

FIRSTSTEIN

A COMPANY'S TRUE VALUE is it's

ENTERPRICE VALUE

NOT MARKET CAP

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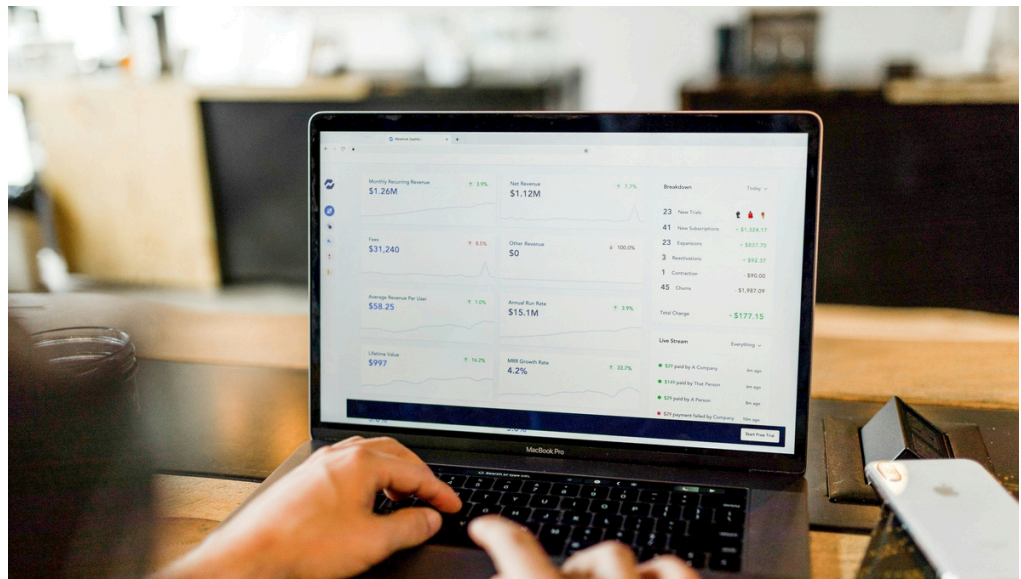
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Many investors rely on market capitalization (market cap) to assess a company's worth. However, this metric only tells part of the story. Enterprise value (EV) offers a more comprehensive picture.

Market cap is simply the stock price multiplied by the number of outstanding shares. While it helps categorize companies by size (small, mid, or large-cap), it fails to consider a crucial factor: debt.



Enterprise Value - The More Complete Picture

EV takes into account both a company's equity (market cap) and its debt.

The formula for calculating EV is:

- $EV = \text{Market Cap} + \text{Total Debt} - \text{Cash}$

Why subtracting Cash?

For the reason that cash on hand isn't directly invested in the business, unlike debt. Subtracting it provides a more accurate picture of the company's value from an acquisition standpoint.

Benefits of Using EV

- For Potential Buyers: EV offers a realistic estimate of a company's acquisition cost.
- For Investors: Understanding a company's EV relative to its market cap is crucial. Debt can significantly impact earnings, which directly affects stock price.

Interpreting the EV/Market Cap Ratio

- High Ratio: This suggests a significant amount of debt, potentially a red flag for investors.
- Low Ratio: Indicates minimal debt, a positive financial attribute.



- EV Below Market Cap: May signify a company with low debt and substantial cash reserves, generally a good sign.

Debt is Not All that Bad, But Moderation is Key. While debt is a common financial tool for businesses, excessive debt can burden a company.

The Takeaway

By considering both market cap and EV, investors gain a clearer understanding of a company's true value and debt level. This empowers them to make informed investment decisions.