

utb.

Pierre Erasmus | Dietmar Ernst

# International Business Valuation



### **Eine Arbeitsgemeinschaft der Verlage**

Böhlau Verlag · Wien · Köln · Weimar  
Verlag Barbara Budrich · Opladen · Toronto  
facultas.wuv · Wien  
Wilhelm Fink · Paderborn  
A. Francke Verlag · Tübingen  
Haupt Verlag · Bern  
Verlag Julius Klinkhardt · Bad Heilbrunn  
Mohr Siebeck · Tübingen  
Nomos Verlagsgesellschaft · Baden-Baden  
Ernst Reinhardt Verlag · München · Basel  
Ferdinand Schöningh · Paderborn  
Eugen Ulmer Verlag · Stuttgart  
UVK Verlagsgesellschaft · Konstanz, mit UVK/Lucius · München  
Vandenhoeck & Ruprecht · Göttingen · Bristol  
vdf Hochschulverlag AG an der ETH Zürich

Pierre Erasmus, Dietmar Ernst

# **International Business Valuation**

UVK Verlagsgesellschaft mbH · Konstanz  
mit UVK/Lucius · München

Online-Angebote oder elektronische Ausgaben sind erhältlich unter [www.utb-shop.de](http://www.utb-shop.de).

Bibliografische Information der Deutschen Bibliothek

Die Deutsche Bibliothek verzeichnet diese Publikation in der Deutschen Nationalbibliografie; detaillierte bibliografische Daten sind im Internet über [<http://dnb.ddb.de>](http://dnb.ddb.de) abrufbar.

Das Werk einschließlich aller seiner Teile ist urheberrechtlich geschützt. Jede Verwertung außerhalb der engen Grenzen des Urheberrechtsgesetzes ist ohne Zustimmung des Verlages unzulässig und strafbar. Das gilt insbesondere für Vervielfältigungen, Übersetzungen, Mikroverfilmungen und die Einspeicherung und Verarbeitung in elektronischen Systemen.

© UVK Verlagsgesellschaft mbH, Konstanz und München 2014

Einbandgestaltung: Atelier Reichert, Stuttgart

Einbandmotiv: © yuliaglam – Fotolia.com

Druck und Bindung: fgb · freiburger graphische betriebe, Freiburg

UVK Verlagsgesellschaft mbH

Schützenstr. 24 · 78462 Konstanz

Tel. 07531-9053-0 · Fax 07531-9053-98

[www.uvk.de](http://www.uvk.de)

UTB-Nr. 4176

**ISBN 978-3-8252-4176-6**

## Preface

International corporate assessment has become a vital part of today's business valuation. Within the scope of continued globalization, financial experts face the perpetual challenge of measuring the assets or capital equipment of their international subsidiaries or foreign direct investments in a reasonable and comprehensive manner. It is these cross-border acquisitions and dispositions in particular, for which sound valuation is indispensable, as proper assessment is indubitably a crucial factor when reviewing profitability and negotiating transaction prices. On these grounds international business valuation is a powerful tool in evaluating strategic choices.

In addition to that it is already a useful instrument in establishing transparency and communicating effectively with investors and will gain importance in day-to-day corporate management, controlling and financial reporting across national borders. Transparency especially has become an essential issue during and after the recent financial meltdown, which in turn led to an increased importance of international business valuation to allay anxieties of investors and other stakeholders.

Thus, the book's message is to explain how international business valuation can be a critical success factor for good decision-making and effective communication.

International business valuation raises the question whether distinctive features need to be factored in when assessing foreign businesses and, if so, how exactly these additional aspects can be incorporated into the appraisal. The country risk premium regarding the investment in emerging and high growth markets deserves special consideration in this context.

In the scholarly debate, two different schools of thought have developed. While formal scientists prefer a theoretical approach, empirical scientists base their perceptions on more practice-oriented findings.

Formal scientists could find notional proof that CAPM does not tolerate any country risk premiums. Hence, their perception clearly

postulates that the question whether such a risk premium should be included in international business valuation can be answered with a simple “No”.

