# Charles Sunnucks (book review)

**Speaker1:** [00:00:04.77] This is the Investor Connect podcast program. I'm Hall Martin and the host of the show in which we interview Angel Investors, venture capital, family offices, private equity, many other investors for early stage and growth companies. I hope you enjoy this episode. Hello, this is Hall Martin with Investor Connect today here with Charles Sunnucks , investor and author of the company Valuation Playbook. Charles, thank you for joining us.

**Speaker2:** [00:00:31.53] Yeah, thanks for having me on.

**Speaker1:** [00:00:33.07] Great. So let's start with what was your background before working with early stage companies?

**Speaker2:** [00:00:37.98] Yeah. So before starting to invest kind of my my background, as you can probably hear from my accent, I'm British. I went out to China for five years, four years of doing that kind of studying Chinese very much got into the kind of growth mindset in terms of investing, came back to the UK and really kind of just over a decade have been investing myself. And then more recently, I've kind of taken a step back to focus on writing this book again.

**Speaker1:** [00:01:06.02] And so what excites you right now in Europe?

**Speaker2:** [00:01:09.27] Well, so certainly not writing. I don't think at the moment, to be honest. My my my passion is investing a lot. I used to write lots of kind of 1000, 2000 word pieces for clients, etc. Writing a kind of fifty thousand word book, as I now realize, is quite, quite, quite different. It's quite liberating being able to write far more. But at the same time, after years of trying to get everything to be as concise, as punchy as possible is quite a different mindset to alter that. So I think for this book, I need to do some marketing around it. And then then later in the year, I'll certainly try and get back into tax and investment. And that's where my heart lies. And kind of I think it's an absolute great career choice for anybody really to go into a great.

**Speaker1:** [00:01:54.42] So you wrote the company valuation playbook. Well, what inspired you to write it?

**Speaker2:** [00:01:59.09] It was very much my own experience. So here in the UK, Cayley's and I imagine it's very much the same in the US as well. Kind of when you get into finance, you're faced with a myriad of of exam's kind of an alphabet soup of exams. And so here we have to do the kind of CFA, IMC, FVA, CEA, the CFA, UK, ESG examination. And so there's lots of exams and those exams are examining people far less. So really, in my view at least, was to give people kind of ready to equip people with the practical tools to actually value a company. It's very hard to get that across an exam question. So the material is not really going to build towards that. And there's lots and lots of brilliant books out there that tell you to to invest in a company at a good value. There's far, far, far fewer. In fact, if you look on Amazon, there's only one that are really directly answers the question, how do you value a company? What what is value is one thing to say kind of investment value. It's quite another to be informed and understand what that means.

**Speaker1:** [00:03:04.93] Great. Can you expand on that? Tell us more about the book and what it does do.

**Speaker2:** [00:03:08.82] Yeah, sure. I broke the book down. It's kind of five core core areas. The first one is assess and not just looks at the quality features of a company. Can I use what I call a kind of cool castle, a moat approach to that? So the course is very much the management of the company, corporate governance, the board, etc. The castle is how attractive the business is itself, kind of profitability, capital structure, etc. And that last bit is just the moat. You've probably heard about this from Warren Buffett before, kind of having a strong economic moat to be able to sustain profitability over time. Then it goes onto the quantitative approach, which is very much just the accounting angle and factfinding, which is targeted at where you can go to find information on companies, especially if you're new to investing. So that's the assessment part. Then it goes on to projecting, projecting both the return profile, so being able to do a financial model and projecting the risk and so what should be required return, et cetera. And then finally, the kind of pricing. So they're kind of using either a relative valuation methodology or intrinsic valuation methodology.

**Speaker1:** [00:04:20.76] Great. And so who is the primary audience for it

**Speaker2:** [00:04:23.88] As an investor? I mean, for me, as really anybody that wants to make informed judgments when they're setting out to invest. And so I think it's quite broad in that sense. I think the people that would benefit from it most, though, are those that are kind of interested in getting to finance or early in their career and finance and really just want something that can shift them up. A couple of gear is quite easily before they have to hit these industry exams. I very much wrote this as the kind of book I wish I had when I was in my early 20s. And the Internet is a great base for getting some information. You can you can find some high level details on valuation. But more often than not, and I'm sure, you know, a little information can be quite dangerous when you don't have full context for that. So so I hope that this book's really a bridge between just the kind of high level of oversight from from the Internet versus kind of the really kind of comprehensive examinations that are out. Which require kind of hundreds of hours of studying.

