

Analysis of Comparables

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Valuation Approach and Methodology

Approach	Income Approach	Market Approach	Cost Approach
Fair Value Estimation	Based on the expected cash flows/ income the business is expected to generate	Based on market multiples or transactions involving sale of comparable assets.	Based on replacement/ reproduction cost – adjusted for age/ obsolescence.
Methods	<ul style="list-style-type: none">• Discounted Cash Flow ('DCF')• Relief From Royalty• Multi-period Excess Earnings• With and Without• Option pricing	<ul style="list-style-type: none">• Market Price• Comparable Companies Multiple• Comparable Transaction Multiple	<ul style="list-style-type: none">• Reproduction Cost• Replacement Cost

Comparable Companies

- Analysis of Comparables is an important foundation of a valuation exercise
- Most of the business valuations, on a 'going concern' premise, are based on Market and/ or Income Approach
- Required both for Market Approach and Income Approach
 - Market Approach: Basis for estimation of Base Multiple
 - Income Approach: Basis for estimation of Beta

Selection of Comparables

ICAI Valuation Standard 103-Valuation Approaches And Methods

- While identifying and selecting the market comparables, a valuer shall consider the following indicative factors such as:

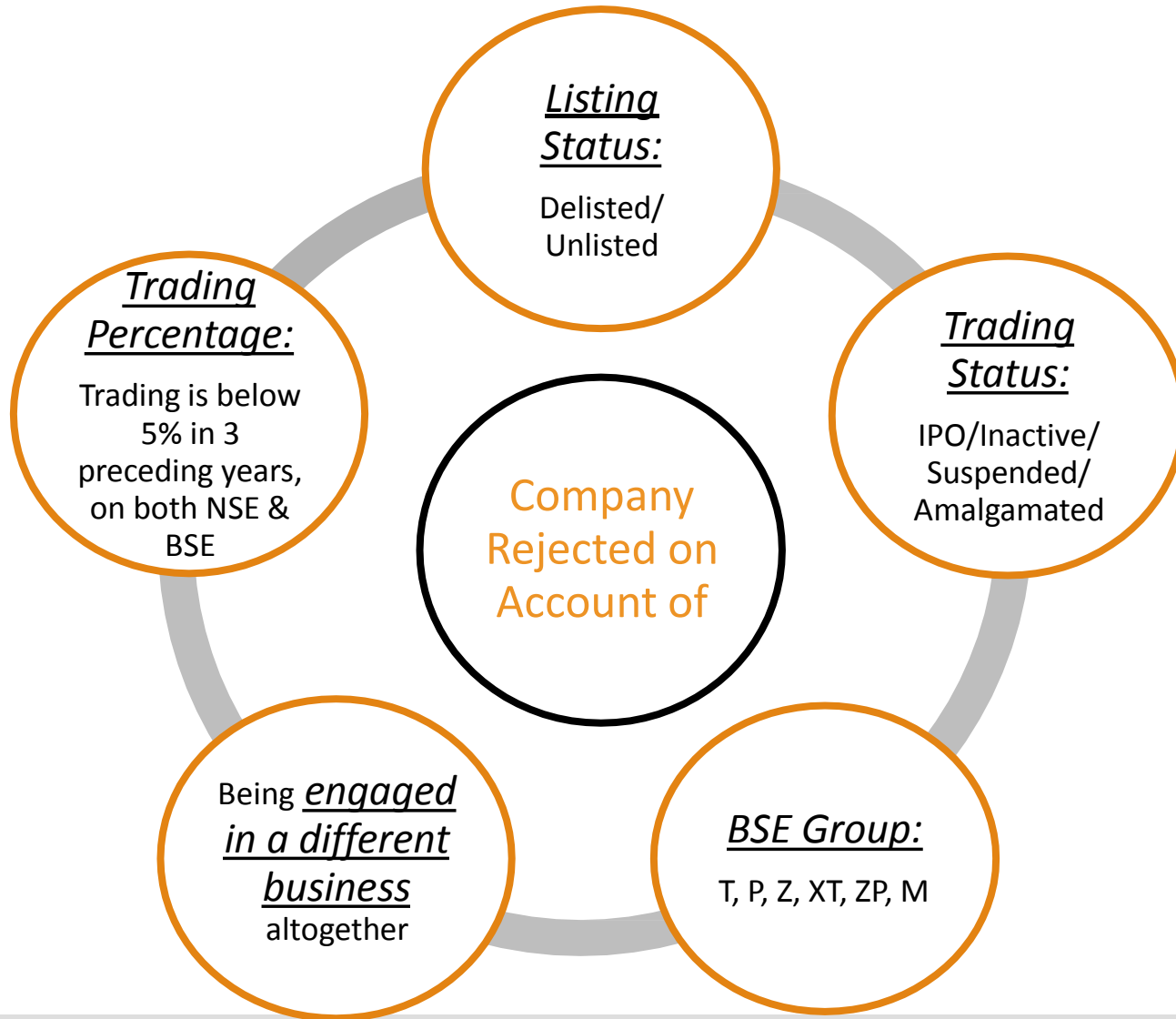
Industry to which the asset belongs

Geographic area of operations

Similar line of business, or similar economic forces that affect the asset being valued