At the same time, empirical scientists – who, by nature, examine practical observations – are aware of the existence of country risk premiums and, therefore, stipulate their inclusion in corporate assessments. This view seems to be supported by two practical observations:

- a) When examining visible prices or correlating stock prices in emerging/high growth markets, it becomes evident that the use of the traditional CAPM frequently leads to inflated values. High discounting rates are required in order to adjust these high values and phase them with actual prices. Such discount rates are often referred to as “country risk premiums”.
- b) An increasing number of auditing firms and investment banks deal with the challenge of assessing emerging/high growth markets by actually using a country risk premium concept, so as to be able to align computed values, observed stock prices and transaction prices.

With this in mind, there seems to be a need to incorporate country risk premiums into valuation models. Or should CAPM actually be a model that is universally valid even across national borders? The deduction of two different answers can be argued:

- a) It can be empirically proven that – against current economics literature and against experts’ opinions of auditors and investment bankers – the traditional CAPM also works for corporate assessment in emerging markets and high growth countries; or
- b) One needs to accept, that a more realistic assessment approach is imperative. The inspection of a country risk premium suggests that a realistic assessment approach also needs to consider the relevance of the non-diversified corporate risks or at least a part thereof. This is due to the fact that organizations in emerging/high growth markets bear a higher risk in all aspects which in turn justifies additional capital costs.

Should the phenomenon of “country risk premium” indeed be empirically proven – and there are some indications that support this theory – then, existing approaches of modelling international business valuation must be constructively debated with the inclusion of these risk premiums. Consequently, research in this field will need to be intensified.

This book is based on the fundamental principle of traditional business valuation and demonstrates how companies and business units are to be assessed outside their domestic markets. It presents different approaches of modelling a country risk premium as developed by investment banks and auditing companies and explains how an international corporate assessment is being conducted using South Africa as an example of an emerging/high growth market. The contents are being depicted by the means of continuous examples. Every example can be found as an Excel data record on the UTB homepage ([www.utb.de](http://www.utb.de)) and the DICF homepage ([www.dicf.de](http://www.dicf.de)) for the interested reader to practice and carry out some virtual international business valuation. Additionally, the reader gets some useful insight on how to obtain and process the data required for international business valuation.

The book is the product of a joint research project between Stellenbosch University and the European School of Finance at Nuertingen-Geislingen University (NGU).

We would like to thank the UTB-Verlag publishing house and its employees for the constructive and enjoyable collaboration. Dr. Jürgen Schechler deserves our special thanks. We greatly benefitted from his support and his ideas.

You are welcome to contact us at [info@dicf.de](mailto:info@dicf.de) for any feedback you’d like to share. We are grateful for additional ideas, comments, criticism and (maybe even) praise.

We wish all our readers an interesting and insightful read.

Pierre Erasmus (Stellenbosch University)

Dietmar Ernst (Nuertingen-Geislingen University; German Institute of Corporate Finance)





# Table of Content

<b>Preface .....</b>	<b>5</b>
<b>Table of Content.....</b>	<b>9</b>
<b>1      Introduction to International Business Valuation .....</b>	<b>13</b>
1.1    The Term International Business Valuation.....	13
1.2    Reasons for International Business Valuations .....	15
1.3    Specifics of International Business Valuations.....	16
1.3.1   Differences in Accounting Standards and Taxation.....	17
1.3.2   Different Currencies .....	18
1.3.3   Exchange Rate Fluctuations and (Hyper-) Inflation .....	19
1.3.4   Country Risks .....	19
1.3.5   Transfer Risks .....	20
1.3.6   Availability and Reliability of Information and Financial Data .....	20
1.3.7   Interpretation of Key Figures Derived from Local Market Data.....	21
1.3.8   Applicability of Traditional Valuation Methods.....	22
1.3.9   Legally Required Valuation Methods.....	23
1.4    Methods of International Business Valuation .....	25
1.4.1   Single Valuation Methods .....	26
1.4.2   Mixed Approaches .....	31
1.4.3   Total Valuation Methods.....	32
1.5    Approaches in International Business Valuation.....	41

