

EARNINGS PER SHARE (EPS) - AS 20

Presentation

by

S RAMANUJAM

Executive Vice President - Group Taxation
The UB Group

1

EARNINGS PER SHARE (EPS) - AS 20

PRELIMINARY

**ACCOUNTING STANDARDS - CAN
IT EVER BE SIMPLIFIED?**

ARE WE LEARNING BASE-BALL?

2

EARNING PER SHARE (EPS) - AS 20

**EFFECTIVE DATE: IN RESPECT OF
ACCOUNTING PERIODS
COMMENCING FROM 1.4.2001 &
ONWARDS**

**MANDATORY : FOR ENTERPRISES
WHOSE SHARES OR POTENTIAL
EQUITY SHARES LISTED ON
RECOGNISED STOCK EXCHANGES**

3

OBJECTIVE

**EPS WILL IMPROVE COMPARISON OF
PERFORMANCE OF DIFFERENT
ENTERPRISE FOR THE SAME PERIOD &
DIFFERENT ACCOUNTING PERIOD FOR
THE SAME ENTERPRISE**

**IF CONSOLIDATED ACCOUNTS ARE
PREPARED THEN EPS SHOULD BE
PREPARED ON THE BASIS OF
CONSOLIDATED STATEMENTS**

4

DEFINITIONS

POTENTIAL EQUITY SHARE - EXAMPLE

- **CONVERTIBLE WARRANTS**
- **CONVERTIBLE DEBENTURES**
- **PREFERENCE SHARES**
- **STOCK OPTIONS**

5

PRESENTATION ON THE FACE OF P&L

SHOULD PRESENT BOTH

- **BASIC EPS AND**
- **DILUTED EPS**

(EVEN IF IT IS A LOSS)

6

BASIC EPS

BASIC EPS = $\frac{\text{PROFIT / LOSS FOR THE PERIOD}}{\text{WEIGHTED AVERAGE NUMBER OF COMMON EQUITY SHARES OUTSTANDING}}$

PROFIT / LOSS = PROFIT (-) PREF. DIVIDEND (-) TAX

DENOMINATOR : (PER SHARE) - MEANS

EQUITY SHARES OUTSTANDING AT THE BEGINNING

(+) EQUITY BOUGHT BACK / ISSUED X
TIME WEIGHTING FACTOR

(SEPARATE ILLUSTRATION FOR BONUS SHARES / PARTLY PAID SHARES / RIGHTS SHARES ARE GIVEN IN THE STANDARD)

7

DILUTED EARNINGS PER SHARE

DILUTED EARNINGS PER SHARE =

NET INCOME AVAILABLE TO COMMON SHAREHOLDERS + NET OF TAX INTEREST / DIVIDEND SAVING ON CONVERTIBLE SECURITIES

WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING + EFFECT OF CONVERTIBLE SECURITIES + NET EFFECT OF STOCK OPTIONS

8

EXTRACTED FROM KOTHARI SUGARS(BIFR CO.)

	31.3.2003	31.3.200
LOSS BEFORE EXCEPTIONAL ITEM	(6,020.38)	(2,816.36)
LESS: EXCEPTIONAL ITEM-RELEIF ON ONE TIME SETTLEMENT OF DEBTS	3,532.89	-
LOSS FOR THE YEAR	(2,487.49)	(2,816.36)
ADD: BALANCE BROUGHT FORWARD	(20,867.53)	(18,051.17)
BALANCE CARRIED TO THE BALANCE SHEET	(23,355.02)	(20,867.53)

EARNING PER SHARE – BASIC AND DILUTED (RS.)		
FACE VALUE OF RS. 10/- :		
- BEFORE EXCEPTIONAL ITEM	(41.88)	(20.21)
- AFTER EXCEPTIONAL ITEM	(18.18)	(20.21)

KOTHARI SUGARS (CONTD)

- **THERE ARE NO POTENTIAL EQUITY SHARES AND HENCE, THE BASIC AND DILUTED EPS ARE THE SAME**
- **NUMERATOR : THE COMPANY HAS ONLY ONE CLASS OF EQUITY - HENCE THE NET LOSS FOR THE YEAR AS INCREASED BY PREFERENCE DIVIDEND DUE AND DIVIDEND TAX THEREON ON CUMULATIVE PREFERENCE SHARES FOR THE CURRENT YEAR IS USED FOR COMPUTATION OF EPS**

KOTHARI SUGARS (CONTD)

- **DENOMINATOR : THE NUMBER OF EQUITY SHARES IS USED AS THE DENOMINATOR**

11

KOTHARI SUGARS (CONTD)

PAID UP CAPITAL

<u>PREFERENCE SHARES</u>			RS/LCS
200,000	16%	CUM.PREF. SHARES OF RS. 100/- EACH	200.00
1,000,000	13.5%	CUM.PREF. SHARES OF RS. 100/- EACH	1,000.00
2,000,000	13.5%	CUM.PREF. SHARES OF RS. 10/- EACH	200.00
<u>EQUITY SHARES</u>			
14,897,092		EQUITY SHARES OF RS. 10/- EACH	1,489.71

