

Valuation Is a Narrative Problem

Same numbers, different stories.



The Uber Paradox (2014)

Two elite investors built Discounted Cash Flow (DCF) models using the exact same public data. Both discounted cash flows perfectly. The difference wasn't arithmetic. The numbers were just the disagreement disguised as a math problem.

Valuation isn't a calculation. It's a story wrapped in numbers.

The 5 Stories Inside Every DCF

What are you actually betting on?



The Spreadsheet vs. Reality

Revenue Growth

A story about demand.
(How many customers are in that queue?)

Operating Margins

A story about competitive advantage. (Do you have pricing power, or are you discounting?)

Reinvestment Rate

A story about capital.
(How many new trucks do you need to buy to keep growing?)

Discount Rate

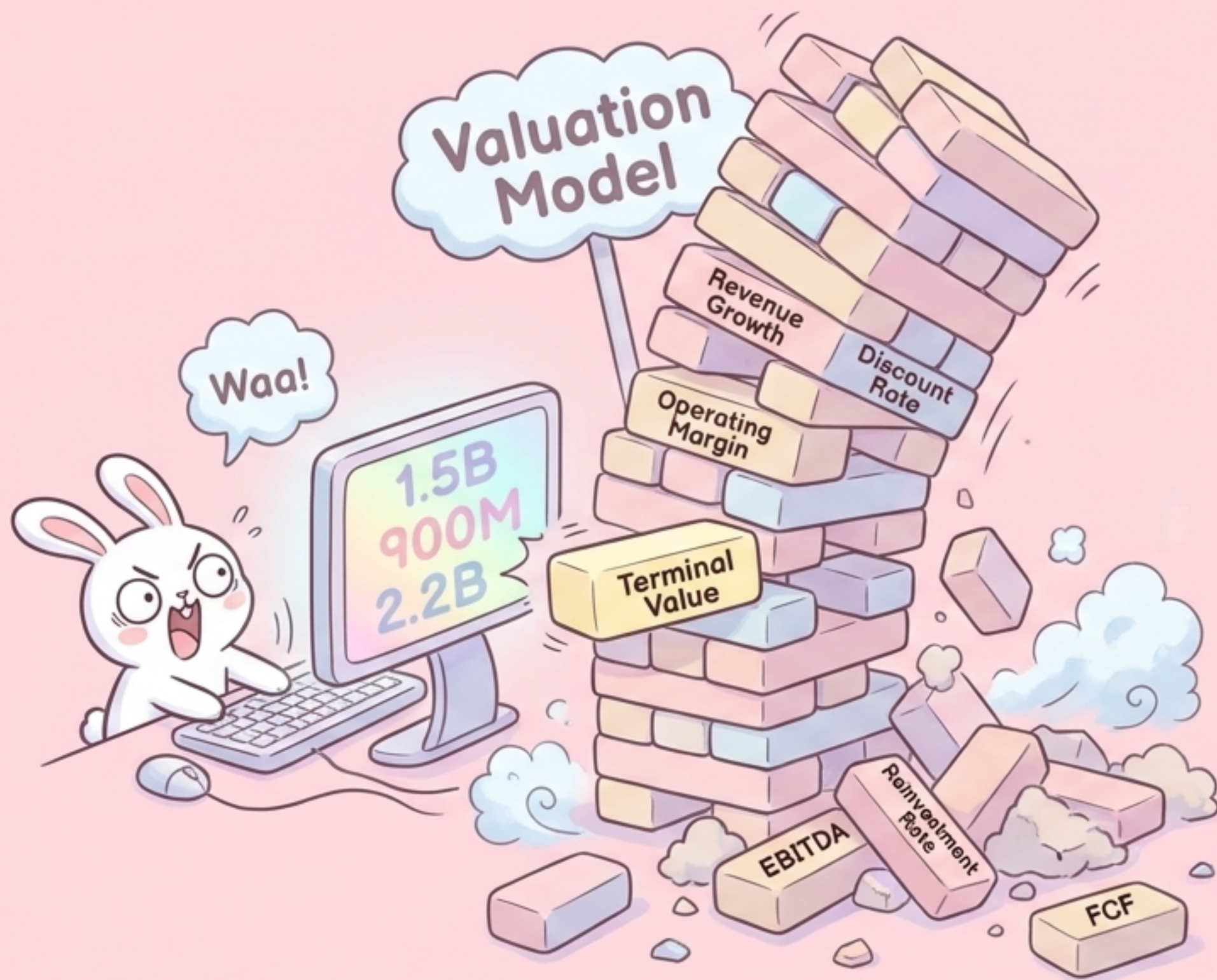
A story about confidence.
(How risky is this business model?)

Terminal Value

A story about maturity.
(What happens when the hyper-growth ends?)

Sensitivity Analysis

Finding the load-bearing wall.



The Illusion of Precision

A DCF produces a single number. That precision is a lie. If you are wrong about one core assumption, the math doesn't save you. You must ask: Which story choice is this valuation actually betting on?

The Fragility of Models

For Growth Companies: The model collapses if Revenue Growth or Terminal Value drops. The thesis is a bet on sustained momentum.

For Mature Companies: The model collapses if Operating Margins shrink. A 2% dip in margins destroys billions in equity.

The Golden Rule

If you can only be right about ONE assumption, which one is it? **Defend that wall.**

The Fudge Factor Trap

Where investors hide their disagreements.