## 10 Table of Content

1.5.1	Presentation of a 5-Step Model for International Valuation .....	41
1.5.2	Business Analysis and Business Planning.....	43
1.5.3	Establishing the Framework Conditions for the Valuation and Choice of One or Several Valuation Methods...	51
1.6	Literature on International Business Valuation.....	54
<b>2</b>	<b>Initial Thoughts on International Business Valuation in Emerging Markets/ High Growth Markets ..</b>	<b>59</b>
2.1	Emerging Markets/High Growth Markets.....	60
2.2	Consideration of Different Currencies in International Business Valuation .....	62
2.2.1	International Business Valuation in Local Currency of the Emerging Markets/High Growth Markets .....	63
2.2.2	International Business Valuation in the Hard Currency of the Reference Market .....	69
2.3	Applicability of CAPM in Emerging Markets/ High Growth Markets .....	73
2.3.1	Critical Assessment of CAPM .....	73
2.3.2	Can the CAPM be used in Emerging Markets/ High Growth Markets?.....	77
<b>3</b>	<b>A Closer Look at Important Model Parameters in International Business Valuation with the CAPM.....</b>	<b>87</b>
3.1	The Market Risk Premium – Definition, Influencing Factors and Determination .....	88
3.1.1	What is the Market Risk Premium? .....	88
3.1.2	Determination of the Market Risk Premium.....	89
3.1.3	Thoughts on the Risk Premium in Emerging Markets/ High Growth Markets.....	94

3.2	Country Risk – An Additional Risk Factor in Emerging Markets/High Growth Markets .....	95
3.2.1	The Need for a Country Risk Premium .....	95
3.2.2	How is the Country Risk Premium Calculated or Estimated? .....	100
3.2.3	Attribution of the Country Risk Premium to the Individual Companies.....	110
3.3	The Beta Factor .....	118
3.3.1	Methodological Questions about the Determination of the Beta Factor.....	118
3.3.2	Determination of Beta Factors in Volatile Markets if Financial Data is not Available .....	120
<b>4</b>	<b>International Business Valuation in South Africa.....</b>	<b>131</b>
4.1	Expanded Model for International Valuation in Volatile Markets.....	133
4.2	Adaptation of Business Planning and Cash Flows .....	136
4.2.1	Adjustment of Cash Flows to Correct for Country-specific Accounting Regulations .....	137
4.2.2	Adjustment of Cash Flows to Correct for Excessive Management Remuneration.....	142
4.2.3	Adjustment of Cash Flows to Correct for Excessive Expensing .....	143
4.2.4	Adjustment of Cash Flows to Correct for Inflation.....	145
4.3	Adjustment of the Cost of Capital (Discount Rates) .....	151
4.3.1	Determination of the Cost of Equity with the help of CAPM-based Models .....	151
4.3.2	Determination of the Cost of Equity with the help of models that are not based on the CAPM.....	182

## 12 Table of Content

4.3.3	Overview of the Calculations Needed for the Models of International Business Valuation.....	191
4.3.4	Comparison of the Models .....	192
4.4	Model Selection .....	195
4.4.1	An Overview of the Cost of Equity of the Various Models.....	198
4.4.2	Determination of the Cost of Debt.....	199
4.5	Additional Adjustments for the Incorporation of Unsystematic Risk .....	201
4.5.1	Company Size (Size Effects).....	203
4.5.2	Block Premium (Majority Discount) .....	204
4.5.3	Mobility Premium (Liquidity, Fungibility Premium) .....	205
4.6	Calculation of the Business Value.....	207
4.6.1	Calculation of the Business Value with the WACC Approach .....	207
4.6.2	Calculation of the Business Value with the Equity Approach .....	221
	<b>Summary of this book .....</b>	<b>237</b>
	<b>Bibliography .....</b>	<b>239</b>
	<b>Index .....</b>	<b>245</b>

# 1 Introduction to International Business Valuation

## Learning Outcomes

- Understanding of the term international business valuation and its relevance as an academic method for the determination of the value of a company.
- Understanding of the reasons for international business valuations.
- Knowledge of the specific features of an international business valuation and the ability to use that knowledge in international business valuations.
- Ability to reproduce the most important approaches to international business valuation.
- Understanding of the 5-step approach towards international business valuation and the ability to present this approach.
- Ability to explain the difference between the single valuation method and the multiple valuation method.
- Knowledge of the literature on international business valuation.

