Why doesn’t Warren Buffett like EBITDA?

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- While VC and PE firms often rely on EBITDA multiples for valuation metrics, Warren Buffett is known for actively disliking this approach
- Its worth considering why…

Why doesn’t Warren Buffett like EBITDA?

- EBITDA
- Earnings before Interest Tax Depreciation and Amortisation
- The exclusion of Depreciation and Amortisation - non cash items - measure the expenditure on Capex

Why doesn't Warren Buffett like EBITDA?

- This means that EBITDA may be useful was a measure of profitability
- It takes no account of the cost of debt capital (interest) or its tax effects (interest costs shelter profits from tax)

Why doesn't Warren Buffett like EBITDA?

- So what does Warren Buffet think?

Why doesn't Warren Buffett like EBITDA?

- "Does management think the tooth fairy pays for capital expenditures?"
- Warren Buffett

Why doesn't Warren Buffett like EBITDA?

- While EBITDA makes comparable comparison of companies easier as it strips out financing effects and accounting policies
- In practice the composition of the elements of EBITDA may vary from one period to another as companies make adjustments
- Buffett does not accept that it is a true representation of a company's financial performance

Why doesn’t Warren Buffett like EBITDA?

- Buffett’s argument is that D&A reduce the value of a firms total assets through the reduction of capital and financial assets
- While not a cash outflow, this does represent what is happening within the business as assets are used and age

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- The effect is therefore to overstate the company's earnings and therefore its value.

Why doesn't Warren Buffett like EBITDA?

- As the EBITDA metric is frequently used, you should be aware of this criticism and the position taken by one of the most influential investors

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