12

**BASIC & DILUTED EARNINGS PER SHARE (EPS) -
(EXTRACTED FROM L&T BALANCE SHEET - YE 31.3.2003**

BASIC PARTICULARS		<u>2002-03</u>	<u>2001-02</u>
P.A.T. (RS/CRS)	A	433.10	346.80
NUMBER OF SHARES SUBSCRIBED	B	24,86,68,756	24,86,60,346
BASIC EPS (RUPEES)	A/B	17.42	13.95
DILUTED:			
PROFIT AFTER TAX	A	433.10	346.80
ADD: INTEREST (NET OF TAX) ON LOAN CONVERTIBLE TO EQUITY SHARES	B	4.31	7.94
		-----	-----
ADJUSTED PROFIT FOR DILUTED EARNINGS PER SHARE	C=A+B	437.41	354.74
		=====	=====

13

L & T - CONTINUED

NUMBER OF SHARES SUBSCRIBED	D	24,86,68,756	24,86,60,346
ADD: POTENTIAL EQUITY SHARES:			
ON CONVERSION OF LOANS	E	5,24,02,500	9,02,48,750
THAT COULD ARISE ON CONVER- SION OF SERIES IV DEBENTURES	F	3,88,956	3,91,651
ON ACCOUNT OF STOCK APPRE- CIATION RIGHTS & OPTIONS	G	1,13,80,395	77,17,202
		-----	-----
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING		31,28,40,607	34,70,17,949
		=====	=====
DILUTED EPS (RUPEES)	C/H	13.98	10.22

14

LIMITATIONS OF EPS AS A PERFORMANCE MEASURE

▶ AN ENTITY'S EARNINGS ARE AFFECTED BY ITS CHOICE OF ACCOUNTING POLICIES

▶ WHERE NEW SHARES ARE ISSUED FOR CASH OR AS CONSIDERATION FOR AN ACQUISITION, THE ADDITIONAL SHARES ARE TO BE TAKEN INTO ACCOUNT FROM THE DATE OF ISSUE. NORMALLY NEW SHARES START EARNING INCOME MUCH LATER.

▶ NEW SHARE ISSUE IS OFTEN ACCOMPANIED BY A DECREASE IN EPS

15

LIMITATIONS OF EPS AS A PERFORMANCE MEASURE (CONTD)

▶ EPS CANNOT BE USED AS A BASIS OF COMPARISON BETWEEN COMPANIES AS THE NUMBER OF SHARES IN ISSUE IN ANY PARTICULAR COMPANY IS NOT RELATED TO THE AMOUNT OF CAPITAL EMPLOYED

▶ THE DILUTED EPS (DEPS) IS A THEORETICAL MEASURE OF THE EFFECT OF DILUTION ON THE BASIC EPS. THERE IS NO EVIDENCE TO SUGGEST THAT EVEN THE MOST SOPHISTICATED ANALYSTS USE DEPS. THIS IS BECAUSE OF ITS HYPOTHETICAL NATURE

▶ 'BUYBACK OF SHARES' BY COMPANIES WITH A VIEW TO BOOST EPS

16

LIMITATIONS OF EPS AS A PERFORMANCE MEASURE (CONTD)

▶▶ REPORTED EARNINGS CAN BE VIEWED AS HAVING TWO COMPONENTS. ONE, THE EPS ON OPERATING INCOME. THE OTHER INCLUDING THAT OF THE NON OPERATING INCOME.

▶▶ REPORTED EPS SHOULD BE SEGREGATED INTO THESE TWO COMPONENTS FOR EPS TO HAVE A MEANINGFUL PREDICTIVE VALUE AS TO THE FUTURE PROSPECTS OF THE REPORTING ENTITY.

17

UNCOMMON FEATURES IN AS 20

▶▶ INCLUDE ALL ITEMS OF INCOME AND EXPENDITURE INCLUDING TAX EXPENSE & EXTRA-ORDINARY ITEMS

▶▶ PEF. DIVIDEND IN RESPECT OF CUMULATIVE PEF. SHARES DOES NOT INCLUDE PEF. DIVIDEND DECLARED IN RESPECT OF PREVIOUS PERIODS

▶▶ EMPHASIS IS TO LOOK AT EQUITY SHARES OUTSTANDING DURING THE PERIOD

▶▶ WEIGHTED AVERAGE : NO. OF DAYS TO BE ADOPTED

18

UNCOMMON FEATURES IN AS 20 (CONTD)

▶ **AMALGAMATION**

IN THE NATURE OF PURCHASE : DATE OF ACQUISITION

IN THE NATURE OF MERGER : FROM THE BEGINNING
OF THE REPORTING
PERIOD

19

UNCOMMON FEATURES IN AS 20 (CONTD)

▶ **BONUS SHARES**

NO NEED TO LOOK AT THE DATE OF ISSUE OF
BONUS

▶ **RIGHTS SHARES**

THIS ASSUMES A BONUS PRICE ADVANTAGE -
RIGHTS PRICE IS LOWER THAN THE MARKET
PRICE

20

UNCOMMON FEATURES IN AS 20 (CONTD)

▶ SHARE APPLICATION MONEY PENDING ALLOTMENT SHOULD BE TREATED AS DILUTIVE POTENTIAL EQUITY SHARES

▶ WHEN RESULTANT CONVERSION OF INTEREST EXPENSE RELATING TO POTENTIAL EQUITY SHARES RESULTING IN INCREASE IN PROFIT MAY LEAD TO A NON-DISCRETIONARY EMPLOYEE PROFIT SHARING PLAN - MAKE THE ADJUSTMENT

▶ MEANING OF THE TERM 'DILUTIVE'?

