



Valuation: Understanding Discounts and Premiums

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Valuation: Understanding Discounts and Premiums

Essential insights for finance and accounting professionals

Discounts and premiums translate differences in rights, liquidity, and information into price. Apply them only when a subject interest differs from the benchmark value you started with (e.g., guideline public multiples or a control-based DCF). This article sets out a practical framework for choosing and applying valuation discounts and premiums, and for avoiding the most common ways they are misused.



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Why discounts and premiums exist



A 15% non-controlling stake in a private company valued at \$80 million is not necessarily worth \$12 million. Depending on how discounts and premiums are applied, or misapplied, the same stake might be valued at anywhere from \$6 million to \$12 million. The difference rarely reflects disagreement about the underlying business. It reflects discipline, or its absence, in handling adjustments to the base value.

Valuation begins with an economic benchmark—cash flows and risk (income approach), market comparables (market approach), or assets (cost approach). But the benchmark rarely mirrors the exact bundle of rights and constraints of the subject interest. Discounts and premiums adjust for those differences so the concluded value reflects what a market participant would pay for **this interest, under these conditions, on this date**.

Three drivers underpin nearly every adjustment:

1. **Control and governance** – Who decides strategy, capital allocation, dividends, and exits?
2. **Marketability (liquidity)** – How quickly and cheaply can you convert to cash?
3. **Information and protection** – What do you know and what safeguards do you have (tag/drag, veto rights, ROFR, board seats)?

Understanding Levels of Value

Valuation adjustments hinge on the level of value you start from. Common reference points include:

- **Enterprise value (control, marketable)** – Whole business under market participant assumptions, often from a DCF.
- **Equity value (control, marketable)** – Ownership of all shares with full governance rights.
- **Minority, marketable** – Price implied by public trading of small blocks; reflects liquidity but not control.
- **Minority, non marketable** – Typical for private company stakes with transfer restrictions; requires DLOM and possibly DLOC.
- **Strategic control** – Control plus buyer specific synergies (usually relevant in M&A pricing, not fair value).

Mapping your subject interest to the correct level avoids double counting and ensures adjustments are applied only when the starting point and target differ.

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The core toolkit



1. Control premium (CP)

A **control premium** is the incremental price for the ability to direct policies, cash flows, and exits. It is observed (imperfectly) in takeover transactions where acquirers pay above unaffected minority trading prices. Note that observed premiums embed synergies and competitive bidding effects, so they tend to overstate the pure control premium.

- **When it belongs:**

Transaction pricing and deal models where the buyer will obtain control and expects to extract control benefits (e.g., optimizing capital structure, divesting non-core assets).

- **When it does *not* belong:**

Many **financial reporting** fair value measurements, those governed by VVS, IFRS 13 and ASC 820 (the Vietnamese Valuation Standard, international and US fair value standards), for a **non-controlling** instrument; also avoid layering CP when your base measurement is already at a control level (e.g., DCF of the whole enterprise with market participant cash flows).

- **Synergy is not control:**

Buyer-specific synergies accrue to the particular acquirer and **should not** be baked into fair value, since fair value reflects what a typical market participant would pay, not what one strategic buyer might justify. Only synergies available to market participants broadly belong in a fair value measurement.

Relationship to DLOC. If you start from a *minority, marketable* base and need a control-level value, analysts often reference the algebraic link:

$$\text{DLOC} = \frac{\text{CP}}{1 + \text{CP}}$$

Example: a 25% control premium implies a **DLOC** \approx 20%. Conversely,

$$\text{CP} = \frac{\text{DLOC}}{1 - \text{DLOC}}$$

Practical tip: Do **not** impose both a CP and then later also a DLOC on the same base—they are inverse lenses around the same minority/control divide.

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2. Discount for lack of control (DLOC)

A **DLOC** reduces value from a control to a non control (minority) basis to reflect limited influence on dividends, strategy, and liquidity events.

- **Typical uses:** Converting a control-based enterprise or equity value (e.g., from an income approach that embeds control assumptions) down to a minority value when the subject interest lacks control.
- **Evidence sources:** Empirical proxies (e.g., control premiums implied by acquisitions), rights analysis (charter terms, shareholder agreements), and scenario modeling (probability weighted dividends/exit timing under current governance).

3. Discount for lack of marketability (DLOM)

The **DLOM** recognizes the cost of being locked into an illiquid investment (private shares, transfer restrictions, thin markets).

Measurement approaches:

- **Empirical studies:** Restricted stock and IPO analyses provide statistical ranges but require careful matching for size, profitability, growth, and holding periods.
- **Option-based models:** Treat illiquidity as the lost value of a “put” to sell (e.g., protective put / Chaffe), or as the cost of waiting until a liquidity event (Longstaff, Finnerty frameworks). Input realism (volatility, horizon, risk-free rate, dividends) is critical.
- **Simulation/calibration:** Monte Carlo to tie the DLOM to specific exit paths, information rights, and expected secondary sales.