**Speaker1:** [00:05:26.12] Well, who else could benefit from reading it?

**Speaker2:** [00:05:28.19] I think I kind of certainly at the other end of the spectrum will be those that have kind of 40s, 50s, 60s, have some savings and want to kind of put that to use make a return, make a return on their savings and not just by the to an ETF. I mean, I touched on this in my book. I mean, I think there are also remarkable kind of social benefits to investing, kind of I think the society having an efficient capital market where you've got people who are investing fundamentally unable to kind of cooperate in price discovery and capital markets, et cetera. I think it's often overlooked how helpful for a society and an economy that can be.

**Speaker1:** [00:06:09.56] Well, do you see company founders and CEOs using it to understand the value of their business rather than waiting for somebody to tell them what they think it is?

**Speaker2:** [00:06:17.68] Yes, absolutely. That that's a very good point, actually. I always have a huge admiration for those, especially entrepreneurs who have built their business up from the bottom and kind of really remarkable, remarkable people. I think in that it takes a very special person to be able to do that. And for this book, I think that would create some excellent insights. In fact, one of the the key people who was helping me with this book, he himself is going to be building up a company. And these kind of I had lots of discussions with him targeted at, well, what's the kind of questions you ask yourself when thinking about your company and how you're going to try and try and market that and say that process? In a way? I mean, you can certainly see if you if you read the book in terms of kind of targeting early stage companies. And we've got a whole chapter actually on early stage and start up companies and kind of answering those kind of valuation questions, which I think many people would have.

**Speaker1:** [00:07:15.86] All right. So what surprised you the most when you wrote it? What did you learn that was maybe changing your your view?

**Speaker2:** [00:07:22.37] Well, nothing's really revolutionary, which I've written. What I have found, though, taking a step back from the investment itself was just I was surprised at how much I wanted to write about behavioral biases. I mean, we know that we all have the same kind of class cloud and otherwise objective opinion and can create errors of judgment, et cetera. But I did a lot of reading and research for this book, and it's very interesting, just kind of being able to write about that. And if you can, understanding it, helping yourself kind of to be able to avoid those type of errors by, for instance, kind of having the right process, kind of asking asking around people who may not agree with you about your investment case, et cetera. I think that's kind of one of the more powerful parts which I didn't expect I'd be keen to write so much on.

**Speaker1:** [00:08:15.05] My experiences is that startup founders are doing an evaluation and they're trying each of the different methods. And then the one that gives them the highest number is, of course, the right one that they propose. The investor on the other side of the table is doing the exact same thing. They're looking at all the valuation metrics, but then they're choosing the lowest value if they're investing or buying to give them the best value for their dollar. How often do you see that playing out like that?

**Speaker2:** [00:08:41.24] Yeah, yeah, absolutely. I mean, this is this is the thing, right, is that that there's a difference between price and value. So what will say what an investor is may be willing to offer the price and what your business is actually valued at. And that can be a big disconnect between those two. It is absolutely kind of not a perfect market, not least in kind of early start up and entrepreneurs. And so being able to if you're an entrepreneur and you want to have confidence when you raise capital, take on new shareholders, that you are not being done over a barrel for want of a better phrase on pricing, you do need to understand stand value, I think is what Warren Buffett he said price is what you pay, value is what you get. And therefore being able to kind of know going into negotiations what the value of your business is. I think that's kind of an incredibly important kind of element to any negotiation.

**Speaker1:** [00:09:42.14] Right. And that's what I always tell people. Valuation is not a formula. It's a negotiation. The math up front is giving you ammunition for the negotiation that comes afterwards because you have to convince the other side that your approach and your numbers are the best way of doing it is the correct way to do it. And they're, of course, trying to do it the other way. How often do you see how can you use valuation in a negotiation, for example?

