# VALUATION OF SHARES

Valuation of shares maybe made for different purposes under different situations. Where the liquidation of the company is impending, the value of its net assets are mainly considered.

Where the success of a business is mainly reflected by its earnings, the importance is given to its earning capacity.

For a going concern, the shareholders become eager to know the amount of net assets backing the business and the profitability of the business together.

Generally, there are two methods for valuation of shares :-

i) Asset Backing Method / Intrinsic Value Method / Net Assets Value Method

ii) Yield Method / Earning Capacity Method.

## A. ASSET BACKING METHOD (Without valuation of goodwill).

| Particulars | Rs. |
|---|---|
| Fixed Assets at revalued figure (goodwill, Land and building, plant and machinery, furniture and fixture etc) | xxx |
| Add: Current Assets, loans and Advances and All types Investments at revalued figure | xxx |
| | xxx |
| Less: External Liabilities / Outside Liabilities (Sundry creditors, Bills Payable, Bank Overdraft, Outstanding Expenses, Provision for taxation, Proposed Dividend, Debentures and Loans with accrued interest thereon, if any, Compensation payable to the worker, damages payable at law). | xxx |
| Net Assets / Net Worth | xxx |
| Less: Preference shareholders claim (Face value of preference share capital, premium payable on redemption, arrear preference dividend if any) | xxx |
| * Add: Notional call money on partly paid up equity shares | |
| Net Assets owned by the equity shareholders | xxx |

a. ∴ Value per fully paid up equity shares.

$$\frac{\text{Net Assets owned by the equity shareholders}}{\text{Total no. of equity shares}}$$

b. Value of each partly paid up equity share.

Intrinsic value of fully paid up equity share − Notional call per share.

## B. Yield Method / Earning capacity Method.

| Particulars | Rs. |
|---|---|
| Average Annual profit (before taxation) | xxx |
| Less: Tax (if tax rate is not given, then assume @ 50%) | xxx |
| | xxx |
| Less: Transfer to Reserve [u/s 205(2A)] (Assuming @ 10%, if percentage is not given) | xxx |
| | xxx |
| Less: Preference Dividend (for current year) | xxx |
| Profit available to the equity shareholders | xxx |

a) Rate of Dividend / Expected rate of return.

$$\frac{\text{Profit available to the equity shareholders}}{\text{Paid up equity share capital}} \times 100$$

b) Value per equity share.

$$\frac{\text{Rate of Dividend / Expected rate of return}}{\text{Normal rate of return}} \times \text{Paid up value of each equity share}$$

c) Fair Value = $\dfrac{\text{Asset Backing Value} + \text{Yield Value}}{2}$