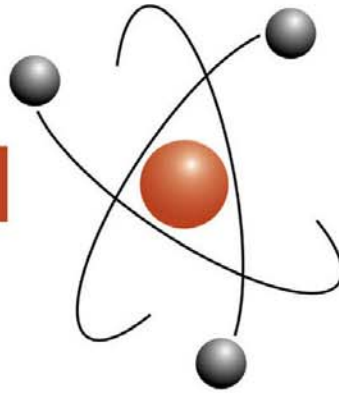


**S U S T A I N**



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**ACTUARIES AND THE FUTURE**

# Non-Insurance Valuations in Practice

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# Overview

- **Introduction**
- **Valuation examples**
- **Typical valuation processes**
- **Observations on GN552**
- **Summary**



# Introduction

- **Background**
- **Scope**



## Valuation Examples

- **Independent Expert's Reports**
- **Business Valuations**
- **Economic Loss Valuation**
- **Option Valuation**



## Independent Expert's Report (IER)

- Report to shareholders
- Governed by ASIC rules (PS75)
- Is it fair?
  - *“value of the offer price or consideration is equal to or greater than the value of the securities”* at 100% control
- Is it reasonable?
  - either fair or else shareholders should accept in the absence of a higher bid



# Business Valuations

- **Valuing unlisted companies**
- **Range of reasons:**
  - financial reporting
  - tax valuation
  - transaction support (whole or part interest)
  - family law



# Economic Loss Valuations

- **Litigation related**
- **Valuing benefits not received due to act or omission**



# Option Valuations

- **Employee options (AASB2)**
  - disclosure of executive remuneration
  - financial reporting
  - Covered by GN510
- **Embedded derivatives (AASB139)**





# Common Definition of Value

- **Fair Market Value**
  - arm's-length transaction
  - willing, but not anxious, buyer
  - willing, but not anxious, seller
  - both fully informed
  - undistorted market



# Typical Valuation Processes

- **Data**

- in most businesses, past events have limited effect on future cash flows (miners are a significant exception)
- management budgets and forecasts are usually optimistic
- less direct relationship between investment market and earnings/cash flow than for insurance & wealth management
- data to project future is often inadequate and/or imprecise
- processes are therefore typically less sophisticated



# Typical Valuation Processes

- **Common Methodologies**
  - Earnings multiple
  - Discounted cash flow (DCF)
  - Risk neutral methods used, but rare outside of options
  - Split out surplus assets and value separately
  - All methods need to be calibrated to market
  - Minority interest vs controlling interest adjustment
  - Negotiability adjustment
- **Cross-check with secondary method**



## Observations on GN552

- **Applies to “economic valuations”**
  - defined as *“the present value or cash equivalent at the valuation date (allowing for time and risk) of all the future cashflows and/or other measures of value that are expected to be derived from the ownership or use of an economic asset for the specified purpose.”*
- **Unusual elements**
  - not market value
  - “for the specified purpose”



## Observations on GN552

- **Derived from insurance specific valuation guidance note (now GN252)**
  - some detail is excessive in wider arena
  - lack of active market for insurance liabilities
- **Some methodologies are not reliable**
  - stock ratios and flow ratios are “rules of thumb”, not valuation methods



## Observations on GN552

- **Methodologies should be market calibrated**
  - Replicating asset must produce market value
  - Earnings multiple should be calibrated to comparable multiples
  - DCF calibrated via discount rate (also secondary check)
  - Risk neutral based on market value for underlying security
- **What is the use of a valuation that does not reflect the market?**



## Summary

- **Most non-insurance valuations are market valuations**
- **Methodologies in GN552 can and should be calibrated to market**
- **Market-calibrated valuation is a market valuation**
- **GN552 should not be limited to “economic valuations”**