## 1.1 The Term International Business Valuation

The advancing globalization has significantly increased the demand for **reliable valuation principles and mechanisms** for cross-border transactions and the valuation of capital assets and current assets of subsidiaries abroad. Especially in the case of cross-border acquisitions and sales of companies, the determination of transaction prices, the related negotiations and any assessment of the economic consequences absolutely depend on a solid valuation.

And valuations also gain in importance with regard to controlling, accounting and transparent communication with the providers of capital. Especially the latter point has caused an increasing demand for business valuations during and after the recent global financial crisis. In the past, companies were able to finance acquisitions abroad with equity capital or unsecured bank loans, thanks to the availability of strong equity capital cushions. During the crisis, they were increasingly forced to raise available collateral by drawing on assets held abroad. The determination of the value of capital assets and current assets held abroad has posed great challenges for companies, financial auditors and banks.

While pragmatic approaches for the valuation of companies abroad were developed by **valuation practitioners**, the academic literature has paid relatively little attention to the topic.

In the following sections the term **international business valuation** refers to the determination of the value of entire companies or participations in companies with a specific focus on the peculiarities of foreign markets. The term foreign markets needs to be defined more precisely and refers both to countries with developed capital markets and also to countries which – in contrast to established industrial nations – do not possess developed capital markets. This poses specific challenges for valuation professionals. At issue is not only the question whether traditional valuation methods can be adequately applied, but rather how they can be included in the valuation process in the absence of appropriate information about **country risk** and **transfer risk**.

### **Definition: International business valuation**

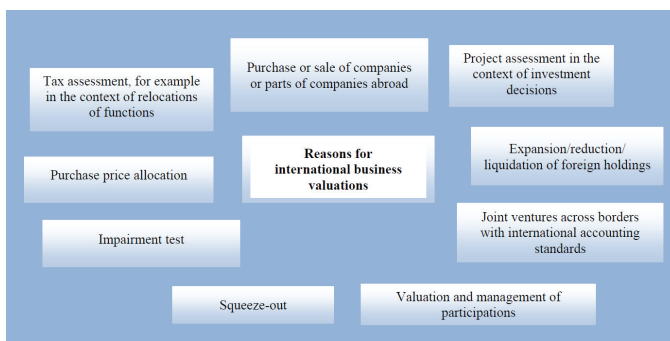
International business valuation is defined as the determination of the value of entire companies or participations in companies with a specific focus on the peculiarities of foreign markets.

In the following, international business valuation is presented from the perspective of a German valuation expert. Thus “Home” refers to Germany in the following, while “Abroad” can be any foreign country.

## 1.2 Reasons for International Business Valuations

As a consequence of the accelerating globalization and the growing international value chain, valuations in an international context are becoming more and more common in daily company business.

Typical **reasons for an international business valuation** are (see Figure 1.1):



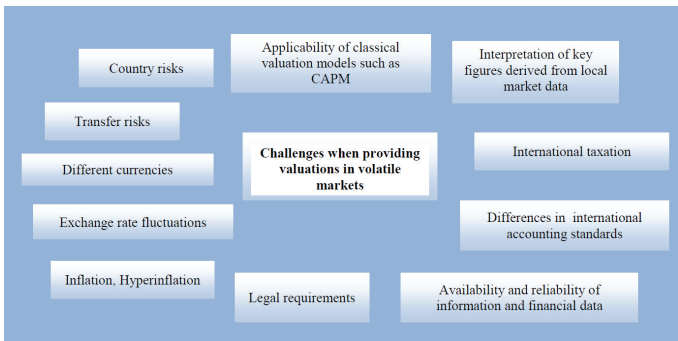
**Figure 1.1:** Reasons for international business valuations

- Purchase or sale of companies or parts of companies abroad
- Project assessment in the context of investment decisions
- Expansion/reduction/liquidation of foreign holdings
- Joint ventures across borders

- Valuation and management of participations
- Squeeze-out
- Impairment test
- Purchase price allocation
- Tax assessment, for example in the context of relocations of functions

### 1.3 Specifics of International Business Valuations

The valuation of companies in “emerging markets” (also “high growth markets”) is subject to a number of specific considerations, which are described in the following. This also makes it possible to address the specifics of the situation by applying appropriate methods of international business valuation.



