



VALUE CREATION FRAMEWORK



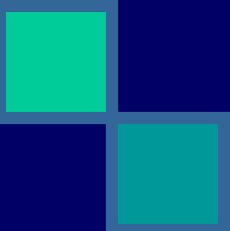

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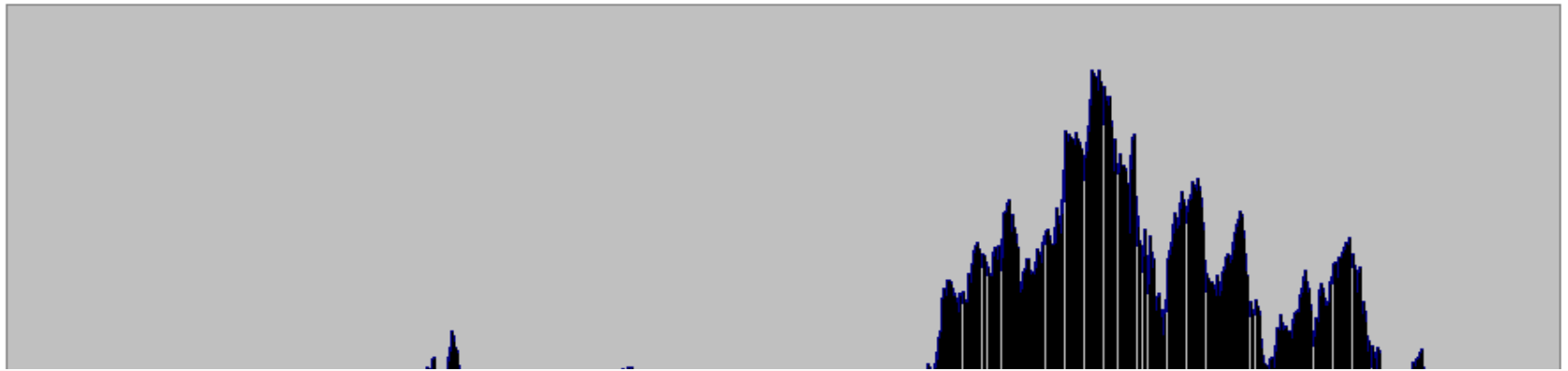
Course ...

- Content and Evaluation is largely left to the faculty ...
- Content is usually a mix of theory and practical inputs
- Evaluation is usually a mix of exams, quizzes, and assignments
- Take Home Assignment has been detailed in your course material
- Class Discipline – Powerpoint Slides, Timeliness, Mobiles, Laptops, Grades / Marks, Deadlines, Rules / Regulations, etc.



What is Value?

- 
- Liquidation Value
 - Operational (Going Concern) Value
 - Historical Value
 - Replacement Value
 - Relative Value (interlinked with above)
- 



Valuation of a asset or resource depends on two key issues:

- (a) Whose perspective are you looking at?
- (b) What is the purpose of valuation?

Ram needs your help ...

Year 2001

- He has INR 40 Million of Investible Funds ...
- Decides to invest in Real Estate ...
- Picks Four Cities ...
- Amsterdam, Boston, Chennai, and Dubai
- Picks an apartment worth INR 10 Million in each place

City	A	B	C	D
Investment in 2001	10	10	10	10

Which City-Apartment (or Investment) of Ram has created value?

City	A	B	C	D
Investment in 2001	10	10	10	10

Updated ...

City	A	B	C	D
Investment in 2001	10	10	10	10
Rent in 2007	0.4	1.3	0.1	0.5
Market Value in 2007	34	11	21	7
Market Value-to-Rent Ratio	85	8.5	210	14
Market Value-to-Investment Ratio	3.4	1.1	2.1	0.7

Jargons in Corporate Context ...

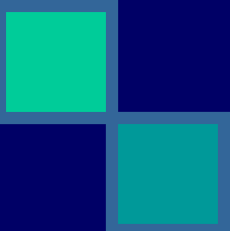

Corporate Context	A	B	C	D
Networth of the Firm (or Book Valu	10	10	10	10
Rent in 2007	0.4	1.3	0.1	0.5
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Jargons in Corporate Context ...

