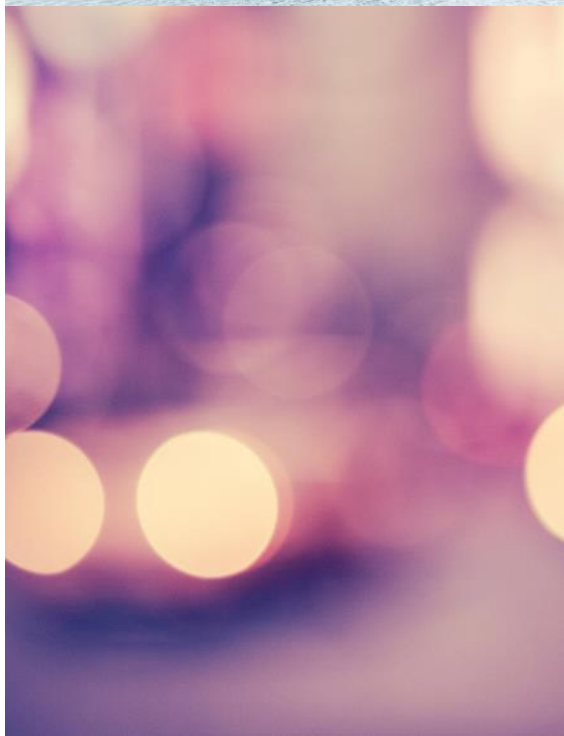


How Top Investment Banks Value Real Stocks

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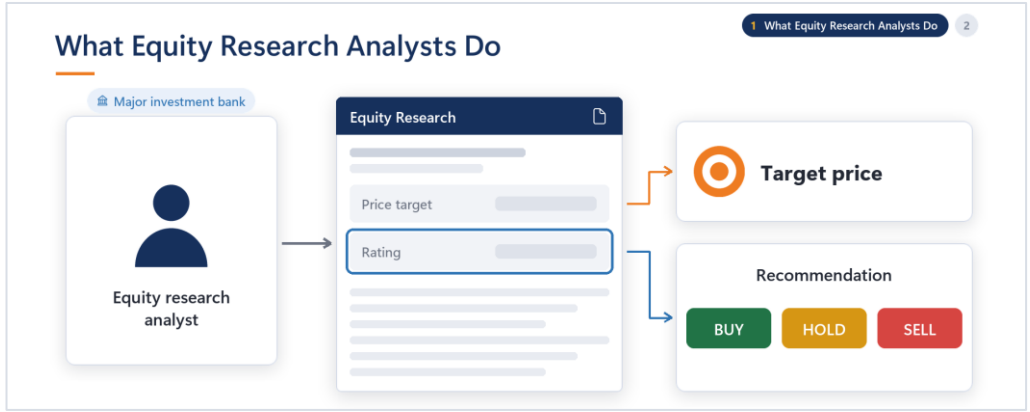
5. How Top Investment Banks Value Real Stocks

📋 What Equity Research Analysts Do

- Equity research analysts at major investment banks publish reports on stocks.
- Each report assigns a target price and a buy, hold or sell recommendation.
- The target price is the analyst's estimate of what the stock is actually worth.
- It is not the price the stock currently trades for.
- This is the value versus price distinction from the opening lesson.

🔍 JP Morgan vs. BofA on Tesla

- Both banks analyzed the same company with the same public information, yet target prices were worlds apart.
- JP Morgan blended DCF at 50% weight with three relative valuation multiples at 50%, anchored to 2-year forward earnings.
- BofA used only relative valuation but projected 5-year forward earnings instead.
- Tesla had rapidly growing revenue but very modest profits, so a 2-year P/E lens produced a low valuation.
- 5-year forward earnings captured far larger projected revenues and profits, pushing the target price dramatically higher.
- JP Morgan used P/S (an equity multiple), BofA used EV/Sales (an enterprise value multiple); this choice also contributed to the divergence.

