

Putting a Value on an Investment

Narrator: “Putting a Value on an Investment.”

Two hands appear, one holding the word Investment and the other the word Worth. Below them is a question mark. **Narrator:** “What is an investment worth? This seemingly simple question can have many answers.”

An electronic display of stock prices appears, followed by overlaying text that reads Current Market Price. **Narrator:** “The starting point for any valuation discussion is the current market price of an asset. This is widely presumed to be a generally objective answer to the question of a financial valuation.”

A blue hexagon labeled Bid and a green hexagon labeled Ask appear side by side. An arrow extends out from each, pointing to the other hexagon. **Narrator:** “The market price records an actual transaction, so it represents a compromise between two people who have opposite objectives in the deal.”

The hexagons move closer together until their sides touch. An image labeled Seller appears on the Ask side, and an image labeled Buyer appears on the Bid side. **Narrator:** “On one side is a seller, who wants to receive as much as possible. On the other, a buyer, who wants to pay as little as possible.”

The word Price appears, followed by a photo of a broker talking on the phone. **Narrator:** “But the price established by this trade can be as perishable as it is clear. Financial market conditions can change in the blink of an eye. So the market’s trade price may only be meaningful at the moment the trade was executed.”

The scene changes to two men standing beside one another in an office, looking at a computer monitor. They fade from view, and the screen lists different valuation measures, including Earnings Per Share, Free Cash Flow Per Share, Book Value Per Share, P/E Ratio, and Growth Rate. **Narrator:** “What’s more, other investors’ assessments about an item’s value may vary from yours. The prices they agreed to might be different from the price you’d have accepted in the same circumstances. That’s why many professionals weigh valuation measures other than market price to build a more complete portrait of investment value.”

An out-of-focus image of a stock exchange building appears, followed by a hand holding a magnifying glass over some line charts. **Narrator:** “For example, shares of common stock are frequently bought and sold directly through a primary stock exchange. However, investors can also trade options for many companies’ shares on different exchanges.”

A set of perfectly balanced scales appears with the words Stock Value on one side and the words Option Value on the other. The scales move up and down like a seesaw. **Narrator:** “In theory, the direct prices and the options prices are synchronized so that a trade price on one exchange can help anticipate the price on the other. Significant discrepancies between these prices from different venues can be a signal calling for further research and evaluation.”

Line graphs appear over a background showing stock prices. **Narrator:** “Fundamental data can also offer checkpoints for stock market prices. Metrics such as earnings per share, free cash flow per share, and book value per share can provide valuation benchmarks. So can a company's financial performance measure.”

The graphs and background fade. **Narrator:** “Of course, none of these by itself offers a precise alternative to market prices. Part of the art and science of investing is weighing all of these factors appropriately to make effective buy and sell decisions.”

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