Problem No.4 (Solution)

Illustration 4 : problem - 4

The Balance sheet of Indian Seamless Steels Ltd. as on 31st March, 2004 revealed the following :

Balance Sheet

Liabilities	₹.	Assets		₹.
Share capital (Issued)		Fixed Assets	9,00,000	
Equity shares of Rs. 10 each		*Less :*		
Rs. 8 paid	8,00,000	Depreciation	1,10,000	7,90,000
Reserves	2,00,000	Goodwill		80,000
Profit & Loss A/c	20,000	Current Assets		4,90,000
10% Debentures	1,00,000	Discount on Debentures		10,000
Current liabilities	2,50,000			
	13,70,000			**13,70,000**

1. Fixed assets and goodwill were revalued at ₹. 7,50,000 and ₹. 1,00,000 respectively.
2. The net profit after tax for the immediately preceding three years were, ₹. 1,10,000 ; ₹. 1,05,000 and ₹. 1,45,000 of which 25 % were transferred to reserves. 25% trd. as (12 के
3. A fair return in the industry in which the company is engaged is considered to be 10%.

Compute the value of companies shares, by

(a) Net Asset method, (b) Yield value method, (c) Fair value method.

Solution : *(a) Net asset method*

Net assets = Agreed value of assets – Agreed value of liabilities.

Agreed Assets :

Fixed assets (Revised value)	₹. 7,50,000
Goodwill (Revised value)	₹. 1,00,000
Current assets (Book value)	₹. 4,90,000
	₹. 13,40,000

Less : Agreed liabilities

10% Debentures	₹. 1,00,000	
Current liabilities	₹. 2,50,000	₹. 3,50,000
Amt Available to Eq shrhs/ **Net Assets**		₹. 9,90,000

$$\text{Intrinsic value of share} = \frac{\text{Net assets}}{\text{No. of equity shares}}$$

$$= \frac{\text{Rs. } 9,90,000}{1,00,000} = \text{Rs. } 9.90$$

Note.... 800,000/8 = 100,000

While computing number of shares paid-up value of shares may be considered.

(b) Yield value method :

$$\text{Yield value} = \frac{\text{Expected rate of dividend}}{\text{Normal rate of return}} \times \text{Paid-up value per share}$$

Expected rate of dividend is calculated as under :

Average profit for the last 3 years

= ₹. (1,10,000 + 1,05,000 + 1,45,000

= ₹. 3,60,000 , 3 years ₹. 1,20,000

Less : Transfer to reserve at 25% ₹. 30,000

Average profit ₹. 90,000

Expected rate of dividend

800,000 : 90,000 :: 100 : ?

100 / 800,000 × 90,000 = 11.25%

$$= \frac{\text{Average profit}}{\text{Paid-up equity capital}} \times 100$$

$$= \frac{90,000}{8,00,000} \times 100 = 11.25\%$$

Yield value per share $= \frac{11.25}{10} \times$ **Rs. 8 = Rs. 9 per share.**

(c) Fair value method :

$$\text{Fair value of share} = \frac{\text{Intrinsic value} + \text{Yield value}}{2}$$

$$= \frac{\text{Rs. } 9.90 + \text{Rs. } 9.00}{2} = \text{Rs. } 9.45 \text{ per share.}$$

Thank u