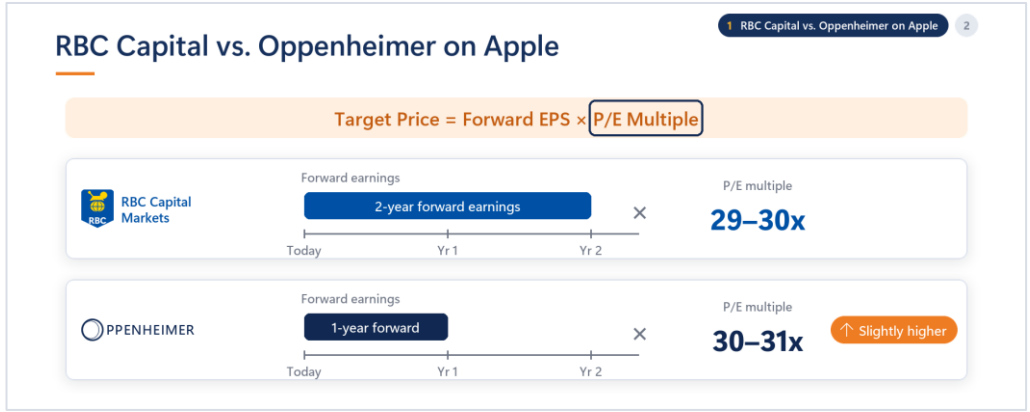




5. How Top Investment Banks Value Real Stocks (Part 2)

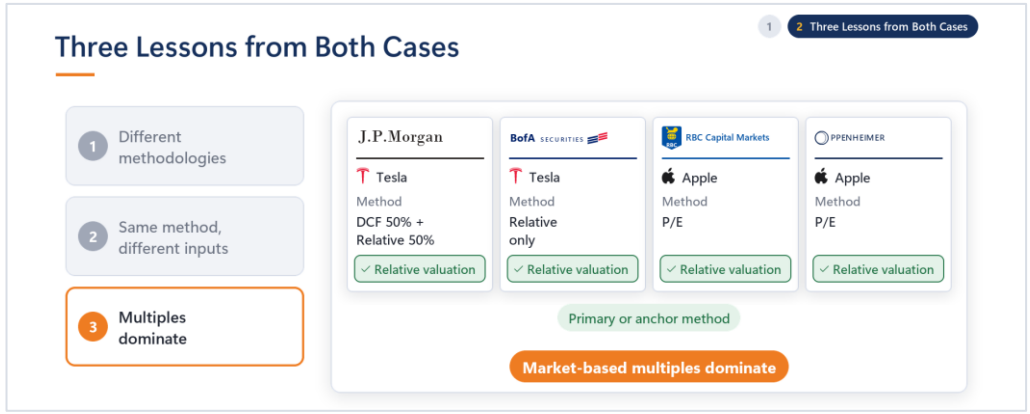
🍎 RBC Capital vs. Oppenheimer on Apple

- Apple, unlike Tesla, had consistently high profit margins, making P/E a natural and sufficient choice for both banks.
- Yet target prices still differed: RBC above $130 and Oppenheimer above $120.
- RBC applied 2-year forward earnings at a multiple of 29 to 30 times.
- Oppenheimer applied 1-year forward earnings at a slightly higher multiple of 30 to 31 times.
- Earnings further into the future are larger for a growing company, so RBC's target price was higher.
- Oppenheimer's higher multiple on a smaller near-term earnings base gave a lower result.



📌 Three Lessons from Both Cases

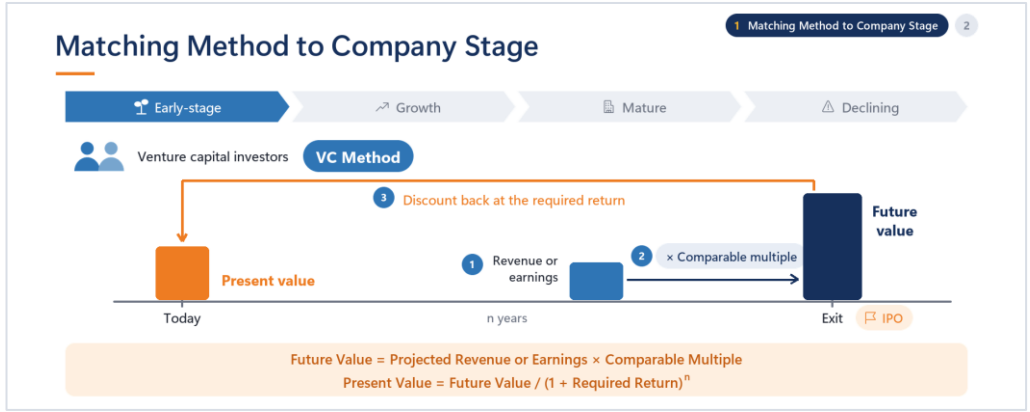
- Four banks studying two companies teach three clear lessons.
- First: the same company can be valued using different methodologies.
- Second: even with the same method, inputs such as forecast horizon and comparable multiples can differ.
- Third: all four reports used relative valuation as their primary or anchor method.
- Market-based multiples dominate equity research practice.
- The differences are not errors; they reflect each analyst's judgment and interpretation of the same business.



5. How Top Investment Banks Value Real Stocks (Part 3)

🔄 Matching Method to Company Stage

- The right valuation method depends on where a company sits in its lifecycle.
- Early-stage companies generate little or no revenue, so a standard DCF is unreliable.
- VC Method: estimate revenue or earnings at an exit such as an IPO, apply a comparable company multiple to get the future value.
- Then discount the future value back at the required rate of return.
- Growth companies have revenue but may carry thin or negative margins; EV/Sales and P/S apply cleanly.
- A DCF works with an explicit assumption on when profitability arrives and at what margin level.
- Mature companies are the most straightforward: stable cash flows let DCF, EV/EBITDA and P/E all work reliably.



📉 Diagnosing Declining Companies

- Declining companies require a diagnosis before any method is selected.
- If the industry is becoming obsolete, the decline is likely permanent and asset-based valuation is more appropriate.
- If the cause is cyclical, the recovery timeline depends on a macroeconomic forecast.
- If poor management is the cause, assess the likelihood and pace of operational improvement.

