SN Valuation
NAV Valuation in Korea
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What is NAV? NAV stands for net asset value. For mutual funds, NAV is the market price for a share unit. What generates the NAV?

NAV is created by 1) asset-liabilities 2) gain/loss in share prices of investments 3) gain/loss in derivatives.

Assets are composed of cash balance, investments, receivables and derivatives. The cash balance changes according to the subscription and redemption. Also, settlement of derivatives and fee payments can change the cash balance.

Investments are calculated from the historical cost of the respective shares and does not change on a daily basis in conjunction with the market. Rather, the market movement is seen in the gain/loss of share prices.

Receivables are spot payments outstanding.

Derivatives are forwards for hedged funds. Similar to investments, the number is the historical cost of the respective forwards and does not change daily.

Liabilities are primarily redemptions payable, and the offsetting spot and forwards. The same dollar amount for spot and forwards are categorized as a liability.

Therefore, asset – liabilities is reduced to cash balance+investments+realized gain in forwards – realized loss – redemptions payables – fees payables.

The gain and loss in investments and derivatives are calculated using the change in the 1) foreign exchange rate for the investments and forwards and 2) change in the underlying mother fund shares for investments.

The key take away from NAV calculations is that like bonds, real estate and stocks, the valuation is equal to the initial capital + the cash flow generated from the capital. Cash flow, in this case, increased value for the investments, is the **ONLY** driver of NAV.

The asset management industry relies solely on value creation by investing in appreciating assets. If running a hedge fund, a short strategy can also create value.

Therefore, we need to invest in assets that generate cash at a rate higher than 1) the cost of owning the asset i.e. interest rate on loan to purchase asset 2) the cost of generating the cash flow i.e. operation is profitable 3) other investment alternatives compared to risk i.e. risk free bonds vs. junk bonds.