

FINAL EXAMINATION

June 2016

P-20(FABV)**Syllabus 2012****Financial Analysis & Business Valuation**

Time Allowed: 3 Hours

Full Marks: 100

*The figures in the margin on the right side indicate full marks.**Please: (1) Answer all bits of a question at one place.**(2) Open a new page for answer to a new question.***Section - A***In this section Answer Question No. 1(a) and 1(b) which is compulsory***1. (a)** Answer the following:

2×6=12

- (i) From the following information, compute the Trend Ratio (%) of Net Sales and comment about the trend in Net Sales.

(₹ in lakhs)

Particulars	2010-11	2011-12	2012-13	2013-14	2014-15
Net Sales (₹ in lakhs)	5,959	6,500	6,809	6,649	7,262

- (ii) Comment on the Fixed Assets Turnover Ratios of both the companies on the basis of the following information:

(₹ in lakhs)

	Company-A		Company-B	
Particulars	2013-14	2014-15	2013-14	2014-15
Sales	250.00	300.00	450.00	750.00
Less Excise	31.25	37.50	56.25	93.75
Net Sales	218.75	262.50	393.75	656.25
Gross Fixed Assets	2,500.00	2,800.00	3,500.00	4,000.00
Less Depreciation	1,500.00	2,000.00	1,250.00	1,500.00
Net Fixed Assets	1,000.00	800.00	2,250.00	2,500.00

Please Turn Over

(iii) The following information has been extracted from the Annual Report, 2015 of XYZ Ltd:

(₹ in lakhs)

Particulars	2013-14	2014-15
Net Sales	5,108	5,054
Operating expenses	3,427	4,071
Operating Profit	1,681	983
Total Assets	14,948	15,520
Return on Assets (ROA)	11.25%	6.33%

You are required to find out the drivers that are responsible for a sharp decline in ROA of the company in 2014-15.

- (iv) If value of B Ltd. is ₹ 50 lakhs, T Ltd. is ₹ 20 lakhs, and on merger their combined value is ₹ 94 lakhs and B Ltd. receives premium on merger ₹ 13 lakhs, then what is the synergy gain?
- (v) SMITH LTD. has PAT of ₹ 400 lakh with extra ordinary income of ₹ 60 lakh. The cost of capital and the applicable tax rate of the company are 20% and 30% respectively. What is the value of SMITH LTD.?
- (vi) Market price per share is ₹ 160; Dividend per share is ₹ 40 and Earnings per share is ₹ 55, price earnings ratio will be _____.

(b) State whether the following statements are true or false:

1×8=8

- (i) Valuation, Sensitivity analysis and presentation are not a part of Financial Modelling Process.
- (ii) Financial analysis which is made by prospective investors is known as internal analysis.
- (iii) If Z-Score is greater than 2.99 it is predicted that the firm belongs to bankrupt class.
- (iv) Whenever the yield on a bond is more than coupon rate, the bond will be trading at a discount.
- (v) A brand is nothing but a glorified product name; hence it has no value.
- (vi) Valuing a firm using discounted cash flow method is conceptually different from valuing a capital project using present value method.
- (vii) Higher the Dividend Payout Ratio of a company, higher is its Price/Earnings (P/E) Ratio.
- (viii) If a company has built up intangibles over a period of time, then it can show them in its Balance Sheet and thus, the book value of the company's share will increase.