Other parameters such as size (for example- revenue, assets, etc), stage of life cycle of the asset, profitability, diversification, etc

Filtering of Comparables: Basic Filters



Other Filters:

- Revenue Filter
- Market Capitalisation Filter
- Loan Book Filter (For Financial Institutions)
- Total Asset Filter (For Financial Institutions)

Case Study

- Company XYZ is a domestic company engaged in packed food segment, say chips/wafers etc. It sells branded products and operates using 2 to 3 sub-brands.
- Turnover – Rs. 750 Crores
- EBITDA Margin – 10%
- PAT Margin – 5%

Determine the Comparable Companies for this entity.

Other Factors Considered

Target Company generates major Revenue from Exports

Filter out

Non Exporting Companies, also based on Revenue % from Exports

Reason:

Risk associated with Forex Gain/Loss

Target Company is a Non-Government Company

Filter Out

Government Companies

Reason:

Risk associated is different

Target Company is a MNC

Filter out

Non-MNCs

Reason:

MNCs usually command a premium

Target Company operates in a certain geographical regions

Filter out

Companies operating in other Geographical Locations

Reason:

Risk differs across geographical regions

Case Study

Particular	Count	Remaining Companies
Total number of companies	822	
<u>Listing Status:</u> Delisted/ Unlisted	640	182
<u>Trading Status:</u> IPO/Inactive/ Suspended/ Amalgamated	64	118
<u>BSE Group:</u> T, P, Z, XT, ZP, M	39	79
Being <u>engaged in a different business</u> altogether Based on Economic Activity(NIC)	52	27
<u>Revenue Filter considered :</u> +/- 80% of Target Companies Revenue	19	8
Rejected on Business Profiling*	4	6
<u>Trading Percentage:</u> Low trading frequency	0	6
<i>Final List of Comparables</i>	0	6

* Even Britannia and Nestle have been considered for Profiling, even though they got excluded in Revenue Filter

Analysis of Comparables

Analysis

- Financial Statements
- MDA
- Industry Reports
- Analysts reports
- Multiples over medium to long term; Forward multiples (if available)

Quantitative and qualitative factors

- Analyst reports
- Significant CWIP
- Recent commissioning of capacity
- Return on capital employed/ Return on equity
- Non-recurring/ Non-operational income/ expenses
- Historical Multiples (Longer period)/ Forward multiple
- Volatility in performance
- Working Capital levels

Quantitative and qualitative factors

- Growth
- Profitability
- Size
- Quality of Promoter and Key Management
- Capital Structure

Case Study – 1

Particulars	Company A	Company B	Subject Compan
Networth	100	300	150
Borrowing	200	150	200
	300	450	350
Net block	125	300	250
CWIP	125	25	30
NCA	50	125	70
	300	450	350
Revenue	200	500	350
EBITDA	25	60	42
<i>EBITDA margin</i>	<i>12.5%</i>	<i>12.0%</i>	<i>12.0%</i>
Market Cap	175	400	229
EV	375	550	
EV/ EBITDA	15.0	9.2	?

Case Study – 1

Particulars	Company A	Company B
EV	375	550
Less: CWIP	-125	-25
EV-CWIP	250	525
Adjusted EV/ EBITDA	10.0	8.8
EBITDA considered	42	
EV/ EBITDA Multiple - Applied	9	9.5
	378	399
Add: CWIP	30	30
EV	408	429
Borrowings	-200	-200
Equity Value	208	229

Case Study – 2

	Revenue	EBITDA	EBITDA Margin	Market Cap	Debt	EV	CAGR (3 years)		
							Revenue	EBITDA	EV/ EBITDA
Company A	150	22	14.7%	126	50.0	176.0	10%	7%	8.0
Company B	130	22	16.9%	164	100.0	264.0	10%	10%	12.0
Company C	300	58	19.3%	541	300.0	841.0	8%	15%	14.5
Company D	200	40	20.0%	300	100.0	400.0	15%	10%	10.0
Mean	195		17.7%				10.8%	11%	11.1
Median	175		18.1%				10.0%	10%	11.0
Subject Company	200	36	18.0%	?	150	?	12%	14%	?

Case Study – 2

Particulars

Peer Companies' Multiple

Mean 11.0

Median 11.1

Adjustments

Growth +ve

EV/ EBITDA multiple considered 13 13.5

EBITDA considered 36

EV/ EBITDA multiple applied 13 13.5

EV 468 486

Less: Borrowings -150 -150

Equity Value 318 336

Practical Considerations

- Limited number of comparable companies
- Lack of Market depth (Analyst coverage/ Trading volume/ Low floating stock)
- Divergence in Multiples of selected companies
- Peer set for Income Approach and Market Approach: Should it be identical?
- Adjustment for Qualitative factors : Need to articulate
- Importance of documentation

Thank you

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