

VALUATION

The Comparables Approach

The basic idea of the Comparable Company Analysis (Comps) is that in a reasonable efficient capital market the value of a share bears some similarities to the values of equities belonging to a similar category.

The Comps approach can be applied as a quick, first approximation for the value of a firm or its equity. But it can also be applied as a cross-check to confirm assumptions made in a Discounted Cash Flow valuation approach. Comps are also known as trading multiples or peer group analysis.

Applying Comps is a relative valuation method: Thereby the value of a business is compared to other similar publicly listed businesses (the peer group) by using trading multiples such as Price to Earnings (P/E), Enterprise Value to EBITDA (EV/EBITDA) or other ratios. Hence, a valuation via Comps reflects what a business is worth at this very moment. Because of this and as Comps are easy to get and process, they are widely used.

Comps can be distinguished into two categories: Equity value-based multiples and enterprise value-based multiples.

Equity value-based multiples, whereby most common are P/E and Price to Book Value (P/BV),

directly point towards the value of the equity of a firm. They are especially relevant where investors acquire minority positions in companies. This set of multiples does explicitly not take into account the different capital structures between the target firm to be valued and its peers.

Enterprise value-based multiples, whereby most common are EV/EBITDA or enterprise value to EBIT (EV/EBIT) or to Sales (EV/S) value an entire company's balance sheet, including both, its equity and all financial liabilities. To get the firm's equity value, one needs to deduct from the enterprise value the firm's net debt, defined as all interest bearing liabilities minus cash and marketable securities.

The selection of the appropriate peer group is most relevant in applying the Comps valuation approach: A peer group is a set of companies which are sufficiently comparable to the company being assessed whereby selection parameters are, among others: same industry, similar characteristics in regards to size, geographic focus, earnings growth or return on investment. – As in reality there are no two businesses alike, adjustments will have to be made in the Comps applied to harmonize the data into a more comparable format. To make such adjustments, however, one would need to have a fair understanding of the industry and the specific strengths and weaknesses of the members of the selected peers.

