Discounted Cash Flow

Implied Enterprise Value to Implied Equity Value

In a DCF, forecasted cash flows and terminal value are discounted to present value, then summed to determine implied enterprise value (for FCFF).

Investors should then convert the implied enterprise value to implied equity value (often called the “bridge”), as enterprise value represents the value of a firm’s core operations to all shareholders (debt, preferred, equity), while equity value represents the value to equity shareholders only.

How to Bridge From Implied Enterprise Value to Implied Equity Value

Here are the steps to calculate the implied enterprise value, then convert this to implied equity value:

- **Step #1**: Sum the present value of the forecasted FCFF’s, including the terminal value, to solve for the implied enterprise value.
- **Step #2**: ADD: **cash & equivalents** (excess cash not needed for operations), **short-term investments** (marketable securities), and **other non-operating assets** (assets not used in core operations, like unconsolidated investments).
- **Step #3**: SUBTRACT: **total debt** (all interest-bearing obligations), **preferred stock** (has priority over common shareholders), **noncontrolling interests** (other investor’s claims on subsidiaries), and **other non-equity claims** (e.g., unfunded pension obligations).

Note #1: This conversion is not needed for FCFE, simple FCF, or EPS, as these represent cash flows to equity shareholders.

Note #2: Use balance sheet values from the most recent quarterly (10-Q) or annual (10-K) filing as of the valuation date.

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