What are Equity Valuation Methods?

Worksheet

Equity valuation methods are techniques like discounted cash flow (DCF), P/E multiples, and comparable analysis used to determine a company's stock value and investment attractiveness.

Questions

1. Which method projects future cash flows and discounts them to present value?

A) P/E ratio
B) Discounted cash flow (DCF)
C) Asset-based valuation
D) Dividend yield

2. A stock with P/E 12 trades below an industry average of 16. This suggests...

A) the stock is overvalued
B) the stock is undervalued
C) earnings are declining
D) no clear conclusion

3. Book value per share = Total equity / Number of shares. This is part of which method?

A) DCF
B) Relative valuation
C) Asset-based valuation
D) Dividend discount

4. Why might two valuation methods give different results for the same stock?

A) One is always wrong
B) Each uses different assumptions and inputs
C) The market sets the price
D) Calculators have errors

5. ABC Corp has projected cash flows of $50M annually for 5 years. Using a 10% discount rate, find the DCF value.

6. Stock X trades at 80, with earnings of5 per share. Industry average P/E is 18. Is it undervalued?

7. Company has assets worth 200M, liabilities50M, with 10M shares outstanding. What is book value per share?

8. Define: What are equity valuation methods?

9. Define: Name three main equity valuation approaches.

10. Define: What is P/E ratio in valuation?

Answer Key

1. B) Discounted cash flow (DCF) — DCF is the only method that explicitly projects and discounts future cash flows.

2. B) the stock is undervalued — Lower P/E than peers indicates the stock may be undervalued relative to earnings.

3. C) Asset-based valuation — Asset-based valuation directly uses the company's equity (assets minus liabilities).

4. B) Each uses different assumptions and inputs — Different methods focus on different financial aspects and use different assumptions.

5. DCF = $50/(1.1) + 50/(1.1)^2 + 50/(1.1)^3 + 50/(1.1)^4 + 50/(1.1)^5 = 45.45 + 41.32 + 37.57 + 34.15 + 31.05$ DCF Value = $189.54M

6. Current P/E = 80 /5 = 16 Industry average = 18 Stock P/E (16) < Industry average (18) → Stock is undervalued

7. Equity = Assets − Liabilities = 200M −50M = 150M Book value per share =150M / 10M = $15 per share

8. Techniques to determine a company's stock intrinsic value using financial analysis.

9. DCF (discounted cash flow), relative valuation (P/E ratios), and asset-based valuation.

10. Stock price divided by earnings per share — compares valuation to peers.