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ECONOMIC VALUE ADDED ANALYSIS IN SELECTED CEMENT COMPANIES

KEY WORDS:

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ABSTRACT

The article examines how the Economic Value Added (EVA) a measure of external performance which is considered to be the best indicator of shareholder value creation is associated with the firm's performance in terms of financial measures of the company such as Economic Value Added (EVA). A sample of 7 companies has been taken from cement industry during the period 2015-2016. The study concludes that Economic Value Added performances in selected companies.

INTRODUCTION

India's cement Industry is a vital part of its economy, providing employment to more than a million people, directly or indirectly. Ever since it was deregulated in 1982, the Indian cement Industry has attracted enormous investments, from both Indian and foreign investors, making it the second largest in the world. The Industry is currently in a turnaround segment, trying to achieve global standards in production, safety, and energy-efficiency.

India has a lot of potential for expansion in the infrastructure and construction sector and the cement sector is expected to largely benefit from it. Some of the recent major government initiatives such as development of 100 smart cities are expected to give a major boost to the sector.

EVA is not a new invention. An accounting performance assess called residual income is defined to be operating profit subtracted with capital charged. EVA is thus one variation of residual income with adjustments to how one calculates income and capital. One of the first to mention the residual income concept was Alfred Marshall in 1890. Marshall defined economic profit as total net gains less the interest on invested capital at the current rate. It was defined as a good way to balance ROI-control.

Knowing this background many academics have been wondering about the big publicity and admire that has surrounded EVA in the recent years. The EVA –concept is often called Economic Profit (EP) in order to keep away from problems caused by the trade marking. On the other hand the name "EVA" is so popular and well known that often all residual income concepts are often called EVA although they do not comprise even the main elements defined by Stern Stewart & Co.

In the 1970's or earlier residual income did not got broad publicity and it did not end up to be the prime performance measure in huge deal of companies. However EVA, practically the same concept with a different name, has done it in the latest years. Moreover the spreading of EVA and other residual income measures does not look to be on a weakening trend. On the contrary the number of companies adopting EVA is increasing fast. We can only guess why residual income did never gain a popularity of this level. One of the probable reasons is that Economic value added (EVA) was marketed with a concept of Market Value Added (MVA) and it did offer a theoretically sound link to market valuation. In the times when investor's demands focus on Shareholder value issue this was a good bite. Possibly also relevant marketing by Stern Stewart & Co. had and has its contribution.

EVA computation methodology of the study

Developed by the American consulting company, Stern Stewart & Co., in the late 1980's, Economic value added (EVA) is performance measure fast gaining recognition worldwide. EVA can basically be defined as the excess of profits generated in a business over and above the cost of funds deployed simply put, EVA is the difference between the net operating profits of a corporate and the cost of capital employed in the business by the corporate. It measures the addition to the shareholders value in terms of wealth maximization, the surplus generated after meeting shareholders prospect.

The calculation is as follows:

EVA = Net Operating Profit after Taxes But before Interest (NOPAT)- Cost of Capital Employed (COCE)

After calculating EVA, in order to find out the best performer (in terms of EVA addition) two ratios have been computed. That is, the EVA created or destroyed to its respective company's Capital employed and Sales turnover made. In the following pages, industry-wise EVA analysis is presented.

EVA Analysis in selected cement companies as on 2015-2016(Rs in Crores)

Sl. No	Company Name	NOPAT Rs. Cr	COCE Rs. Cr	EVA created/ destroyed Rs. Cr	EVA/ CE per Rs.100	Rank	EVA/ Sales per Rs. 100	Rank
1	Ultra tech	3417.58	1003.02	2414.55	10.10	1	8.28	1
2	JK Lakshmi	270.65	280.89	-10.24	-0.35		-0.30	
3	Birla Cement	353.23	400.95	-47.72	-1.42		-.94	
4	JK Cement	483.69	411.80	71.89	1.91		1.66	
5	Ramco cement	752.81	460.15	292.66	7.40	2	5.99	2
6	Shree cement	1468.53	938.62	529.91	6.16		5.89	
7	Rain cement	49.8	109.15	-59.35	-99.54		-5.33	

Source: Computed from Secondary Data – CMIE prowess

EVA Analysis in cement companies

7 Companies were analyzed in the Cement Industry. The relevant data are given in Table. Four Companies have created economic value for their shareholders during the study period. Ultra tech ltd. has created the highest EVA among the companies studied which created Rs. 2414.55 crore annually during the study period. Ramco cement, shree cement are other two notable performers.

EVA per Rs. 100 capital employed ranking reveals that the south based blue chip Company, viz. Ultra tech Cements as the top EVA creator among the 7 companies analyzed.Ramco takes the second spot.

Similar ranking based on EVA per Rs.100 sales turnover; place Ultra tech cement as the best company closely followed by the Ramco Cements.

CONCLUSION

Economic value added has become the most fashionable measurement for determining the ability of a corporates to generate an suitable rate of return. Despite the comparatively recent adoption of EVA as an internal and external financial performance measure, its conceptual underpinnings derive from a well established micro economic literature concerning the link between firm earnings and wealth creation.EVA metrics provide managers with a commanding tool to consider investment and spending decisions against capital requirements and investors' prospect. The observation of EVA is based on the effective economic principle that firm's value increases only if it is able to generate surplus over its cost of capital and therefore it is based on well-built theoretical association. It can also be linked to a company's recompense system, so that managers are paid (or not) based on their ability to combine efficient asset utilization with profitable operating consequences. Admittedly, EVA is one of the ways to evaluate the usefulness of a performance measure. EVA identifies not only end results, but also the cost of the input of funds to get the consequences. This provides a basis for the measurement of efficiency and motivates managers to be more efficient with funds, which is usually valuable. But, EVA is not contributing to the stock return because the investors' assurance and belief is on the provision of dividends to the share holder rather than increasing worth of the Industry. However, this method must be cautiously applied to ensure that it is measuring economic effects properly and does not create time-horizon alteration. In all EVA can be used as internal measure for performance appraisal but at alone cannot be act as an investor's investment decision making assess to earn good returns from the equity investment in the Indian environment.

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