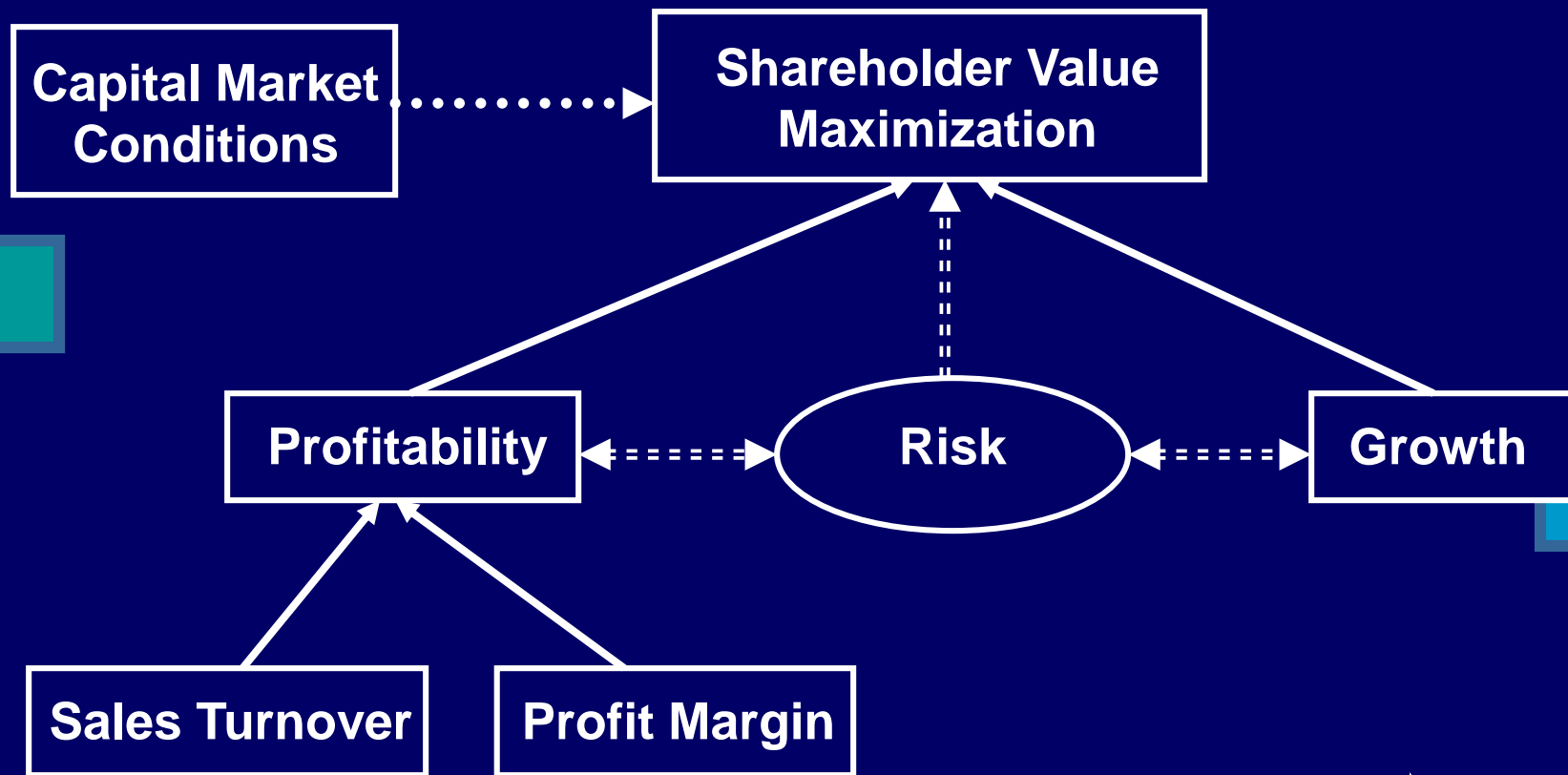
Corporate Context	A	B	C	D
Book Value per Share	10	10	10	10
Earnings Per Share (EPS) in 2007	0.4	1.3	0.1	0.5
Market Price (MP) per Share in 2007	34	11	21	7
P/E Ratio	85	8.5	210	14
P/BV Ratio	3.4	1.1	2.1	0.7



Importance of Market Value

- 
- Factors influencing shareholder value
 - Profitability
 - Growth
 - Risk
 - Capital Market Conditions
 - Can we put this in a framework and find measures?
- 

Valuation Framework ...



Source: Doctoral Dissertation, title '*Financial Performance and Diversification Strategy of Indian Business Groups*', Indian Institute of Management Calcutta, March 2001, <http://ssrn.com/abstract=1021148>.

