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Comparative study of Economic Value Added: A case study on five Indian companies.

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Abstract: Economic value added (EVA) is one of financial performance assessment method. EVA defined as the difference between NOPAT and cost of capital (Young & O'Byrne, 2001). The cost of capital is equal to the invested cost of capital (capital use) multiplied by the weighted average cost of capital (WACC). EVA is the residual income a company earns after capital costs are deducted. More specifically, it is operating profits minus the required dollar-amount return for the capital employed (Horne, 2002). EVA is not a new concept globally. It is based on residual concept that is calculated by deducting capital charges from the operating profits. One variation between EVA and residual income is to know how to work out on return and cost to get maximum return. Stern Stewart &Co. introduced this system in 1982.The list of some of the companies using EVA are Coca-Cola, Eliy Lily Monsanto and others. Companies adopted EVA by number of ways the initial interest was introduced a few years ago by a magazine article about EVA. . Idea of EVA has been given by Stern Stewart & Co, a New York based global financial consultant. Most of the companies consider the returns but not the entire cost they consider only the cost of debt and cost of preference shares. Management considers Equity as a cost free capital. In this situation shareholder returns are manipulative. Equity is a costly source of finance.

Keywords: : Economic Value Added, Net Operating Profit After Tax, Weighted Average Cost of Capital, Earning After Tax.

Review of Literature

Bolek, Monika Kacprzyk, Marta Wolski, Rafał (2012) Economic Value Added(EVA) a profitability measure and a Cash Conversion Cycle a liquidity and profitability measure are presented in this article. **Li, Pingli, Tang, Guliang and Dai, Narisa, (2012)** Key Conclusions the evolutionary change is achieved in Chinese state-owned enterprises by staged performance measurement system development in which Economic Value Added is introduced gradually. **Othman, I.W.; Pok Wee Ching ; Ghazali, A.W. (2012)** This study examines the relationship between Economic Value Added (EVA), being the measurement for value creation of companies and the Malaysian stock market performance. **Ashok Banerjee (2000)** Maximizing shareholder value has become the new corporate paradigm .Corporations in the US have started disclosing EVA information from the beginning of 90s as a measure of corporate performance. **Bahri, Moujib, (2008).** Nowadays, companies are facing complex challenges. Theyhave to deal with a business environment characterized by rapid and significant changes. **William g. Sullivana& Kim lascola needy (2007)** This paper discusses a measure for estimating the wealth creation potential of capital investments in manufacturing

Introduction & Research Methodology with objects and limitations

EVA is positive if NOPAT exceed the cost of financing. The authors of EVA state that, in this case,the company has created shareholder value. On the other hand when EVA is negative, the company is destroying the value of the shareholder. Bennet Stewart and Joel Stern jointly founded Global Financial Consultancy firm based in New York under the name "Stern Stewart Co", This Company has a strong faith that EVA is a true economic measurement tool than any other financial measurement tool. In a study till 2008 just 37 companies in India have disclosed EVA in their financial report. There are irregularities in the study of EVA calculation so the companies avoid accepting EVA as performance measurement tool. EVA is based on the concept that a successful firm should earn at least its cost of capital. Firms that earn higher returns than financing costs enhance thewealth of shareholder. EVA can be used as financial performance assessment and focus on value creation; EVA make the company more concern to capital structure policy; EVA make the management focus on maximizing the investment return and minimizethe cost of capital; EVA can be applied to select profitable projects/investments. EVA value can be grouped into three categories: *EVA > 0 or EVA is positive* In this position means the management of the company has succeeded in creating economic value added for the company. *EVA value = 0* In this position means the management of the company is in break even.The company suffered a setback but at the same time does not progress economically. *EVA < 0 or EVA is negative* In this position means there no additional economic value added or the company can't meet shareholders and creditors (investors) expectation.) EVA is a tool which helps to focus managers' attention on the impact of their decisions inincreasing shareholders' wealth. EVA is a good guide for investors; as on the bias of EVA, they can decide whether aparticular company is worth investing money in or not. EVA can be used as a basis for valuation of goodwill and shares. EVA is a good controlling device in a decentralized enterprise. Management can apply EVA to find out EVA contribution of each decentralized unit or segment of the company. It shows the cost management of businesses and illustrates working capital availability after the deduction of its actual opportunity cost. Though EVA does not take size differences into consideration. A plant or division that is larger insize will obviously have a higher EVA, in comparison to something that is smaller in size, which could distort your calculations and give you an inaccurate result. EVA can be used for personal gains by the manager, which might not be particularlyprofitable for the firm. EVA might overemphasize the immediate need to generate the results. It might put more emphasis on short-term gains than long-term ones. EVA measures corporation's true economic profit and help to understand which business units best utilized their assets to generate returns and maximize shareholders value. The following aspects of Economic Value have inspired me to take this project:

EVA is better discloser of genuine addition or draining the net worth of shareholders.
Unlike other taking techniques it can be used in decision- making process.
EVA is better technique of measure of performance.

This empirical study has been taken up with the following objectives.
To compare and contrast EVA with other measures of performance like (ratios, ROI).
To measure the financial performance of some household and personal care productmanufacturing companies in INDIA.
The study is based on accounting information. So all the limitations of accounting apply tothis study.
The study has only made a humble attempt at evaluating financial performance anddoes not and cannot claim as the perfect study.
The data used for calculation is historical data and may have some adjustments made.
Time constraint.

