The bridge from enterprise value to equity value

The most common misunderstanding in a price conversation: one side talks about the value of the business, the other about the amount on the transfer. These are two different numbers, and the distance between them is often wider than the argument about the multiple.

What a valuation measures

The income and market approaches value the business as a whole — the ability of operating assets to generate cash, regardless of who financed them. The result is enterprise value. A buyer, however, pays for shares, and takes on all of the company's financial obligations along with them.

Three elements of the bridge

From enterprise value I deduct interest-bearing debt, add cash — but only the surplus part, because some of the balance is working capital the business needs to operate — and adjust for items that are neither: tax arrears, deposits, amounts owed to the owner, uninvoiced claims. Each of them carries a number and an amount.

Where the bridge breaks

Usually in three places. First: an owner's loan treated once as debt and once as equity — that has to be settled before the calculation, not after. Second: year-end cash that is a seasonal customer prepayment rather than a surplus. Third: working capital at completion differing from the normal level, which moves the price without changing the valuation.

WHAT I CHECK FIRST

01 Whether the owner's loan is debt or equity — decided and written down

02 How much of the cash balance is genuinely surplus

03 The normal level of working capital and the deviation at completion

04 Off-balance-sheet obligations: guarantees, sureties, litigation

The bridge belongs in the document line by line, not hidden inside a single figure. That way the parties argue about a specific item rather than about the whole valuation.

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