**Speaker2:** [00:10:05.45] Yeah, I think I mean, if you understand, I think it's hugely I think it's hugely beneficial, actually, because you understand the component parts that go into it and then you can articulate why it should be such that there's plenty of clever tricks. So kind of this mate of mine who helped me, certainly. The start up part, apparently, one of the better tricks the bankers do is can you give out some high growth forecasts? And of course, they'll be too high and kind of you can kind of negotiate with bankers, but then all they'll do is kind of change the discount rate to kind of kind of balance it out, that there's a number of those kind of little nuances which are just like small little insights, which I think kind of do help. And if you can understand what the discount rate is, what a risk premium is, what are expected returns and kind of know those kind of terminology and the way that any banker or kind of potential buyer, for instance, may try and kind of frame a valuation, I think that's certainly kind of helps at least tilt the scales in your favor when it comes to negotiations.

**Speaker1:** [00:11:07.39] As you point out, he startup founders proposing their valuation. And no matter what they put out there, the investor will push back and say, how did you arrive at that? And those who can articulate the values? Well, usually when those who say, well, I just think I'm worth that don't usually when or when very often. So it's interesting to see how you can articulate your values and numbers as well as in negotiations as well. But what was the most important takeaway you found in writing this book?

**Speaker2:** [00:11:36.54] For me, the most important for what? I hope that anybody reading the most important takeaway, it is not necessarily that you need to memorize every chapter is simply the kind of key principles behind valuation, behind relative valuation that you are standardizing kind of companies by using some type of measure or ratio or of using intrinsic valuation that the key principle that the company is worth the return, the adjusted returns that it will generate. I think kind of when you when you kind of when you start to kind of be able to really digest that when going into value anything and not just equity of a small company or a big company, but even a bond, if you want to raise that, once you understand those principles, they're actually kind of very widely applicable to any type of financial instrument.

**Speaker1:** [00:12:26.73] Great. And then. Well, how did the book change the way you think about valuations?

**Speaker2:** [00:12:30.99] I've always said that I'm a kind of long term investor. I kind of don't invest in something, even for 20 seconds, if you wouldn't be willing to hold it for 20 years type philosophy. And I, I suppose I was kind of become almost more entrenched in that, especially while writing this. Obviously, we've had the Corona, covid, etc. being locked down. And it does make you step back and think because especially more of the mature companies where you get a dividend people and got paid their dividend this year and therefore the company collapses. And you kind of think, I mean, even if you thought that the company wasn't going to grow at all over the next 20 years and its life was to stop, then one dividend payment is not going to really kind of make a large difference. I mean, most people obviously make about five percent difference to your total return.

**Speaker1:** [00:13:22.29] And so based on writing this book, in your experience, what are you going to do next?

**Speaker2:** [00:13:27.24] I think ultimately I'll be going back to active investment in writing this book. I've probably written about twice the contents that will actually go into the books. I've almost got at the beginning. I wrote a lot on the history of companies and kind of capital markets, but I ended up feeling actually the kind of reader that probably wants to buy this book is somebody that simply wants to invest. There's actually a lot of good books out there on kind of the history of capital markets already. And I don't really feel but I was kind of adding to to that in a way. So it's so unfortunate. I just literally just dropped the chapters are so I've almost lost that kind of quarter of a book, kind of ready and waiting at some point. I did want to write more.

**Speaker1:** [00:14:11.94] They write well. What are your current thoughts on valuation levels today? We're coming out of covid in various stages of reopening and the markets are at all time highs these days. Is this a bubble or are these valuations justified?

**Speaker2:** [00:14:27.12] Yeah, it's a it's a tough one. I mean, I think I mean, obviously, valuations have decoupled massively. Most of the high growth companies obviously done very well. A lot of value companies have in many ways, valuations have become even more depressed. I mean, my my view at the moment is that everybody is being rational. Long term interest rates are very low. And so that is the reason why growth companies valuations are so high. People are not discounting kind of having to wait for a company's cash flow as a very high level. And therefore, you are going to get an inflated price. I think where people are not being rational is that if interest rates are low, that's because long term growth rate expectations are low. That's because people expect that kind of that there will be going to be considerable slowdown and contraction in economic growth at some point in some countries. You've got negative rates of. And so I think you've got these so you've got low discount rates, so, so high cap, kind of inflated cash flows, but at the same time, I think growth expectations over the next decade, I think for many companies at least, they will prove to be considerably inflated.