**Figure 1.2:** Overview of problematic areas in international valuation in volatile markets



Figure 1.2 provides a first overview of challenges and problems which valuation experts repeatedly face when dealing with international business valuation in high growth markets/emerging markets.

### 1.3.1 Differences in Accounting Standards and Taxation

One problem faced in international business valuations refers to the fact that **local accounting regulations** are often not comparable with international accounting standards, especially if their use – at a minimum for companies with a capital market orientation – is not mandatory.

The comparability of **financial figures** of companies abroad with those of companies in developed countries is frequently rather limited because of the existence of country-specific rules. So even if a valuation expert is able to define a peer group, comparisons, for example of profitability, are made difficult. Annual reports or key figures must therefore first be adjusted in order to allow a suitable analysis or conclusions and to eliminate distortions of the true economic performance of the valuation object.

Obtaining the necessary knowledge about **country-specific accounting regulations** is frequently associated with substantial effort and requires specific knowledge. This is an additional challenge for the valuation expert. While disclosure requirements have increasingly been tightened over the past years, especially in developed countries, less restrictive rules are frequently observable in emerging markets/high growth markets. This trend is likely to continue for a number of years. And the mandatory use of international accounting standards has yet to be realized. But a tendency of increasing alignment and harmonization of the accounting and reporting systems of emerging markets/high growth markets with international standards is observable. This will increase the transparency and attractiveness for international investors.

The current **tax regime** and corresponding legal requirements are also relevant for valuation. At issue is not only the adequate consid-

eration of tax expenses that directly affect payments as a consequence of the legal form, but also the assessment of company structures driven by tax considerations, possibility and implications for the disbursement of funds as well as tax risks.

### 1.3.2 Different Currencies

When valuing businesses in a single currency area, exchange rate effects and exchange rate calculations are not relevant. But if the perspective of the valuation expert is different with regard to the currency at home, a decision has to be made about the relevant currency for the valuation exercise.

A valuation can be done either in the **local currency** of the home country of the company under consideration or in a **reference currency**. This is relevant for the aspect of currency equivalency in the valuation exercise.

Once the base currency has been selected, consistency in conducting the valuation is important, especially when determining and calculating the cash flows and the discount rates. They need to be translated into the chosen currency using **consistent assumptions**.

Due to the specific situation in emerging markets/high growth markets with regard to the currency, **valuation exercises** can be problematic. As an example, a valuation in local currency can be difficult, because the riskless rate of interest, which is needed to calculate the cost of capital, is hard to determine due to a lack of long-term public bonds issued by the government of the emerging market/high growth market. This, as well as other related features, can imply the significantly increased complexity of the valuation.

### 1.3.3 Exchange Rate Fluctuations and (Hyper-) Inflation

Many foreign currencies are frequently very volatile, both with regard to **exchange rate fluctuations** and **inflation** (loss of purchasing power).

And the standard practice of **fixing** the local currency to a stable foreign currency, such as Dollar or Euro should not mask this volatility. Frequently overlooked are revaluations of the local currency, which can be significant in some cases.

Exchange rate fluctuations and inflationary developments can also lead to massive distortions in the **annual financial statements**. Thus they must be taken into consideration when determining cash flows or discount rates.

### 1.3.4 Country Risks

Investments in emerging markets/high growth markets are frequently rewarded with high growth rates. But these increased opportunities usually also correspond with additional macroeconomic risks. If investors take a stake in countries such as Brazil, Russia, India, China or South Africa (so-called BRICS countries), they are exposed to political or economic turbulences in these markets. No company that is active in the emerging market/high growth market is able to escape the influence or the situation inside this country over the long term. If a country collapses politically or economically, this also affects the best run companies.

Does this mean that an investment, for example in Brazil, generally has a higher risk than an investment in Germany, France or the United States?

When the investment is considered in isolation, this question about the general relevance of country specific risks must be answered in the affirmative from the perspective of valuation experts and investors. In the context of a globally diversified group of companies, an investment in an economic region that is far away from the home

country and has its own currency can still make a positive contribution from a risk perspective. Examples are the manufacturing sites of major German automobile companies in the US, which achieve natural hedging against currency fluctuations in the Euro-Dollar relationship.