Section B*In this section, Answer any five questions from the following*

2. (a) Vedika Ltd. finds on 31st December, 2015 that it is short of funds with which to implement its branch expansion programme. On 1st January, 2015, it had a bank balance of ₹ 1,80,000 in its current account. From the following information, prepare a statement for the Board of Directors to show how the overdraft of ₹ 68,750 at 31st December, 2015 has arisen: 10

Figures as per Balance Sheet
(as on 31st December)

	2014	2015
	(₹)	(₹)
Fixed Assets	7,50,000	11,20,000
Stock and stores	1,90,000	3,00,000
Debtors	3,80,000	3,65,000
Bank Balance/(Overdraft)	1,80,000	(68,750)
Trade Creditors	2,70,000	3,50,000
Share Capital (in shares of ₹ 10 each)	2,50,000	3,00,000
Bills Receivable	87,500	95,000

The profit for the year ended 31st December, 2015 before charging depreciation and taxation amounted to ₹ 2,40,000. The 5,000 shares were issued on 1st January, 2015 at a premium of ₹ 5 per share. ₹ 1,37,500 was paid in March 2015 by way of income tax including tax on distribution of dividend. Dividend was paid as follows for 2014 (final) on the capital on 31-12-2014 @ 10% less tax 25%. For 2015 (interim) 5% on capital on 31st March, 2015 free of tax.

- (b) The operating and cost data of ABC Ltd. are:

Sales ₹ 20,00,000

Variable Costs ₹ 14,00,000

Fixed Costs ₹ 4,00,000 (including 15% interest on ₹ 10,00,000)

You are required to

- Calculate its operating, financial and combined leverage and
- determine the additional sales to double its EBIT.

3+3=6

3. (a) The following financial statements have been extracted from the Annual Report 2015-16 of METCALF TEXTILES Ltd. a largest Textile Company, having a strong presence in over 80 countries in the world.

The company wants to keep its shareholders happy by giving them a fair rate of return. The company is using return on equity (ROE) as one of the metrics of performance evaluation for determining the return for shareholders. Due to intense competition, in recent years, its ROE is under pressure and to maintain the level of ROE, the company is to change its business Model-in that, it is varying its, margin, assets utilization and leverage.

Please Turn Over

You are required to:

- (i) Carryout the DuPont Analysis considering the financial parameters given below and show how the return on equity (ROE) of the company (Metcalf Textiles Ltd.) is changing due to change in its Margins, Assets utilisation and Leverage over the period of four years.
- (ii) Give your comments on the trend of the said parameters. 8+2=10

Statement of Profit & Loss for year ended March 31,

(Amount in ₹ crore)

	2013	2014	2015	2016
Total revenue	7998	8992	9976	11804
Profit before tax	1855	1612	1990	2817
Profit after tax	1514	1345	1574	2110
Dividend	225	315	225	225
Tax on dividend	37	51	36	38
Retained earnings	1252	979	1313	1847

Balance Sheet as at 31st March,

(Amount in ₹ crore)

	2013	2014	2015	2016
Equity and Liabilities				
1. Shareholders' fund				
a. Share capital	225	225	225	225
Reserves and Surplus	8055	9034	10347	12194
2. Non-current liabilities:				
Loan Funds	7	617	17	1352
3. Current liabilities				
Deferred Tax	<u>251</u>	<u>296</u>	<u>324</u>	<u>392</u>
	<u>8538</u>	<u>10172</u>	<u>10913</u>	<u>14163</u>
Assets				
1. Non-current assets:				
Fixed Assets	3774	4369	4685	5276
2. Non-current investments				
Investments	371	799	1449	3642
3. Current assets	<u>4393</u>	<u>5004</u>	<u>4779</u>	<u>5245</u>
	<u>8538</u>	<u>10172</u>	<u>10913</u>	<u>14163</u>

- (b) The following information has been extracted from the records of SITERAZE Ltd. as on 31st March, 2016:

(Amount in ₹ lakh)

Equity Share capital (of ₹ 10 each)	800
Sales (net)	4000
Market value of Equity Share (₹ 8 each)	640
Working Capital	(400)
Total Assets	2800
Retained Earnings	200
EBIT	472
Book Value of Total Debt	1800

Required:

Calculate, the Z-Score of Siteraze Ltd. using ALTMAN'S (1968) MODEL and comment on it. 5+1=6