Key determinants: Expected holding period, cash distributions while illiquid, volatility, size/quality of information, and transfer restrictions (ROFRs, consent rights).

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4. Other (less frequent adjustments)

- **Voting vs. non voting** share differentials. Discounts range from 0% to 5% unless a takeover is involved.
- **Blockage discounts** for large positions in thinly traded public names
- **Key person / customer concentration**—typically reflected in cash flows or discount rates rather than as a separate “plug” (avoid double counting)
- **Portfolio/structural discounts** at holding companies for leakages, tax friction, and governance layering

Start with the right base, then adjust—once

Your adjustment path depends on your **starting point**:

- **DCF of the whole enterprise** (market participant assumptions) → typically **control, marketable** basis for total invested capital. Convert to equity, then to minority if the subject lacks control, and finally to non marketable if illiquid.
- **Guideline Public Company (GPC) multiples** from unaffected trading prices → **minority, marketable** basis. If valuing a controlling stake, consider whether a CP is warranted (and defensible) or instead bring the DCF to bear as your control cross check.
- **Guideline Transaction Method (GTM)** → usually **control** (and often reflects some synergy). Be careful not to add a CP on top of control implied transaction multiples.

Multiplicative sequencing:

Value final = Base × (1 – DLOC) × (1 – DLOM) × (1 – Other discounts)

Never add percentages; addition overstates the effect.



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Starting method	Implied level of value	If subject is non-controlling	If subject is illiquid	Add a control premium?
DCF (entity, market-participant assumptions)	Control, marketable	Apply DLOC	Apply DLOM	No, already control
Guideline Public Company (GPC) multiples	Minority, marketable	Already minority, no DLOC needed	Apply DLOM	Only with caution; defensible if subject will obtain control
Guideline Transaction Method (GTM) multiples	Control (often synergy-tinged)	Apply DLOC; do NOT add CP	Apply DLOM	No, already control, possibly with synergy

A concise decision map

1. What rights does the subject have?

Control? If *no*, you are on a **minority** footing (or you need to apply a DLOC to a control base).

2. What is the baseline of your method?

- GPC → minority/marketable
- DCF (entity) → control/marketable
- GTM → control (possibly synergy tinged)

3. Is there a liquidity constraint consistent with market participant assumptions?

If yes, estimate **DLOM** based on realistic horizon and volatility.

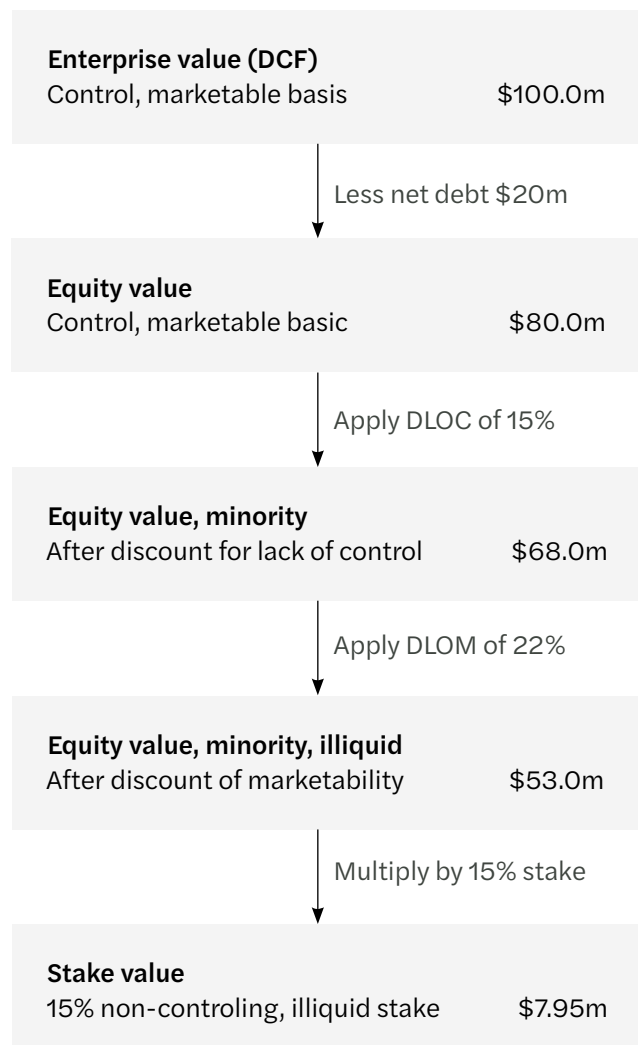
4. Are you double counting any risk already in cash flows or discount rate?

