/day

How much cash flow?

Net \$1.50/day

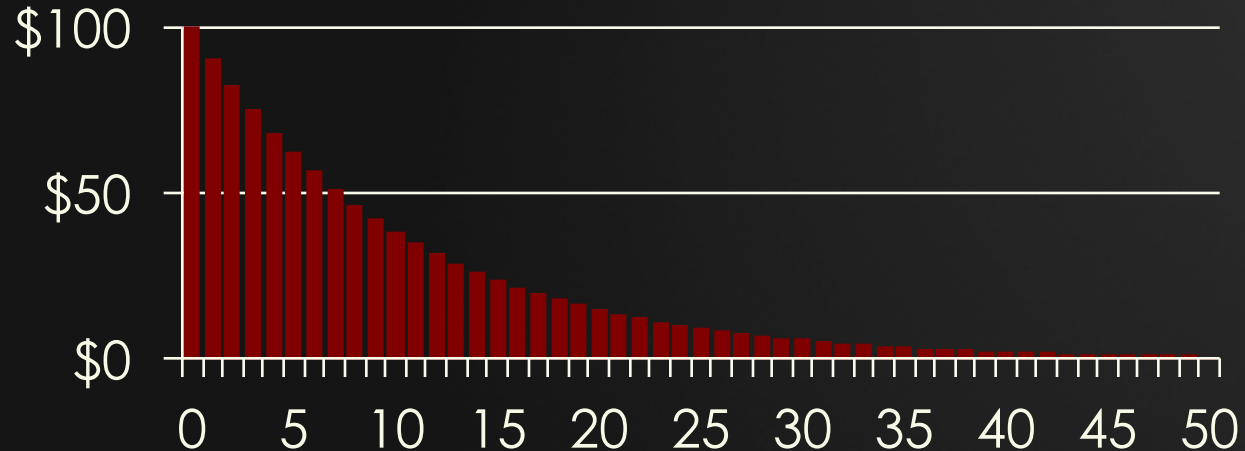
Can we put a realistic price on this asset?

# DCF PRACTICAL EXAMPLE: WATER WELL



Problem: Is it worth infinity?

Remember:



# DCF PRACTICAL EXAMPLE: WATER WELL

Discount rate: 15%

Build a spreadsheet model

- ▶ Step 1: What are the cash flows
- ▶ Step 2: What are they worth today?
- ▶ Step 3: Add up the present values