4. The Finance manager has been asked to make a projected statement of profit and loss of Pure Cable Limited for the next F.Y. 2016-17 so that the company can make a budget for F.Y. 2016-17. For this purpose, the following information has been collected by the finance manager:

Statement of profit and loss of Pure Cable Limited for the year ending on March 31,

Particulars	(₹ in lakhs)	2015	2016
Income			
Revenue from Operations (gross)		21,826.40	24,235.30
Less: Excise Duty		1,184.80	1,528.50
Revenue From Operations (Net)		20,641.60	22,706.80
Other Income		319.90	241.70
Total Revenue		20,961.50	22,948.50
Expenses			
Cost of Materials Consumed		15,769.50	17,129.20
Purchase of Stock-in-Trade		24.00	60.40
(Increase)/ Decrease in Inventories of Finished Goods, Work in Progress and Stock-in-Trade		126.90	(296.80)
Employee Benefit Expenses		260.70	133.80
Depreciation, Amortization and Impairment		394.70	466.30
Other Expenses		2,234.60	2,671.50
Total Expenses		18,810.40	20,164.40
Profit Before Interest and Tax		2,151.10	2,784.10
Less: Interest		663.37	583.04
Profit Before Tax		1,487.73	2,201.06
Less: Tax @ 34%		505.83	748.36
Profit After Tax		981.90	1,452.70

Additional Information:

- Gross Revenue from Operations will increase by the same rate as it increased from F.Y.2014-15 to F.Y. 2015-16.
- As per the recent Union Budget, the Excise Rate on the company's product has been increased to 6.50% for the F.Y.2016-17 and the corporate income tax rate will remain unchanged at 34% (including cess/surcharge as applicable).
- Seeing the past trend, other incomes will be reduced by 5%.
- It is strongly felt that the expenses to sales ratio of F.Y.2015-16 for all expenses (except interest and taxes) will remain unchanged for F.Y.2016-17.

(e) Interest expense will reduce by 2%.

Assuming that you are the finance manager of the company, you are required to make Projected Statement of Profit and Loss for the F.Y.2016-17 as per the data given above. 16

5. A Limited and B Limited are in negotiations in which A Limited has expressed the desire to acquire B Limited and it is decided that A Limited will acquire B Limited. For this, purpose, the following information has been extracted from the books of both the companies for F.Y.2015-16.

		(₹ in lakhs)	
Particulars	A Limited	B Limited	
Statement of Profit and Loss:			
Revenue from Operations	1,200	630	
Less:			
Cost of materials consumed, net of expenses capitalized	634	280	
Other Operating Expenses	62	32	
Interest	10	5	
Depreciation and Amortization	64	75	
Operating Profit	430	238	
Net Non-Operating Income	42	27	
Profit Before Tax	472	265	
Tax	160	90	
Profit After Tax	312	175	
Balance Sheet:			
Share Capital (Face value of Shares of both the companies- ₹ 10)	300	200	
Reserves and surplus	3,210	1,356	
Non-Current Liabilities	440	104	
Current Liabilities	1,235	750	
Total Liabilities	5,185	2,410	
Net Fixed Assets	2,985	1,850	
Non-Current Investments & Other Non-Current Assets	575	355	
Current Assets	1,625	205	
Total Asset	5,185	2,410	
Additional Information:			
Promoters holding in the Company	40%	30%	
Free Float Market Capitalization			
(Assuming that promoters shares are not available for trading in the market)	₹ 3,150-00	₹ 1,400-00	

In a joint meeting of the directors of both companies, the following decisions are taken:

- The swap ratio will be decided by considering the following parameters with the weights as given below:
 - Book Value 25%
 - Market Price 40%
 - EPS 25%
 - Net Profit Ratio 10%
- All assets and liabilities will be taken over by A Limited at book values.
- The combined profit will increase by 10% due to synergy gains arising because of higher scale of operations.

- (iv) It is expected that the market will look this decision of A Limited as 'a value creator' decision and consequently, it is expected that A Limited's P/E Ratio will increase by 10% from its existing level after the acquisition of B Limited.