If risk is in the WACC or explicit scenarios, don't also insert a separate "discount" for the same thing.

5. Calibrate to observable prices when available.

If you have a recent, orderly transaction in the same instrument, reconcile your adjustments to that anchor.

- You value a private company via DCF at **\$100m enterprise value** (control/marketable).
- Less net debt **\$20m** => **Equity (control, marketable) = \$80m**.
- Subject: **15% non controlling** stake with transfer restrictions; expected liquidity **4 years**.





DLOC: Governance assessment and transaction evidence indicate a **DLOC of 15%** from control to minority.

DLOM: Option-based model calibrated to 4 year horizon and 35% volatility implies **DLOM of 22%**.

Audit note: Document how governance terms led to 15% (not 25%); archive your DLOM inputs, model, and sensitivity to horizon and volatility; reconcile to any secondary trades or prior rounds.

What auditors and boards look for

1. **Clear identification of the starting level of value** (control vs. minority; marketable vs. non marketable).
2. **Market participant basis** under IFRS 13/ASC 820: inputs and assumptions should be those a typical buyer and seller would use, not entity specific preferences.
3. **Method specific consistency:** No CP on GTM multiples; no DLOC if you already started from minority multiples.
4. **Evidence and calibration:** Point to empirical studies appropriately and, whenever possible, calibrate to observed transactions in the same or similar instruments.
5. **Robust sensitivity analysis:** Horizons, volatility, and distribution assumptions materially swing DLOM—show ranges and justify selections.
6. **No double counting:** If customer concentration increased your discount rate, don't add a standalone "concentration discount."

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Frequent pitfalls (and how to avoid them)

- **Adding, not multiplying, discounts.** Fix: Always compound multiplicatively.
- **Layering CP and using GTM multiples.** Fix: Recognize GTM is already control based.
- **Borrowing a DLOM from a generic range.** Fix: Tie horizon and volatility to your facts; cite the model/study; calibrate if there's a nearby trade.
- **Ignoring specific rights.** Fix: Read the charter and shareholders' agreement—tag/drag, ROFR, veto rights, liquidation preferences, and information rights can expand or reduce discounts materially.
- **Including buyer specific synergies in fair value.** Fix: Limit to market participant synergies or handle synergies in transaction pricing narratives, not fair value.
- **Overlooking tax and leakage at holdcos.** Fix: If valuing a holding company, reflect dividend taxes, costs, and structural subordination—often via a “holdco discount.”

How to quantify DLOM defensibly (a practical recipe)

1. **Set the holding period** to the realistically expected liquidity event (secondary sale, IPO, buyback).
2. **Estimate volatility** from guideline public peers adjusted for leverage and size; triangulate with historical private performance if relevant.
3. **Model cash flows while illiquid** (dividends, distributions).
4. **Select the framework** (e.g., protective put or restricted stock calibration) and compute the implied discount.
5. **Cross-check** against empirical study ranges for companies of similar size and profitability.
6. **Sensitivity table** (e.g., ± 1 year horizon; ± 5 – 10 pp volatility) for governance/audit.



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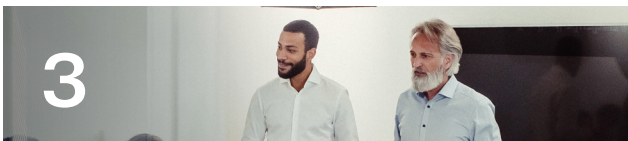
Regional and private market nuances (ASEAN/Vietnam context)



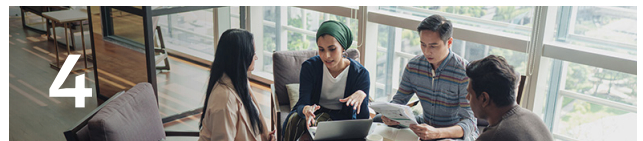
Thinner exit markets can lengthen expected holding periods and widen DLOMs versus mature markets.



Shareholder agreements often carry strong ROFRs/consents—read the fine print; a narrow buyer pool is a liquidity constraint.



Foreign ownership caps and licensing regimes may affect both control value (resulting in foreign shareholders not capable of holding majority ownership) and marketability (limiting number of potential buyers if cap is already reached); reflect these via rights analysis and horizon assumptions rather than blanket “country” add-ons.



Local financing conditions influence the *extractability* of control benefits (e.g., ability to lever, pay dividends), moderating any control premium narrative.

Discounts and premiums are a discipline, not a plug. Identify the level of value your method delivers, apply each adjustment only where the subject genuinely differs from that benchmark, and never apply the same adjustment twice. Done well, they make a valuation defensible to auditors, boards, and counterparties. Done casually, they introduce the very subjectivity they were meant to remove.

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