There is fundamental agreement among valuation practitioners that country risks must be considered in the context of international business valuation. But there is disagreement about the determination of the relevant premium needed to compensate for the country risk in a valuation exercise. Of particular relevance in this regard is the aspect of risk equivalency, especially with regard to the determination of capital costs when assessing the net present value of earnings.

### **1.3.5 Transfer Risks**

Transfer risks can jeopardize the business success of foreign investments and relate to the repatriation of profits and capital. Transfer risks include exchange restrictions imposed by a government or the central bank, which make it impossible for the investor to be repaid. While the investor has deposited the respective amount in local currency, he does not get access to the needed foreign reserves, since the central bank does not provide them.

Also considered a transfer risk is the possibility that payments from a country in financial difficulties are refinanced even though they are due. Such a transnational agreement reached by the Paris Club can delay payment by several years.

### **1.3.6 Availability and Reliability of Information and Financial Data**

The procurement of information and financial data for the company abroad which needs to be valued as well as for its environment and comparable companies often constitute additional problems when conducting an international valuation. As it turns out, the

**data history** in emerging markets/high growth markets often is of insufficient length or does not exist at all.

In case data is available, it must be assessed how **reliable** and **meaningful** it is. The quality of the valuation result depends to a large degree on these factors and requires a major effort concerning research and analysis. Frequently fundamental data such as the **intrinsic value** or validity of sales and rental contracts for land and real estate must be questioned. And in many emerging markets/high growth markets it cannot be assumed that the transfer of ownership does not impinge on the continuation of existing agreements concerning the calculation and payment of taxes, liquidity and trading lines at banks or distribution and service contracts.

### 1.3.7 Interpretation of Key Figures Derived from Local Market Data

A frequently utilized approach in business valuation is the determination of parameters from data observed on the capital market. One example is the beta factor, which is obtained from a regression of the company returns on the returns of a suitable index. But how meaningful are these types of calculations in light of frequently observable features such as **illiquidity**, **lack of transparency** and **high transaction costs** on the financial markets in the emerging markets/high growth markets? Does the share price reflect the adequate value of the company, even though there is very little trading in the stock and quotations are frequently not based on any trading? Thus ratios and indicators which are based on illiquid and less developed capital markets must be used with greater reservations compared to developed markets. Not only the general availability of financial market information but also its significance causes problems for the valuation expert.<sup>1</sup>

---

<sup>1</sup> See Damodaran, A. (2009), p. 5.

### 1.3.8 Applicability of Traditional Valuation Methods

It must be stated initially that in light of the conceptual difficulties and the scarcity of information, the task is not to develop a new valuation approach. The **traditional valuation methods**, predominantly the discounted cash flow (DCF) approach in all its variations, continue to be widely used by practitioners.

And with regard to the existing capital market models for the determination of risk, the Capital Asset Pricing Model (CAPM) – despite all its limitations – continues to be the accepted standard for the determination of the cost of capital and is used by practitioners globally. But it remains questionable whether the CAPM is also a suitable model for the determination of the cost of capital in emerging markets/high growth markets. As will be shown, CAPM cannot be used in its basic form and must be adapted accordingly. In this regard, several variants of the CAPM or alternative approaches are suggested. These variants are special in the sense that the relationship between model parameters – riskless return, beta, market risk premium and country risk premium – must be defined in a way that adequately captures all risks in emerging markets/high growth markets risks, but also avoids double counting of these risks.

Among academics and practitioners as well as in the current literature there is **disagreement** about how to implement the specifics of emerging markets/high growth markets and which models should be used concretely in an international valuation. This disagreement is certainly also one reason for the current lack of a unified standard. Instead a large number of different models for international business valuation continue to exist. Partly this expresses a desirable plurality of methodologies, but it is also the unsatisfactory answer to the question of how to conduct valuations in incomplete markets.

In summary it can be stated that a valuation expert is confronted with **numerous problematic areas** when conducting an international business valuation. Put differently, the existing conceptual

difficulties in valuation exercises become more severe in the case of international valuations.

Due to the many **situational factors** which interact in an international valuation, it is not always easy to point to a simple solution. It is the responsibility of the valuation expert to take these factors into consideration in his own valuation approach.

