SHAREHOLDER VALUE CREATION of NSE NIFTYFIFTY AND BSE SENSEX -A COMPARATIVE STUDY

1. INTRODUCTION

Shareholders expect management to generate value over and above the costs of resources consumed, including the cost of using capital. If suppliers of capital do not receive a fair return to compensate them for the risk they are taking, they will withdraw their capital in search of better returns, since value will be lost. A company that is destroying value will always struggle to attract further capital to finance expansion since it will be hamstrung by a share price that stands at a discount to the underlying value of its assets and by higher interest rates on debt or bank loans demanded by creditors.

Wealth creation refers to changes in the wealth of shareholders on a periodic (annual) basis. Applicable to exchange-listed firms, changes in shareholder wealth are inferred mostly from changes in stock prices, dividends paid, and equity rose during the period. Since stock prices reflect investor expectations about future cash flows, creating wealth for shareholders requires that the firm undertake investment decisions that have a positive net present value (NPV).

The shareholder value creation approach helps to strengthen the competitive position of the firm by focusing on wealth creation. It provides an objective and consistent framework of evaluation and decision-making across all functions, departments and units of the firm. It can be easily implemented since cash flow data can be obtained by suitably adapting the firm's existing system of financial projection and planning. The only additional input needed is the cost of capital. The adoption of the shareholder value creation approach does require a change of the mind-set and educating managers about the shareholders value approach and its implementation.

2. REVIEW OF LITERATURE

Pandya and Marvadi (2016) analysed the impact of value based measures on created shareholder value in Indian banking sector. They have also compared the performance of the banks, as regard to created shareholder value and predominant value based measures. The banks that were listed on Bombay Stock Exchange (BSE) for the period 2004-2005 to 2013-2014 were used to collect the data. The study included the various explanatory variables like Marked Value Added (MVA), Economic Value Added(EVA), Cash Value Added (CVA) and Weighted Average Cost of Capital (WACC) and were used for the purpose of analyzing the results. Furthermore, correlation analysis was carried out in order to measure the association between created shareholder value and value based performance measures. The impact of value based measures on created shareholder value was examined by means of using multiple regression analysis. It was observed that in context of Indian Banks, EVA emerged as to be the highest contributor in created shareholder value, followed by CVA and MVA. It was also found that the value based performance measures had a positive effect on created shareholder value across the various analysis arrangements i.e. overall banking sector, public sector banks and private sector banks. The SBI achieved the first rank in public sector banks, whereas, ICICI bank amongst the private sector banks shown the highest value of CVA and EVA respectively.

Sinha and Sharma (2016) analysed the impact of bank specific, industry specific and macroeconomic factors affecting profitability of Indian Banks. The study used panel data from 42 commercial banks of India for a period of 2000-2013 to evaluate the persistence of bank profits and endogeneity of the factors Generalized Method of Moments (GMM). The Return on Assets (ROA), significantly indicated towards moderate degree of persistence of profits. The study used Herfindahl-Hirschman Index (HHI) to test Structure conduct Hypothesis (SCP). It was found that Bank profits are positively related to the GDP growth and inflation rate affects bank profits negatively.

Bhargav Pandya (2015) had undertaken study on “shareholder value creation: an overview” found that the shareholder value creation approach helps to strengthen the competitive position of the firm by focusing wealth creation. It provides an objectives and the consistent framework of evaluation and decision making across all functions, department and units of the firm.

Nikoo (2015) analysed the impact of Capital structure theory, introduced by Modigliani and Miller (1958) on banks’ performance in stock exchange of Tehran. The data was collected on 17 banks of Tehran from 2009-2014. The study aimed to develop a model to measure the impact of capital structure on the bank efficiency measured by Earning per Share (EPS), Return on Equity 57 (ROE) and Return on Assets (ROA).The results shown that capital structure positively impacts the bank performance.