Research is a structured enquiry that utilizes acceptable scientific methodology to solve problems and create new knowledge that is generally applicable. Research methodology is a way to solve the research problem in a systematic manner. The sequence or steps, which will be followed, are explained under in detail. The study on EVA of household and personal careproduct manufacturing companies in INDIA is based on the secondary data collected from the annual reports of the company. Last five years Balance sheet, Profit & loss A/c, cash flowstatement and stock price of the company were taken for analysis.

Sample Size

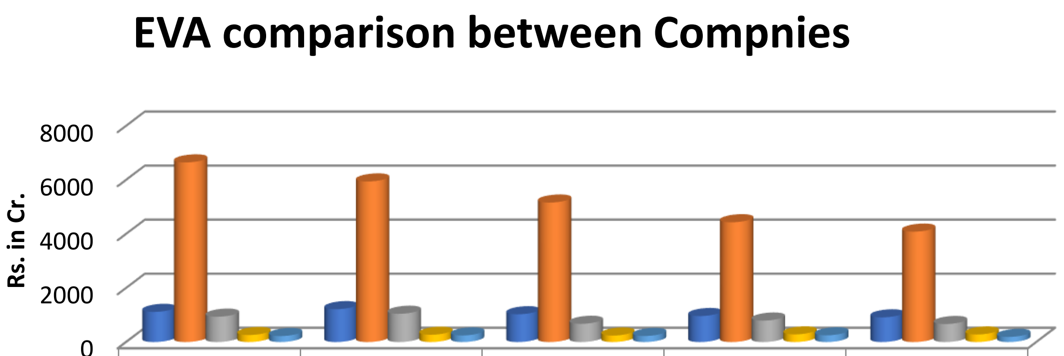
Sample size: Balance sheet of five companies for the period of 5 years (2016 – 2020) has been taken to compute the EVA. All these companies are NSE listed. Following is the companies,

1. DABUR INDIA.
2. HUL.
3. Marico Ltd.
4. Emami Ltd.
5. Gillette India Ltd.

ECONOMIC VALUE ADDED

Now we can compare these five company's performance year by year

	Dabur	HUL	Marrico	Emami	Gillette
2020	1115.49	6646.11	937.63	259.81	220.38
2019	1215.36	5942.21	1045.64	269.78	243.57
2018	1027.51	5160.90	673.84	240.00	223.28
2017	961.30	4432.28	793.22	282.61	248.72
2016	912.20	4084.26	666.55	279.85	189.97



	2020	2019	2018	2017	2016
Dabur	1115.49	1215.36	1027.51	961.3	912.2
HUL	6646.11	5942.21	5160.9	4432.28	4084.26
Marrico	937.63	1045.64	673.84	793.22	666.55
Emami	259.81	269.78	240	282.61	279.85
Gillette	220.38	243.57	223.28	248.72	189.97

Interpretations Analysis, Findings , Suggestions with Conclusions

As per chart HUL is giving good result and they continuously increasing their EVA.
All the four companies give positive EVA .
EMAMI and GILLETTE is giving consistent results from last 5 year.
DABUR shows gradually increase from past 4 years but in 2020 it is decreased their EVA.
MARICO is showing many fluctuations in their performance.
During the years 2016 up to 2020 HUL and DABUR is able to create increasing financial indicators such as sales, net profits, assets, equity, and earning per share.
EVA values were positive annually for all selected company.The positive of EVA for the year 2016 up to 2020 is a satisfactory accomplishment. It means the company has been able to give value add to investors and creditors.
All above companies are creating the wealth of the shareholder have a low equity cost andthe profit is enough to cover the equity cost. It means these companies are investing its fundsin profitable projects
The declining of EVA in some year should make the company more concern to find out thecauses. EVA was decreased. It caused by increasing the cost of capital. The increasing cost of capital caused by increasing interest rate.
HUL is ranked 1^{st} on selected 5 companies and DABUR maintain 2^{nd} position

Increasing assets would create good market capitalization.

Return on investment that is EPS is high in case of HUL and DABUR and along with that they have strong balancesheet and strong cash inflow.
Further, the results showed that sales and profit after tax are found to have astrongerrelationship with EVA.
EAMAMI and GILLETTE have stable EVA but they lack to capture market.

MARICO have so many fluctuation in their performance.

With the help of EVA, as cost of equity is considered in its calculation, the company which is giving more profit after deducting the cost of equity is a well performing companythan any other.

In the uncertain macroeconomic situation, the company need implements an effective strategy. To maintain company performance, companies need to implements some strategies as follows:

a. Strengthen internal financing to reduce financing from debt.

b. Produce its products by using local raw material (try to avoid imported raw material)

c. Focus on profitable investment and unleash unprofitable investment

d. Top management commitment, patience and perseverance to see through a complex implementation process is important.

e. Companies should cut down the cost where it possible and maximize profit.

f. Companies expand their business and should focus on rural area for sales maximization

i. The companies should disclose economic value added in their annual report.

j. Should use their assets more effectively and properly for that they should have good management decisions and implementation of that decisions

Conclusions

At last we can conclude that EVA is a financial measure based on operating income after tax.EVA is the most reliable source to know the performance of the company in today era. A company should be a wealth creator not the wealth destroyer for the shareholder. In the EVA system a company will be a wealth creator if its operations are as good as it can generate profit more than the cost of capital which includes the cost of equity as well. In our study there are five companies which are the wealth creator companies. EVA has both advantages and limitations.Thus, using EVA only is no case a good decision. Rather, it should be used with other to take decisions more effectively. Companies may go for simulations over past several years' performance to find out the areas where EVA as a managerial tool is stronger over others; and where other tools show importan correlations. Then, a set of tools can be used simultaneously in line with the philosophy of management.

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