THE STAKEHOLDER'S POINT OF VIEW AND BUSINESS AND VALUATION CHALLENGES

Disclaimer:

The position expressed on these slides are personal opinions and are not related to my former and current positions as former Global Vice-Chairman at EY, Global Senior Advisor at Duff and Phelps and Trustee at IVSC, nor represent any academic view of ESCP Europe.

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Macroeconomics Patterns

- **Huge economic uncertainty** = growth, decrease /recession?
- **Commercial war and foreign exchange currency fluctuations** as an instrument of trading war
- **Negative interest rate.** What does this mean? Excess liquidity, deflation
- **Huge volatility in stock prices** – Stocks is the only asset class which has not yet erased the risk premium
- **Climate change, energy transition, new business models** – How and where corporations create externalities?

Shareholders / Stakeholders Valuation Challenges

- Valuations are made for shareholders - discounted cash flows - one value
  Consider cloud of points with a weighted average based on probability
- Based on Business Plan (BP) provided by management which is often too optimistic and a discount rate which reflects a high cost of capital
- Generally 3 to 5 years, too short terms to account for long term effect of externalities
- No real scenarii on BP – High – Medium – Low with probability assigned. What about bankruptcy? How discount rates take this into account?
- Only enacted laws and regulations
- Intrinsic valuation disconnected from market value in some industry
- Stakeholders is a broader category than shareholders!
  Future investors are part of this category, they want to invest and partner with clean companies and look at parameters which could influence future value

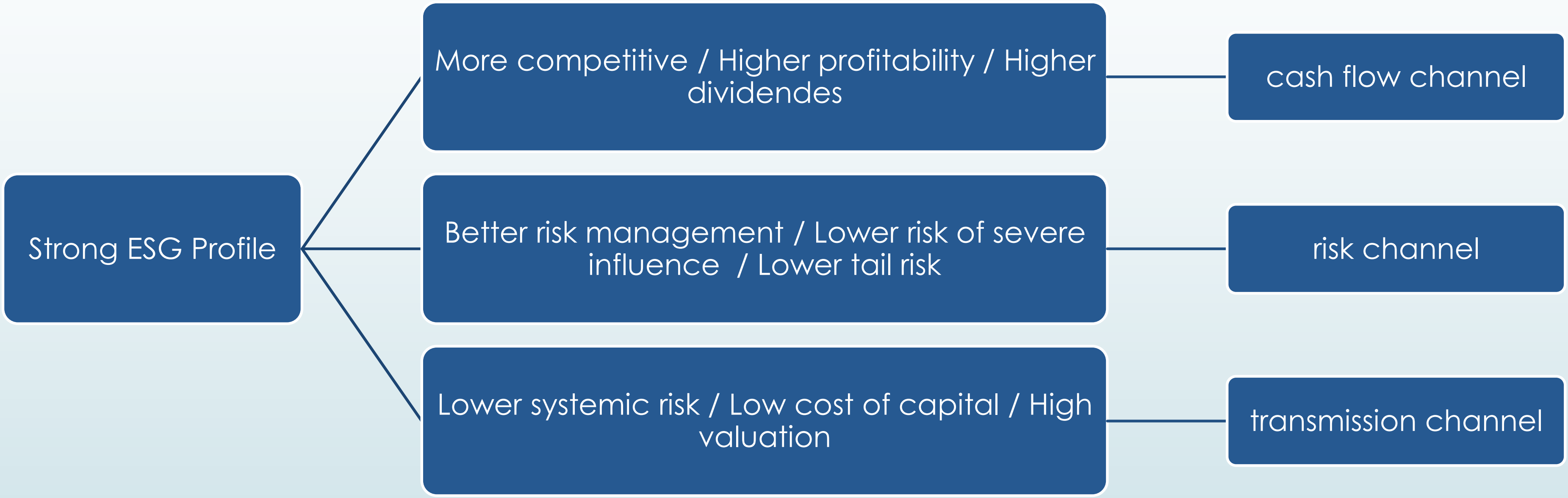
Shareholders / Stakeholders Valuation Challenges

- Focus on a wider spectrum of values to account for current and future risks, business disruption and externalities
- Identification of other KPI and attributes which may explain valuation beyond pure financial parameters (citizenship, quality of the workforce, well being, ESG creation) What is the level of correlation and how is this impacting the cost of capital and improve future valuation?
- Identification of externalities created by corporation whether they are positive or negative
- Externalities can influence value as authorities becoming more aware of these. May want to tax negative or reward positive externalities - may impact future cash flows
- Will facilitate a better allocation of capital
- Examples :
    - Carbon tax / replacement value of water / Shale gas and impact on environment
    - What is the value of oil and gas if fossil rigs cannot be used anymore?
    - Tobacco industry

Shareholders / Stakeholders Valuation Challenges

- **Challenges: How to value externalities to substantiate the valuation?**
  - Current valuation rarely take into consideration externalities – Disclosures do not compensate
  - Need to access data
  - Access research – including academics
  - Build correlation (see below)
  - Management and governance

Shareholders / Stakeholders Valuation Challenges



Source: MSCI

- **Identification of externalities**
  - More understanding of cost / better pricing as customer will better understand the value chain
  - Better risk management in case externalities become a real cost
  - Remediation strategies

Cost of capital and negative interest rates

- **Why cost of capital has not really gone down despite negative interest rates?**
  - Cost of equity still high despite lower expected return, better resilience of corporation and stronger risk management
- **Why? increase risk pressure to account for**
  - Pressure on future growth
  - Size of intangible more difficult to value
  - Perception that negative rates are an anomaly and that rates will go up as inflation appears
  - What if it turns to be wrong?
  - What else?
- **Concern by banking regulations that this leads to wrong allocation between debt and equity**
  - Systemic risk/ credit risk
- **Is there really a bubble in stock market?**

Q&A

Thank you for your attention.