Pooja Sharma and Abhay Grover (2015) explore and study the shareholder’s value creation in Indian companies as measured by EVA and to determine the key factors that have an impact on shareholders’ value creation. In the present study we have taken dividend and capital structure as independent variable and EVA as dependent variable. Regression technique has been used in order to examine the impact of Dividend and Capital structure on Shareholder Value Creation (SVC). The study reveals that both Dividend and Capital structure have influence on the Shareholder Value Creation. It is also found that mostly all companies are having positive EVA which indicates that these companies are not only thinking about profit maximization but also focusing on the objective of wealth maximization.

Siddhartha Sankar Saha and Mitrendu Narayan Roy (2015), empirically analyses business performance of Indian computer software industry over the years 2003-04 to 2012-13 with the help of Return Of Investment (ROI) and Economic Value Added (EVA) of select 10 companies in this industry. A comparative analysis of ROI and EVA reflected in these companies is made using some statistical tools like average, Standard Deviation, Maximum and Minimum values and Coefficient of Variation. It is observed that Tata Consultancy Services (TCS), Infosys and Wipro are the top companies in this industry in terms of their ROI and EVA. One way ANOVA conducted to analyse the significant difference among select companies in terms of their ROI and EVA shows that select companies are significantly different. Pearson's Correlation Coefficient (r) between ROI and EVA depicts a strong positive correlation between these two business performance indicators. Significance of this correlation is then tested using t test. The result suggests that the correlation between ROI and EVA is not significant in this industry. Impact of EVA and select economic variables on ROI is analysed with the help of Multiple Regression Analysis. Standardised regression coefficients for each predictor variables estimated based on Ordinary Least Square Method indicate the relationship between each predictor variable and ROI. Significance of regression coefficients are tested using t test. It is observed that variables like Net Operating Profit after Tax, Capital Employed, Net Sales, etc. significantly influence ROI in this industry. Adjusted Coefficient of Multiple Determinations (R2) shows a strong association between ROI and its predictor variables. Finally, the model perfectly fits the data according to one way ANOVA result.

Bhadesiya (2015) analysed the shareholder value creation in private sector banks of India. This study made an attempt to analyse, establish and judge the relationship between Economic Value Added (EVA) and Earnings per Share (EPS) in private sector banks of India. The Annual reports of six private sector banks and various websites were used to retrieve the required information about the financial data of private banks. The accounting tools such as EVA and EPS were used for performance analysis. Whereas, evaluation of study variables was done through the use of statistical tools like Mean, Variance, Pearson's Correlation and t-test. The computation of EVA was done by means of including the component like Net Operating Profit after Tax (NOPAT), Capital Employed (CE) and Weighted Average Cost of Capital (WACC). The results of study revealed that majority of banks had a significant and positive relationship between EVA and EPS, both the measures were interrelated, as net profit and number of equity share were common in calculation of EVA and EPS. Thus, it was concluded that majority of banks had a significant relationship between EVA and EPS.

Karam (2014) analysed operational risk using concepts of loss distribution and then used Extreme Value Theory (EVT). They normalized the external data using OLS to a Lebanese bank. They measure error induced in OCR to analyse risk by curve estimation. The authors designed a model for operational risk and also developed scales for measuring risk.

Das (2013) analysed the efficiency scores of thirty-one state co-operative banks by applying DEA approach for the year 2010-11. The results concluded that twenty-one banks are completely efficient while remaining are less or in-efficient. The results proposed that the banks must reduce number of bank employees and the capital to increase efficiency.

Bhasin (2013) evaluated and compared the appropriateness of Economic Value Added (EVA) approach over the conventional measures of corporate performance in context of measuring the shareholder value creation. The study was primarily based on secondary sources of data in relation to measure the traditional as well as Economic Value based performance of select companies during the period 2006-2011. The empirical results suggested that there were significant variations in the shareholder value creation, based upon the EVA across the selected companies. Furthermore, it was observed that EVA and ROCE were statistically significant that is companies with higher EVA should provide more benefits in long run to the shareholders and concluded that EVA is a better performance indicator than conventional accounting measures in explaining market value.

