CBCS SCHEME

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16MBAFM406

Fourth Semester MBA Degree Examination, Dec.2018/Jan.2019
Corporate Valuation

Time: 3 hrs. Max. Marks:80

Note: *1. Answer any FOUR full questions from Q.No.1 to 7.*
2. Q.No. 8 is compulsory.
3. P.V. table is permitted.

Important Note : 1. On completing your answers, compulsorily draw diagonal cross lines on the remaining blank pages.
2. Any revealing of identification, appeal to evaluator and /or equations written eg, 42+8 = 50, will be treated as malpractice.

1 a. What do you mean by Economic profit? **(02 Marks)**

b. The current dividend on an equity share of international computers limited is Rs.3. The present growth rate is 50%. However, this will decline linearly over a period of 10 years and then stabilize at 12%. What is the intrinsic value per share of international computers limited, as per 'H' dividend discount model, if investors require a return of 16%? **(06 Marks)**

c. Briefly explain different enterprise valuation multiples. Give examples. **(08 Marks)**

2 a. Outline the different attributes of intangible assets. **(02 Marks)**

b. Discuss the five broad approaches for valuing a company. **(06 Marks)**

c. Moon is growing at an above average rate. It foresees a growth rate of 20% per annum in free cash flows to equity holders in the next 4 years. It is likely to fall to 12% in the next two years. After that, the growth rate is expected to stabilize at 5% per annum. The amount of free cash flow (FCFE) per equity share at the beginning of current year is Rs.10. Find out the maximum price at which an investor, follower of the free cash approach, will be prepared to buy the company's shares as on date, assuming an equity capitalization rate of 14%? **(08 Marks)**

3 a. What is an efficient market? **(02 Marks)**

b. Zenith company's ROIC is 18% and its 'g' is 12%. Zenith's depreciation and amortization charges (DA) is 10%, tax rate 30%, WACC is 14%. Determine EV to EBITDA multiple. **(06 Marks)**

c. List and the explain steps involved in developing financial forecasts. **(08 Marks)**

4 a. What are the sources of bias in valuation? **(02 Marks)**

b. Modern Ltd, after-tax operating margin is 12% and growth rate is 11%. Its reinvestment rate is 70% and its WACC is 13%. Compute the EV to sales multiple. **(06 Marks)**

c. The following information is available for Tejas company:

ROE	= 25%
Cost of Equity (K_e)	= 17%
Dividend payout ratio	= 50%
Book value per share	= 70
Net profit margin	= 10%
g	= 12.5%

Calculate the following for Tejas company:
i) P_0/E_1 ii) P_0/B_0 iii) P_0/S_0 iv) Value ratio. **(08 Marks)**

5 a. Bring out the limitations of the DCF approach. **(02 Marks)**
b. What are the common misconceptions about the efficiency market hypothesis? **(06 Marks)**
c. Discuss briefly the three levels of valuing a company as per strategic approach to valuation. **(08 Marks)**

6 a. What do you mean by synergy? **(02 Marks)**
b. Discuss the steps involved in relative valuation. **(06 Marks)**
c. The profit and loss account and balance sheet of Laxmi Corporation for 2 years (year 1, year 2) are given below.

Profit and loss Account (in million)		
Particulars	Year 1	Year 2
Net sales	5600	6440
Income from marketable securities	140	210
Non-operating income	70	140
Total income	5810	6790
Cost of goods sold	3220	3780
Selling and administration expenses	700	770
Depreciation	350	420
Interest expenses	336	392
Total cost and expenses	4606	5362
PBT	1204	1428
Tax provision	364	448
PAT	840	980
Dividend	420	560
Retained Earnings	420	420

BALANCE SHEET		
Equity capital	2100	2100
Reserves and surplus	1680	2100
Debt	2520	2940
	6300	7140
Fixed assets	4200	4550
Investments	1260	1400
Net current assets	840	1190
	6300	7140

Assume a tax rate of 40%.
i) What is the EBIT for year 2?
ii) What is the tax on EBIT for year 2?
iii) What is the NOPLAT for year 2?
iv) What is the Free Cash Flow to the Firm (FCFF) for year 2? **(08 Marks)**

7 a. Mention the reasons for using P/E multiple in relative valuations. **(02 Marks)**
b. Discuss the guidelines for corporate valuation. **(06 Marks)**
c. 'Zero' Ventures, a PE investor is considering investing 5000 million in the equity of 'Hero', a start-up IT company. Zero's required return from this investment is 35% and its planned holding period is 5 years. Hero has projected an EBITDA of 7000 million for year 5. An EBITDA multiple of 6 for year 5 is considered reasonable. AT the end of year 5, Hero is likely to have a debt of 2500 million and a cash balance of 800 million.
i) What ownership share in 'Hero' should 'zero' ventures ask for?
ii) What is the post-money investment value of the firm's equity?
iii) What is the pre-money investment value? **(08 Marks)**

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8 **CASE STUDY**

'M' corporation is expected to grow at a higher rate for 4 years; thereafter the growth rate will fall and stabilize at a lower level. The following information has been assembled:

Base Year (Year 0) Information

Revenues	3000 million
EBIT	500 million
Capital expenditure	350 million
Depreciation	250 million
Net working capital as a percentage of revenues	25%
Corporate tax rate (for all time)	30%
Paid-up equity capital (10 par)	400 million
Market value of debt	1200 million

Input for the High Growth phase	
Length of high growth phase	4 years
Growth rate in revenues, depreciation, EBIT and capex	20%
Net working capital as a percentage of revenues	25%
Cost of debt (pre-tax)	13%
Debt equity ratio	1:1
Risk free rate	11%
Market risk premium	7%
Equity beta	1.129

Inputs for the stable growth period	
Expected growth rate in revenues and EBIT	10%
Net working capital as a percentage of revenues	25%
Cost of debt (pre-tax)	12.14%
Risk-free rate	10%
Market risk premium	6%
Equity beta	1
Debt-equity ratio capital expenditure are offset by depreciation	2:3

Required:

i) What is the WACC for the high growth phase and the stable growth phase?

ii) What is the value of the firm? **(16 Marks)**

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