Given the above information, you are required to compute assuming that the acquisition will be completed as per the terms given.

- (a) The Swap Ratio
 (b) Book Value per share of A Limited after acquisition
 (c) Earnings per share of A Limited after acquisition
 (d) Market Price of A Limited's share after acquisition

7+3+3+3=16

6. (a) The following are the summarized balance sheets of two companies, Radha Ltd. and Soami Ltd. as on 31.03.2016:

Liabilities	Radha Ltd.	Soami Ltd.	Assets	Radha Ltd.	Soami Ltd.
Equity Shares of ₹ 10 each	15,00,000	10,00,000	Goodwill	2,00,000	1,00,000
Reserves	3,00,000	2,00,000	Net Tangible Block	17,00,000	14,00,000
10% Debentures	6,00,000	4,00,000	Current Assets	8,00,000	6,00,000
Creditors	3,00,000	5,00,000			
	27,00,000	21,00,000		27,00,000	21,00,000

Additional information:

- Assets are to be revalued as follows-

Particulars	Radha Ltd.	Soami Ltd.
Revaluation of Tangible Block	21,00,000	12,00,000
Revaluation of Current Assets	10,00,000	4,00,000
- Average annual profits for three years before charging debenture interest:
 Radha Ltd. ₹ 4,50,000; Soami Ltd. ₹ 3,10,000
- Goodwill is to be valued at three year's purchase of average super profits for 3 years. Such average is to be calculated after adjustment of depreciation at 10% on the amount of increase/decrease on revaluation of fixed assets. In case of Soami Ltd. claims of ₹ 10,000 which was omitted, is to be adjusted against its average profit. Income tax is to be ignored.
- Normal profit capital employed is to be taken at 12%, capital employed being considered on the basis of net revalued amount of Tangible assets.

Ascertain the value of Goodwill of Radha Ltd. and Soami Ltd.

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- (b) Dayal Ltd. furnishes the following information relating to the previous three years, and request you to compute the value of the brand of the company:

(₹ in lakhs)

Particulars	2013	2014	2015
Profit before interest and tax	75.00	85.25	150.00
Loss on Sale of Assets	3.00	--	18.00
Non-operating income	12.00	7.25	8.00

Inflation was 9% for 2014 and 15% for 2015. If the capitalization factor considering internal and external value drivers to the brand is 14. Determine the brand value.

6

Assume an all inclusive future tax rate of 35%.

7. (a) For Goal Ltd. the FCFE projected for next 3 years are stated below along with the immediately past year FCFE. You are required to value equity share by DCF approach. From Year 4 FCFE is expected to grow at 3% p.a. Cost of equity is measured at 15% p.a. Number of shares outstanding is 1,00,000. 8

	Past Year	Projected		
		Year 1	Year 2	Year 3
FCFE (₹ Lakhs)	160	180	200	220

Discounting Factor @ 15% p.a. Year1 = 0.869565, Year 2 = 0.756144, Year 3 = 0.657516.

- (b) Calculate Economic value added (EVA) with the help of the following information of Moon Ltd.: 4
 Financial leverage: 1.4 times;
 Equity capital ₹ 170 lakhs;
 Reserve and surplus ₹ 130 lakhs;
 10% debentures ₹ 400 lakhs;
 Cost of equity: 15%
 Income tax: 30%
- (c) Sun Ltd. has announced issue of warrants on 1:1 basis for its equity shareholders. The warrants are convertible at an exercise price of 12. Warrants are detachable and trading at ₹ 7. What is the minimum price of the warrant and what is the warrant premium if the current price of the stock is ₹ 16? 4

8. Write a short note on any four of the following:

4×4=16

- Quality of Earnings
- Methodology of Brand Valuation
- Human Resource Accounting
- Off-Balance Sheet Financing
- Hostile Takeover Bids