**Speaker1:** [00:15:38.90] Ok. And early stage vesting and later stage investing are very different when it comes to valuation. You know, traditional methods like discounted cash flow and those things don't really work in the early stage. But how do you characterize the difference between those two methodologies?

**Speaker2:** [00:15:54.71] Yes, send a book I said to my chapter on early stage companies, I still distinguish it as intrinsic and relative. But to do that quite differently, obviously, when you're looking at Relisten, for instance, you don't have any kind of cash flow or earnings or even often sales to think about, to say so. Quite often it's looking at relative transactions. And in the case of intrinsic kind of the framework I've proposed is not trying to locate the individual cash flows of the company. It's about projecting kind of five years out, 10 years out, what you'll be able to get out of the company at a later period when the company does have some performance metrics. For instance, sales of earnings, which can be which value can be anchored to, and then discounting the discounting that back to the present value. And what you typically find is lot of entrepreneurs, a lot of them will use relative value when thinking about valuations and comparable transactions. But many of the professionals, those that kind of work in these environments, et cetera, they will often use intrinsic valuation and discounted cash flow, which is it takes a bit more time. It takes more time to also get your head around that. But it's a kind of far more kind of fundamental approach and going to bring a bit more clarity and detail to a valuation.

**Speaker1:** [00:17:20.85] Great. And then oftentimes there are biases that investors bring to these valuations. What do you see happening out there in that area?

**Speaker2:** [00:17:28.58] Yes, in terms of biases, it's like we've covered I, I think had a perhaps bias in the recent 12 months has been I mean, I suppose everybody gets more depressed than in a down market and going to things kind of tend to kind of total over. So I know in the US you've obviously comes some of those growth markets, especially growth companies, have done very well here in the U.K. A kind of depression seems to have like almost kind of circled in on itself. And people seem to be not particularly positive about stocks. So I wouldn't say kind of more recently, we've seen anything particular in terms of behavioral biases that you really seem to see that during a depression or when the market is particularly for profit at the moment. I think for a lot of these growth, companies actually can valuations obviously high. But the days are like when you look at the the opportunities and the strike, the the opportunity for persistent structural growth of those businesses. There is justification to their valuations in many cases, but not all cases.

**Speaker1:** [00:18:38.59] I mean, I see when the last units that we have here, what else should we cover that we haven't?

**Speaker2:** [00:18:44.09] I think you've been pretty comprehensive in your questions, actually, so. Yeah, no, no. I think that there's a good question, certainly.

**Speaker1:** [00:18:52.79] Right. Well, how best for listeners to get back in touch with you?

**Speaker2:** [00:18:57.56] Well, I will be creating my own website, actually. So if you kind of Google the book, the company valuation playbook, hopefully that will come up as one of the top hits. I'm almost on LinkedIn as well. So you obviously feel feel free to send me any questions if you if you have some or if there's anything that if you do read the book, if you if there is anything that you don't feel is clear and perhaps I could add some clarity to.

**Speaker1:** [00:19:22.19] Great, we'll put those in the show notes. And I want to thank you for joining us today. Hope to have you back for a follow up soon.

**Speaker2:** [00:19:27.77] Okay. Thanks for your time.

**Speaker1:** [00:19:29.60] Investor contact helps investors interested in startup funding. In this podcast series, experienced investors share their experience and advice. You can learn more at Investor Connect, Doug. Paul Martin is the director of investor Canek, which is a 523 non-profit dedicated to the education of investors for early stage funding, all the opinions expressed by Hall and podcast guests are solely their own opinions and do not reflect the opinion of Investor Connect. This podcast is for informational purposes only and should not be relied upon as a basis for investment decisions.