Pradeep and Rakesh (2013) find that the Market capitalization method is gradually accepted by all the stakeholders to know the value creation or destruction by their respective companies. Currently, innovations, brand value, image of the corporate, skills and experience of employees are the intangibles which are directly or indirectly affecting market capitalization and shareholders' value creation in general whereas Model fees, Industrial & Product design, customers network are affecting in particular. By creating and enhancing intangible components, the Indian automobile companies can maximise value for their shareholders. In addition to this voluntary reporting by the companies in the annual reports is equally important to understand value creation process.

Oladele (2013) analysed time series and cross-sectional data for 21 banks listed in Nigerian Stock exchange using OLS (Ordinary Least Squares Method). The study concluded that 31 financial policy was not much significant whereas profitability and dividend policy were found to significantly impact the creation of shareholder value.

Largani (2012) observed that implementing the inappropriate criteria for performance assessment ends in the situation w (Anand 2013)here the company's value is not directed toward the real value, and, as a result, causes the loss of a group of shareholders and the abundant profit of the other group. Finally, with respect to the criticisms made by the researchers of financial field, it is necessary, by realizing innovative criteria, to take a firm step in order to make accurate decisions in financing, operating and investing sections.

Pandye (2010) opined that the objective of Shareholder Wealth Maximization takes care of the questions of timing and the risk of the expected benefits. These problems are handled by considering the Weighted Average Cost of Capital (WACC) while calculating the return.

Pablo Fernandez (2004) shows that to claim that EP, EVA or CVA measures firm's value creation in each period is a tremendous error. These parameter may be useful for measuring the performance of managers or business units, but it makes no sense at all to use EP, EVA and CVA to measure value creation in each period. The problems with these parameters start when one tries t o give these parameters a meaning (that of value creation) that they do not have. Value always depends on expectations.

Penman(2001) puts forth that "the choice between cash accounting and accrual accounting is at the very heart of accounting research, for the differences involves issues of recognition and measurement that define an accounting system. The implication is that accrual accounting does not matter ". One can be cynical about the accounting used in valuation models and so can differ to cash flow models.

Weaver S.C(2001) is of the opinion that the series of adjustment to the NOPAT and the book value proposed by stern steward & co., with the intention of " giving more economic meaning " to EVA and the book values, however do not solve the EVA problems, but rather tends to worse them. In addition, when any of these adjustments are made, EVA's present value is no longer the same as the MVA; unless another adjustment is made to the book value that is equal to the present value of the adjustments to the incomes statement.

Farslo, Degler, Degner (2000) stock price reflects the company's current performance; therefore, the level of EVA isn't important, but changes in that level are. Management focus on these two issues can result in dramatically increasing EVA.

Klieman (1999) compared the performance of 71 companies that adopted EVA between 1987 and 1996 with that of its most direct competitors that did not adopt the EVA. The results showed that the companies that introduced EVA had on an average a higher shareholder return than their immediate competitors: 2.6% in the year of introduction, 5.7%, 9% AND 11.1% during the following years. It is also seen that debt ratio increases slightly and sale of assets increases significantly after introduction EVA.

Ashok banerjee (1998) presented a general look at the vexed question of the relationship between principal and agent. Industry practices with regard to free cash flows of firm and excess capacity have been examined.

It is observed that the industry distributes little free cash to shareholders and the larger part of free cash flows invested in the business for expansion and modernisation result in wonderful development of free cash flows and there by destroying shareholder wealth h (ROI<Ke).

Penman and sougiannis (1998) made a comparison of dividend, cash flow and earnings approaches to equity valuation and admit that "dividend, cash flow and earnings approaches are equivalent when the respective pay-offs are predicted to infinity". But they claim that the finite horizon analysis accrual earnings techniques dominate free cash flow and dividend discounting approaches.