Value Maximization Measures

- If 'n' is the number of equity shares
- Earnings Per Share (E.P.S.) = PAT/n
- Market Capitalization = (Market Price per share) x n
- Book Value of Equity (BV) = NW/n
- Price-to-Earnings Per Share (P/E Ratio)
= Market Price per Share/EPS = Market Capitalization/PAT
- Price-to-Book Value Per Share (P/BV Ratio)
= Market Value per Share/BV per share
= Market Capitalization/Net Worth



■ Shall we value some firms ...

- Infosys Technologies

Market Price is 1,601 and P/BV ratio is 8.2

- Colgate Palmolive

Market Price is 382 and P/BV ratio is 18.5

- Tata Steel

Market Price is 839 and P/BV ratio is 3.5

- Essar Steel

Market Price is 47 and P/BV ratio is 1.3

- Shree Rama Multi Tech

Market Price is 8 and P/BV ratio is 0.1

Shall we value some firms ...

3/12/2007	Price	BV	P/BV	EPS	P/EPS
Infosys	1601	195	8.2	73.3	22
Colgate Palmolive	382	21	18.5	15.9	24
Tata Steel	839	240	3.5	60.1	14
Essar Steel	47	37	1.3	5.5	9
Shree Rama	8	64	0.1	-14.5	
Zenith Exports	84	170	0.5	0.1	1197

Shall we value some firms ...

Zee Telefilm (in 1999, 2002, and 2007)

- Dec-1999 was period when stock market was on a bull run especially for IT and Media sectors ... then (?)
- Profitability (+, −, and 0)
- Growth (+, −, and 0)
- Risk (−, −, and 0)
- Capital Market Conditions (+, −, and 0)
- Result: Prices moved from 1900 to 70 to 370
- P/BV moved from 22 to 0.7 to 7
- Similarly, we can do it for other firms ...
- Note: In 2006, Zee Tele was split into Zee Entertainment and Zee News