Reverse-Engineering the Price

If your valuation is too low, it's tempting to fix it by lowering the discount rate to argue the company is less risky than the market thinks. This is rationalization, not analysis.

Discount Rate = Business Risk

Beta measures past stock price volatility. It does not measure future business reality.

The Gut Check

If the model says: 8% Discount Rate.

- ☒ - Would you personally lend this company money at 8%?
- ☒ - If you think there's a real chance they can't pay you back, the rate is too low.

Don't let the math justify a story you want to be true.

Who Computes vs. Who Narrates

The Division of Labor in Modern Investing



The Agent Computes

- Retrieves 10 years of financial data instantly.
- Builds flawless DCF math and scenario mechanics.

The Blindspot: It defaults to Wall Street Consensus. If you accept its valuation, you are outsourcing your judgment to the average opinion.

The Human Narrates

- Checks assumption consistency (e.g., You can't have 30% growth with 0% reinvestment).
- Judges uncertainty and competitive dynamics.

The Edge: You find the exact assumption where the consensus story is wrong, inject your thesis, and let the agent recompute.

The agent generates the baseline. You generate the **alpha**.

The Three Lenses of Valuation

Every valuation technique is a variation of these three frameworks.
Each has a specific utility, and a specific way it lies to you.



Intrinsic (DCF)

The Logic:



Value = Present value of future cash flows.

The Lie:



Decimal precision creates a false sense of certainty for unknowable futures.



Relative (Multiples)

The Logic:

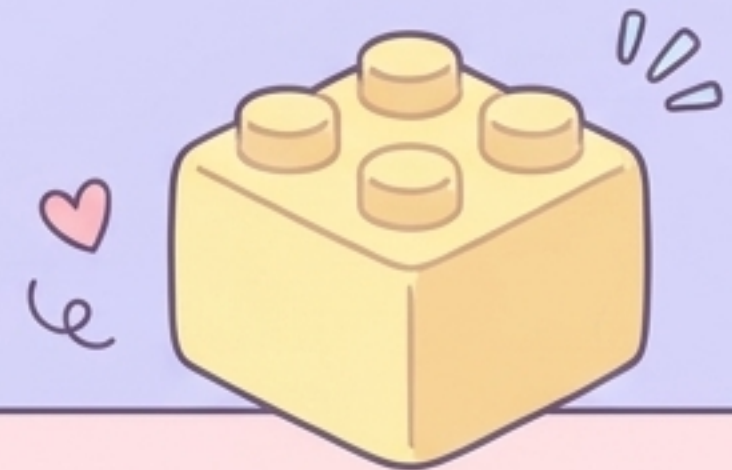


Value = What similar companies trade for (e.g., 15x earnings).

The Lie:



Anchors to market prices, masking when entire sectors are in a bubble.



Asset-Based

The Logic:



Value = Selling assets minus paying debts.

The Lie:



Treats the company as a pile of static objects, ignoring the value of a going operating concern.

Multiples Are Summaries, Not Answers

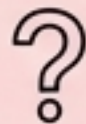
The **Compression Problem**: A multiple is a one-sentence summary of someone else's story. It compresses growth, margins, risk, and reinvestment into a single ratio.



Price-to-Earnings (P/E)

The most common shorthand.

Flaw: Ignores capital structure and debt entirely.



EV/EBITDA

Strips out debt and tax differences.

Flaw: Ignores real expenses like capital expenditures (capex).



Price-to-Free-Cash-Flow (P/FCF)

Grounded in actual cash available to shareholders.

Flaw: Highly volatile year-to-year based on investment cycles.



Price-to-Sales (P/S)

Used for pre-profit companies.

Flaw: Revenue without profitability is not inherently valuable.



The Trap of Relative Valuation

Cheap Relative to Expensive is Still Expensive



The Cisco Illusion (1999)



The Consensus:

Analysts argued Cisco was reasonably valued at 120x earnings because its tech peers traded at similarly high multiples.



The Reality:

On an absolute basis, the valuation required Cisco to grow earnings at 25-30% annually for a decade.



The Result:

That growth did not happen. The stock fell 80% and took over two decades to recover.

If the consensus story is **wrong**, multiples will not warn you. They will **confirm** the bubble.

Four Ways Agent Valuations Fail

Where Default Logic Breaks Down

1. Consensus as Original Thought

Agents pull analyst estimates, meaning their valuation simply reverse-engineers the current stock price. It's circular logic.



2. Terminal Value Hand-Waving



Agents default to 2-3% perpetual growth. This single, unexamined assumption often dictates 60-80% of the total valuation.

3. Discount Rate Blindness

Agents use CAPM and beta (historical price volatility) to calculate risk. But historical price stability does not equal future business safety.



4. Growth Extrapolation



Agents project recent high growth trends forward, ignoring total addressable market (TAM) limits and the gravity of mean-reversion.



Guardrails and The Damodaran Principle

Defeating Motivated Reasoning



Three Guardrails:

Pre-commitment

Write down the specific metrics that would prove your story wrong BEFORE you buy the stock.

Inversion

Ask your agent to build the strongest, most specific bear case. Generic risks do not count.

The Outsider Test

If questioning an assumption makes you defensive, your analysis is contaminated by emotion.

The Ultimate Rule

When the story changes, the valuation changes. The agent computes flawlessly. Your job is the honesty to tell a story you might not like, and the discipline to change it when reality contradicts it.