

Methods to Calculate the Terminal Value (TV)

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Description

Example

1

Gordon Growth Method

- The more common, preferred method of calculating terminal values
- Assumes FCF is generated at a constant rate into perpetuity after the terminal year (n): *"Terminal Growth Rate (TGR)"*
- $TV = (FCF_n \times (1 + TGR)) / (WACC - TGR)$

- Terminal Year FCF: \$10M
- Terminal Growth Rate: 2% p/a
- WACC: 8%

$$TV = (\$10M \times 1.02) / (0.08 - 0.02) = \$170M$$

→ Accounts for the value of all Future FCF into perpetuity after the Terminal Year

2

Exit Multiple Method

- Assumes the business is sold at the terminal year for a multiple of a financial metric, based on comparable trading (or transaction) multiples
- $TV = \text{Financial Metric} \times \text{Valuation Multiple}$
- We will be using the Gordon Growth Method from hereon, given it is preferred

- Terminal Year: FY2025F
- Terminal Year EBITDA: \$20M
- Exit EBITDA Multiple: 8.0x

$$TV = (\$20M \times 8.0x) = \$160M$$

→ Accounts for the value of all Future FCF into perpetuity after the Terminal Year