Biddle, Bowen and Wallace (1997) used relative and incremental information tests to examine whether stock returns were more highly associated with EVA, residual income or cash flow from operations. They concluded that while 'for some firms EVA may be an effective tool for internal decision making, performance measurement, and incentive compensation, it does not dominate earnings in its association with stock market returns'.

Kramer and Pushner (1997) the performance measure economic value added (EVA) has been adopted by a rapidly growing number of firms and is beginning to appear in mainstream finance textbooks. Despite such acceptance, little empirical work has been done on the ability of EVA to reflect market value added. The results do not fully support the arguments of EVA proponents that it is the best internal measure of corporate success in adding value to shareholder investments.

O'Byrne (1997) estimated that changes in EVA explain more variation in long-term stock returns than changes in earnings.

Bacidore et al (1997) developed a refined EVA (REVA), computing capital charges based on market values of debt and equity instead of adjusted book values. For the years between 1982 and 1992, they compared the explanatory power of EVA and REVA on market-risk adjusted excess returns, and found that REVA out-performed EVA in measuring firm performance.

Agarwal et al., (1996) carried out a study on Singapore market data to investigate the usefulness of the P/E ratio as a valuation modal. They are of the opinion that the identified fundamental variables, which are supposed to determine the value of firm, also explain a significant portion of the variability in the price-to-book value ratio. Therefore the letter can be used as a proxy for the former.

Cole et al., (1996) examined the predictive power of traditional market indicators like dividend yield and market-to-book ratio and address the claim that these are no longer value indicators. They found that share repurchase activity has not been especially high through most of the 1990s and that after adjusting for buyback the dividend yield remains low. Likewise the M/B ration remains at high record once charges for retiree health liabilities have been taken into account.

Stern and Stewart (1994) concluded that the EVA stands well out from the crowd as the single best measure of wealth creation on a contemporaneous basis and is almost 50% better than its closest accounting-based competitor [including EPS, ROE and ROI] in explaining changes in shareholder wealth.

Gary Wilson(1990) puts forth that a CFO adds value by "being creative" (that is rethinking assumptions about ownership and control, what an asset is, how to optimise cost of capital while achieving strategic goals and what really drives the company's value)

The author is of the opinion that a CFO should be first and foremost a strategic business executive. Creative value for shareholders must be the primary economic objective of a business executive. And this can be attained through franchising. Franchising, an intangible asset produces very tangible results and is really the linchpin in the value creation. To quote the author "creativity creates value". In finance, it means structuring deals creatively.

Gordon Donaldson (1985) has discovered that many managers do not pay sufficient attention to how the achievement of different goals will affect the flow of funds. The author demonstrates how a company can check whether its strategic and financial goals are consistent with reality. Such an analysis may better prepare the company to make the right trade-offs among conflicting goals and anticipate what are the consequences of its actions may be.

3. STATEMENT OF THE PROBLEM

The concern for value creation, till even recently, was only skin-deep. Indian companies, given to operating under a regulated regime for over 40years, and in the options of any market worth its name for corporate control never give any importance to maximising the corporate and the shareholder value. Except for a few select companies, most never bothered to meet the change in the value of expectation of the shareholder are to become cost competitive. No conscious effect is made to upgrade technologies, improve productivity and efficiency, avoid over/manning or unlock investments that had become anfractuous or non-value adding. Companies either did not pay the dividend or paid at a level that is far lower than the opportunity cost of the investor. With no plans in place as to how to overcome the existing in efficiencies and exploit emerging opportunities, shareholder perceived that the value creation abilities of such firms are limited which intern resulted in depressed price of their shares.

However, beginning 1991, deregulation of Indian industrial sector ushered in a new era. There is definitely a clear indication that certain firms had already started thinking and acting in terms of their value enhancing capabilities. Some of private sector companies which are now generally considered as shareholder value driven companies. However , the some of the companies have not at fully moved towards becoming true shareholders value driving companies in the eyes of the capital market, as reflected in the low appreciation of their share prices vis-a-vis their competitors as well as their own book value per share.

