What Does Intrinsic Valuation tell us about Fair Value?

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- The concept of "Fair Value" is highly subjective, but its an important question in valuation

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- In essence, when making an investment, an investor wants to know whether he is paying too much for the investment?
- Will he make a satisfactory return?
- This is more likely if the price is undervaluing the asset or if it is at "Fair Value" as opposed to over valuing it

What Does Intrinsic Valuation tell us about Fair Value?

- A Fairly Valued asset is one where its true value is equal to its market value
- The “true” value is seldom known but investors use valuation methods to attempt to calculate it

What Does Intrinsic Valuation tell us about Fair Value?

- This means that using Intrinsic or Absolute methods such as DCF or DDM enable investors to calculate a value - based on their assumptions - which they can compare to the market value

What Does Intrinsic Valuation tell us about Fair Value?

- This consequently enables them to form a view as to whether the asset is fairly valued or not
- As we have seen that viewpoint is highly subjective and dependent on the assumptions in the calculation

What Does Intrinsic Valuation tell us about Fair Value?

- In the event that there is a significant difference between intrinsic value and market value, there is an opportunity for arbitrage
- If the stock is over valued, it can be sold short
- If it is undervalued, it can be bought in the market in expectation of a positive investment return in the future.

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