

JAIPURIA INSTITUTE OF MANAGEMENT, NOIDA

PGDM / PGDM (M) / PGDM (SM)

IV TRIMESTER (Batch 2021-23)

END TERM EXAMINATION, NOVEMBER 2022

Course Name	Corporate Valuation	Course Code	20224
Max. Time	2 hours	Max. Marks	40 MM

INSTRUCTIONS:

- This is an open book exam. Students can bring the textbook. They can use a calculator.
- Workings should form part of the answers.

Case Study (40 marks)

Prasthan Ltd (P) was established in 1995 to manufacture textile machinery. The management has estimated that Prasthan's sales have grown at about 11% per year, and profit after tax at 9%.

P's top management has chalked out an expansion plan to reduce its earnings instability. The company laid down three-pronged strategy to go for proposed expansion. First, the company should focus on technology up-gradation and capacity expansion. Second, the management is evaluating the possibility of bringing more value-added products in its product portfolio. Third, it is seriously thinking of replacing some senior executives of different group companies that are not performing well.

P has identified that the Kooch Ltd (K), one of its subsidiary, is especially not doing well. The top management has just fired K's VP (Marketing) and a couple of very senior executives from production and finance departments. They have just contacted SBI Capital Markets Ltd (SBI Caps) for consulting K on valuation and equity research matters. They have transferred the marketing head and two production managers of another group company which was doing very well to K. They have also tied up with a German firm, for strategic technology transfer and it is expected to bring in positive results for Kooch. However, it will cost Kooch Rs.1 crore as royalty fee payable to the firm every year.

K is known for its quality of products and strong after-sales service. Owing to its poor management, the company's performance in the past few years has not been good. Its sales have grown at 4% per annum during 2018 to 2022 against the industry growth rate of 10%. The company's share price is currently Rs 23. For the past six months or so, there has not been any significant change in the share price of the company. The risk free return and market return are 7% and 14.5% respectively. The beta of K Ltd is 1.08.

P's management thinks that if the change of key personnel at K goes in favour coupled with the strategic technology transfer, it could bring in positive results in the form of improved profitability. There would be increase in K's growth rate in sales upto 9% over a period of 5 years with 1% increase every year and reduction of cost of goods sold to 66% and selling and administrative expenses to 16% of sales within first year of such change. This would be possible by eliminating slow moving items from K's product portfolio too. P anticipates that to support the growth in K's sales, capex equal to 5% of sales may be needed each year. Projected corporate tax rate is 35%.

You are required to estimate a forecast of the future profitability of K. Starting from 2023, assuming a forecast period of four years. Appraise a valuation report based on free cash flows to the firm to ascertain the value the equity of K Ltd. You may make appropriate assumptions, wherever necessary.

Kooch Ltd.
Summarized Profit and Loss Account

(Rs. in crore)

	2018	2019	2020	2021	2022
Net sales	1442	1477	1580	1642	1695
Cost of goods sold	995	1042	1125	1165	1195
Selling & Admin. Expenses	260	275	280	292	302
Depreciation	37	40	45	45	40
Total expenses	1292	1357	1450	1502	1537
Profit before int. and tax	150	120	130	140	158
Interest	19	15	23	25	30
Tax	45	34	35	40	45
Profit after tax (PAT)	86	71	72	75	83
Per share data (Rs.)					
Earning per share	3.44	2.84	2.88	3.00	3.32
Dividend per share	1.80	1.60	1.60	1.60	1.80
Average price per share	26.48	34.92	30.32	27.88	24.65

Summarized Balance Sheet

As on 31st March, 2022

(Rs. in crore)

Sources of Funds

Equity Capital (Rs 10 face value)	250	
Reserves & Surplus	<u>480</u>	
Shareholders' Funds		730
Borrowed Funds:		
Secured debt and		
Unsecured loans		<u>240</u>
Capital Employed		<u>970</u>

Applications of Funds

Gross Block	657	
Less: Accumulated Depreciation	<u>285</u>	
Net Block		372
Investments		23
Current Assets	753	
Less: Current Liabilities	<u>178</u>	
Working Capital		<u>575</u>
Net Assets		<u>970</u>