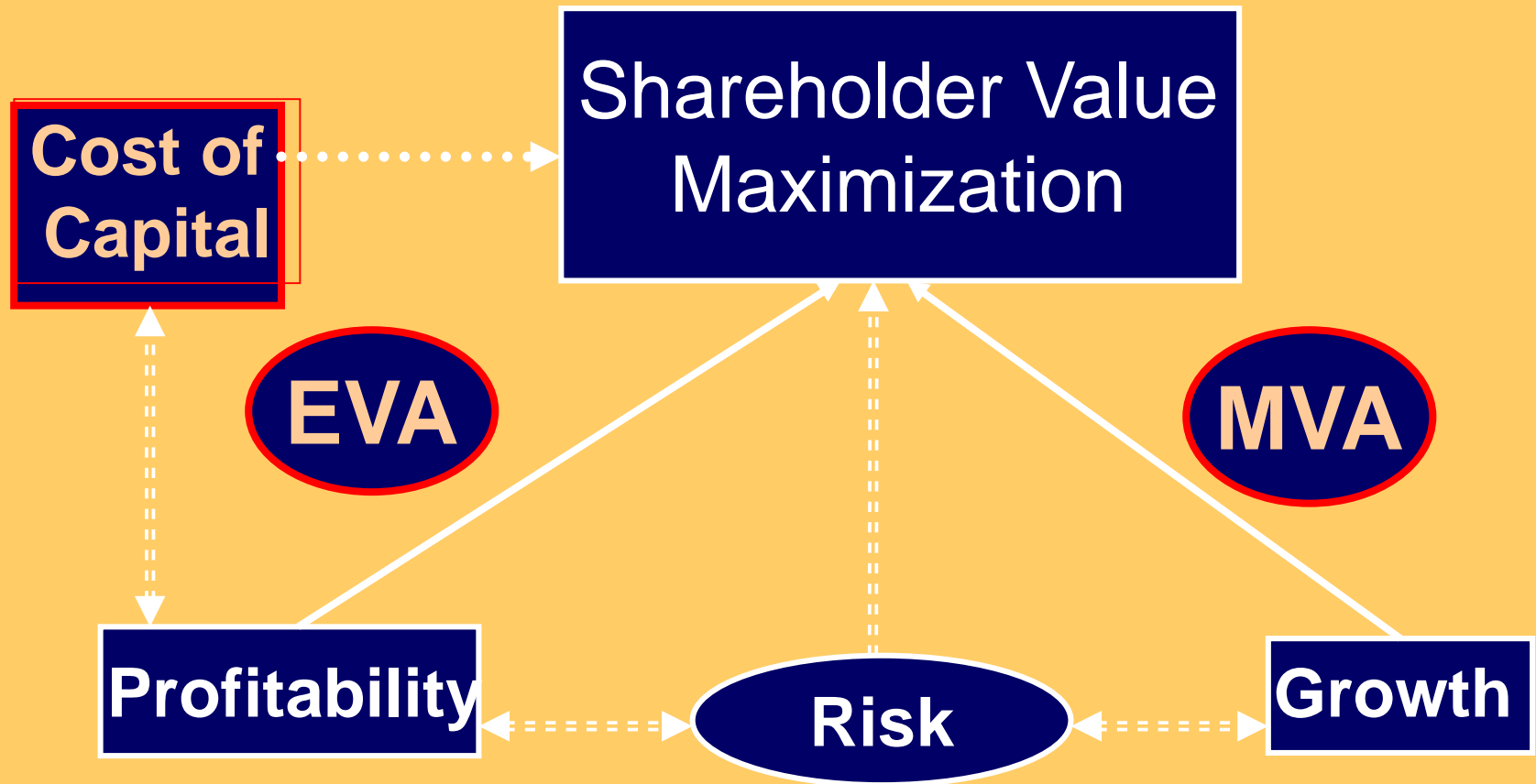
India's Tyre Sector

Performance Measure	Apollo Tyres	Falcon Tyres	TVS Srichakra	Vikrant Tyres
Growth Measure (CAGR _{TA})	12.56	11.10	18.72	32.43
Profitability Measure (ROA)	9.80	9.48	15.58	7.90
Profit Margin Measure (NPM)	3.36	2.51	5.30	2.83
Asset Utilization Measure (STA)	1.53	1.97	2.15	1.44
Risk Measure (VROA)	0.11	0.22	0.11	0.33
Market-to-Book Value Ratio	1.03	0.40	1.44	0.83
Tobin's Q Ratio (approximate)	0.84	0.62	1.05	0.77
Sales	1323	99	140	377
Market Capitalization	291	7	30	46

Note:

1. **Data Source for Computation: CMIE-PROWESS**
2. **Time Period of Study is FY 1997-2000 (mean of 4 years)**

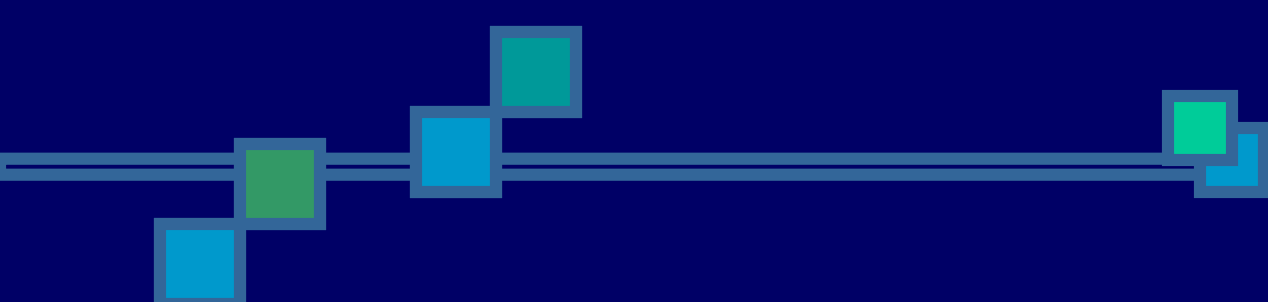
Can we connect this to Costs or EVA ...



→ Market Capitalization = EVA + Present Value (of Future EVAs) ...


→ Market Capitalization = EVA + MVA ...

The Four Different Categories		Example
EVA Positive	MVA Negative	?
EVA Positive	MVA Positive	?
EVA Negative	MVA Positive	?
EVA Negative	MVA Negative	?

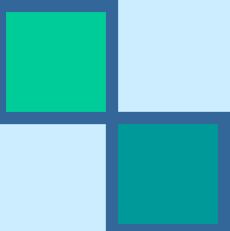


		Remarks
EVA Positive	MVA Negative	Firms not able to adjust to environment changes
EVA Positive	MVA Positive	
EVA Negative	MVA Positive	Firms with value accumulation or future dependent
EVA Negative	MVA Negative	Organizations with a different goal (not SVM)





What was the purpose of this discussion?

- 
- Accept Market Capitalization as the goal (of the firm)
 - Understand the factors driving Market Capitalization; and the way they do it
 - Link EVA, MVA, NPV and Capex to the Valuation of the Firm
 - Next Sessions: Different Approaches to Valuation & Equity Discounted Cash Flows
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