The **basic principle** of an international valuation resembles that of a domestic valuation. For methods that rely on capital values, cash flows need to be determined, which are discounted using an adequate cost of capital. The market based approaches meanwhile rely on the calculation of multiples for a peer group, which are applied to the relevant reference value of the company to be valued. The difference and also the difficulty stem from the availability of data as well as the additional risk factors which are present in emerging markets/high growth markets and must be taken into consideration when determining input parameters. This requires that cash flows and multiples are adjusted and the CAPM is modified or expanded. Of particular relevance in this regard is the assessment of the reliability of the future cash flows, initially in foreign currency, but ultimately in the reference currency which is preferred by the principal.

### 1.3.9 Legally Required Valuation Methods

Mandatory legal regulations concerning the valuation of assets exist in some emerging markets/high growth markets. In China for example this is the “**Statutory Valuation**” which is legally mandated whenever assets are purchased or transferred that directly or indirectly are owned by the Chinese state.

With its “Decree 91” under the working title “Statutory Valuation”, the Chinese government in 1990 laid the foundations for the mandatory application of “Generally Accepted Valuation Practices” in China. The purpose was to prevent the **sale of government assets** by State Owned Enterprises (SOEs) below their value, or at least to make this more difficult.

**Decree 91** mandates that the statutory valuation approach must be applied in case of:

- contributions in kind
- liquidation
- mergers which change the ownership structure
- share purchases

The statutory valuation can only be conducted by one of 6,000 Chinese valuation companies that hold a government license. The selection and commissioning of the valuation firm is usually done by the seller of the government assets, in other words by the SOEs. The sales price of the transferred assets is only allowed to deviate by a maximum of 10% from the value assigned with the help of the statutory valuation (“90% Rule”).

For publicly listed companies, **public bidding** via the equity exchange must take place. In this case the seller is required to publish information about the company and the assets that are for sale as well as the result of the statutory valuation. The offer must be made public within 20 working days.

For companies that are not publicly listed, the business value is usually derived by valuing all assets (“**Asset Approach**”). Since the valuer is hired by the government, he will usually prefer valuation approaches that result in a particularly high total valuation. And he has a lot of leeway in this regard. For capital assets the valuer can use either historical acquisition costs or current replacement costs. Especially for machinery purchased abroad, this can have a massive effect on the valuation due to the volatility of exchange rates. And the choice of depreciation methods also leaves considerable scope. Frequently the approach “Economic Life” is chosen, even though the asset has long been completely amortized from the perspective of accounting. It holds in general that the value of an asset can never fall below the threshold of 15% of the purchase price. For buildings the residual value amounts to 30% of construction costs. The valuer furthermore has significant freedom when it comes to the valuation of provisions, current assets, contingent liabilities and goodwill.



**International accountancy firms** are usually not accredited as “Statutory Valuer”. However, they offer support in the process. This service is called “Statutory Valuation Monitoring” for example and is offered in combination with the implementation of legal, tax, financial and environmental due diligence. The aim of the consulting service is to supervise the valuation process and to support the interests of the interested foreign party in a dialogue with the Chinese valuer. It is frequently possible that adept arguments voiced by the adviser can convince the Chinese valuer to apply an approach that is more advantageous or at least neutral for the buyer or that he does not use the full scope that is given to him to the sole advantage of the seller. The aim is to achieve a more realistic valuation result from the perspective of the potential foreign buyer. It is important in this regard that the interested foreign party obtains knowledgeable support before the proceedings begin, since the transaction value can only deviate by a maximum of ten percent from the statutory valuation as discussed above.

## 1.4 Methods of International Business Valuation

As already mentioned, the methods of international business valuation do not fundamentally differ from the known valuation approaches. In applied international business valuation, some methods appear to be particularly adequate and for emerging markets/high growth markets a few specific valuation methods were developed.

In the following, the methods which are preferred in international business valuation are briefly explained. As can be seen in Figure 1.3, the business valuation approaches can be broken down into single valuation methods, mixed methods and total valuation methods. Since the methods which focus on the capital value (DCF approaches) are of central relevance in the context of international business valuation, they are presented in detail in the following chapters and illustrated with the help of the Case Study. For this