Hence, an attempt has been made in the present study to measure the value created by select Indian companies for its shareholders.

4. OBJECTIVES

1. To study the shareholder value creation of NSE Nifty companies

2. To study the shareholder value creation of BSE Sensex companies
3. To compare the shareholder value creation in NSE and BSE Indexes
4. To examine the perception of the individual investors on shareholder value creation.

5. CONCEPTUAL FRAMEWORK

Looking at the history of large corporations who have grown many fold post liberalisation, by adapting to rapidly changing and very challenging business environment. Many a times, the change is forced upon the company by external environment such as increased competition, new product launch, disruptive innovations, new and more efficient technology, the emergence of new competing products, new markets, a new class of consumers, demographic changes, business cycle etc. wiser corporations foresee the external changes well in advance and change themselves accordingly, whereas, not so wiser firms are forced to change in due course of time, without which they would fail. The firms that have foresight over the market and the changing scenario transform themselves at the peak of their performance and thereby, continue to enjoy the leadership position in the market for a long period of time. There is a pressure on wealth of shareholders. These changes reduce the benefits of real owner of the company. So there is a need to study how we balance between meeting global changes without sacrificing wealth of the shareholders.

Profile of sample constituents

1. **Companies** The industry sectors considered on the basis of market capitalisation comprises of 10 sectors namely, Info tech, Pharma, Auto mobiles, Oil and gas, Sugar, Steel, Text tile, FMCG , Capital goods and Cement, listed in ET500 in November 2016. This is to study shareholder value creation from the company perspective by adopting **Pablo Fernandez** model.
2. **Individual investors** A diverse mix of person- salaried, professional, managers, entrepreneurs, consultants, retired persons and students will be contacted through stock brokers, sub-brokers and personal contacts. Thus clients of karvy consultancy, share khan, way2wealth, motilal oswal and geojit will be chosen as respondents.

6. SCOPE OF THE STUDY

The scope of the present research can be viewed from two different perspectives

1. **Company perspective:** to know the different performance metrics used to measure shareholder value creation by adopting **Pablo Fernandez** model.
2. **Stakeholder perspective:** the study aims to know the perceptions of the retail investors with respect shareholder value creation.

The study covers the time period of ten years from 2007-08 to 2017-18.

The study is restricted to the select index companies.

7. METHODOLOGY

Sample survey method for Indian companies

Considering the practicability and the time limit, the researcher chose index companies on the basis of judgement sampling. The list of companies are gathered from ET500, June 2016 ranked on the basis of market capitalisation, P/E Ratio, RONW and other parameters to form the sampling frame and these companies are listed on BSE and NSE.

To elicit the perceptions of investors the data will be collected from them by administering the questionnaires. The researcher will be consulted the individual investors on the aspects of shareholder value creation and measurement.

Sample survey method for individual investors

In respect of retail investors both judgement sampling and snowball sampling techniques will be used. Judgement sampling will comprised a deliberate selection of sample respondents that confirmed to some predetermined criteria. Snowball sampling method will be used to identify and collect feedback from respondents by building up a list of investors by using a initial set of its members as informants.

In turn, these initial respondents will be supplied names of other investors known to them until a fairly adequate list available from which the researcher gathered inputs. The initial respondents will be constituted the investors who attend “investors meet” conducted by stock exchanges and also those who visited the leading and established stock broking houses.

8. CHAPTERISATION

The theses will be presented in six chapters. The chapters are so designed that each chapter provides answers to the research questions formulated and helps in fulfilling the research objectives.

Chapter – I: Introduction

Chapter – II: Share Holder Value Creation of NSE Nifty Fifty Companies

Chapter – III: Share Holder Value Creation of BSE Sensex Companies

Chapter –IV: Comparison of Share Holder Value Creation in BSE and NSE companies

Chapter – V: Perception of Investors on Share Holder Value Creation

Chapter – VI: Summary of Findings, Conclusions and Suggestions

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