21

UNCOMMON FEATURES IN AS 20 (CONTD)

▶ DILUTED EARNINGS PER SHARE =

ASSUMED PROCEEDS FROM THE ISSUE OF SHARES SHOULD BE CONSIDERED TO HAVE BEEN RECEIVED FROM THE ISSUE OF SHARES AT FAIR VALUE

FAIR VALUE =

AVERAGE OF 6 MONTHS WEEKLY CLOSING PRICE

22

UNCOMMON FEATURES IN AS 20 (CONTD)

▶▶ INCLUDE CONVERTIBLE SECURITIES IN EPS CALCULATIONS UNDER THE “IF CONVERTED” METHOD. UNDER THE METHOD, THE SECURITIES ARE ASSUMED TO HAVE BEEN CONVERTED AT THE BEGINNING OF THE PERIOD WITH A CORRESPONDING ADDITION OF INTEREST TO THE INCOME

▶▶ MEANING OF THE TERM - “ANTI-DILUTIVE”

23

DISCLOSURE

▶▶ COMPUTE BASIC PLUS DILUTED EPS ON THE BASIS OF EARNINGS EXCLUDING EXTRA-ORDINARY ITEMS (NET OF TAX EXPENSE) AND

▶▶ AMOUNT USED AS THE NUMERATOR WITH REGARD TO BASIC + DEPS (TO RECONCILE WITH P&L)

▶▶ WEIGHTED AVERAGE NO. OF EQUITY SHARES USED AS DENOMINATOR & RECONCILIATION WITH BASIC + DEPS

24

DISCLOSURE (CONTD)

▶▶ **NOMINAL VALUE OF SHARES ALONG WITH EPS FIGURES**

NOTE: ICAI HAS INDICATED THAT SMALL & MEDIUM COMMERCIAL ENTERPRISES WILL BE EXEMPTED FROM COMPLYING WITH AS 20

25

SUMMARY

EARNINGS PER SHARE

▶▶ **FIRST AMERICAN PRONOUNCEMENT WAS ISSUED IN 1969; INDIAN GAP ISSUED IN 2001**

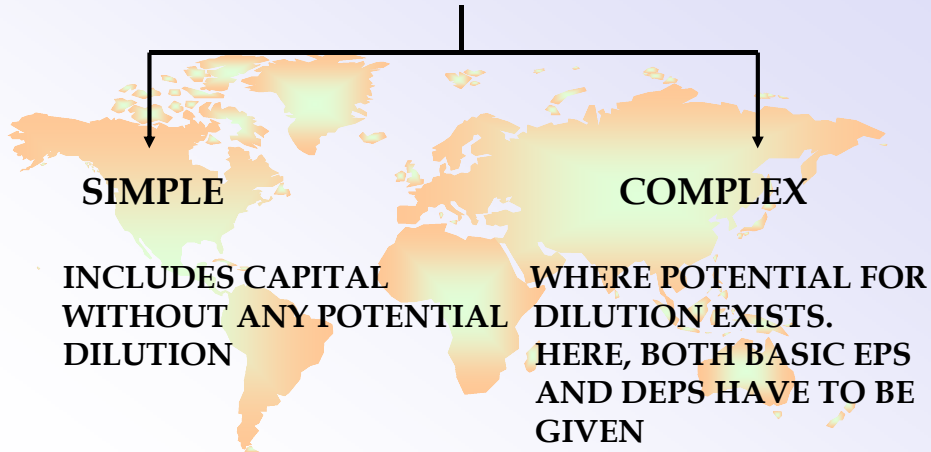
▶▶ **CORRESPONDING AMERICAN STANDARD IS FAS 128; CORRESPONDING STANDARD IN IAS IS IAS 33**

▶▶ **POTENTIAL REDUCTION IN EPS FIGURE IS CALLED DILUTION**

26

SUMMARY CONTD/-

CAPITAL STRUCTURE



27

SUMMARY CONTD/-

- ▶▶ EPS CALCULATED ON THE BASIS OF SHARES OUTSTANDING
- ▶▶ ANTI-DILUTION REFERS TO INCREASE IN EPS OR DECREASE IN LOSS PER SHARE; IF POTENTIAL COMMON SHARES INCREASE THE EPS, THEY ARE ANTI-DILUTIVE AND HENCE, WILL NOT FORM PART OF DILUTED EPS

28

