Session : 2019-20

M.COM.- FIRST YEAR

(II SEMESTER)

CORPORATE FINANCIAL ACCOUNTING

(I-2002)

UNIT – IV : CORPORATE FINANCIAL REPORTING

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LEARNING OBJECTIVES

After you have gone through this unit, you should be able to describe –

- Meaning of Corporate Financial Reporting (***CFR***);
- Types of Corporate Financial Reporting;
- Annual Corporate Report (***ACR***) : Meaning, contents & significance;
- Factors compelling ***CFR***;
- Objectives of ***CFR***;
- Value Added Statement (***VAS***): Meaning, Difference between Value Added & Profit, Advantages & Weaknesses of ***VAS***;
- Gross Value Added (***GVA***) **v/s** Net Value Added (***NVA***)
- Economic Value Added (***EVA***) : Meaning, Components, Benefits and Drawbacks, VA **v/s** EVA;
- Market Value Added (***MVA***);
- Shareholder Value Added (***SVA***).

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MARKET VALUE ADDED (*MVA*)

► It is a difference between the current market value of a company and the capital contributed by all investors.

► As MVA represents the NPV of a series of EVA values hence these are said to be closely related.

FORMULA

MVA = Market Value of Capital

(-)

Capital Invested

► The higher the MVA, the better.

► It is an indication of company's capacity to increase shareholder value over time.

MARKET VALUE ADDED (*MVA*)

In other words,

MVA can be interpreted as :

“ The amount of wealth created by the management for its investors over and above their investment in the company.”

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HIGH v/s LOW
MVA

► The aim of the company should be to maximize MVA instead of maximizing the value of the company.

► The reason is that the value of the company can be easily maximized by investing ever-increasing amounts of capital .

► A ***high*** MVA is an evidence of –

(i) effective management and **(ii)** strong operational capabilities.

► It indicates that the company has created substantial wealth for its shareholders.

HIGH v/s LOW
MVA

- A ***low*** MVA means -

$$V_1 < V_2$$

V_1 = **Value of management's action and investments.**

V_2 = **Value of the capital contributed by shareholders.**

— VE *MVA*

- A ***negative*** MVA means that the management's actions and investments have diminished and reversed the value of capital contributed by shareholders.

EVA v/s *MVA*

► The relationship between these two (i.e. **EVA & MVA**) is more complicated as compared to the relationship between **EVA and Firm Value** (*or say*, Market Value of a firm).

► Market value of a firm reflects not only the Expected EVA of Assets in place but also the Expected EVA from future projects.

► The Market Value can decrease even though the EVA is higher if the

Actual EVA < Expected EVA

EVA v/s *MVA*

► This does not mean that increasing EVA is bad from a corporate finance point of view. Rather, if a firm is given a choice between –

(i) Delivering a **"Below-Expectation"** EVA and

(ii) "No" EVA at all

the firm should go with **(i)** option i.e. it should deliver the "Below-Expectation" EVA b'coz an old saying is that ***" Something is better than Nothing"***.

► For firms with **high** anticipated growth (and excess returns), the **correlation** between increasing year-to-year EVA and market value will be **weaker**.

► But the result will altogether be different (i.e. correlation will be **stronger**) for firms with **low** *or* **no** anticipated growth.

VA **v/s** ***EVA***

BASIS OF DIFFERENCE

1. MEANING
2. PURPOSE
3. FOCUS
4. INFORMATION
5. TIME VALUE OF MONEY
6. COMPUTATION

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VA **v/s** ***EVA***

1. **MEANING**

- ***VA*** is the **wealth** that a firm has been able to create through the collective effort of **CME** (i.e. **C**apital, **M**anagement & **E**mployees)
- ***EVA*** is the **surplus** generated by an entity after meeting an equitable charge towards the providers of Capital.

VA v/s *EVA*

2. PURPOSE

- ***VA*** provides a useful measure in **analysing the performance and activity** of the reporting entity.
- ***EVA*** is a management tool that helps managers in taking **decisions** which finally increase the shareholders' wealth.

VA **v/s** ***EVA***

3. FOCUS

- ***VA*** focuses on the performance of firm and contribution towards **various groups**.
- ***EVA*** focuses on firm's ability to create surplus above **shareholders' expectations**.

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VA v/s *EVA*

4. INFORMATION

- ***VA*** reporting is based on the Profit & Loss account information, which is primarily an **internal data**.
- ***EVA*** reporting uses **market information** and estimates like Cost of Capital, Beta, Risk Free Rate of Return *etc*.

VA **v/s** ***EVA***

5. TIME VALUE OF MONEY

- ***VA*** does not recognize time value of money, since it deals with the wealth created by the firm during a specified time period e.g. a financial year.

- ***EVA*** recognizes time value of money through the use of ***WACC*** in reporting. The WACC is based on the Present Value (***PV***) of future interest / dividend outflows.

VA v/s *EVA*

6. COMPUTATION

- ***VA*** = **Market Price of a Firm's Output**

(-)

Cost of Bought in Materials & Services

- ***EVA*** = **NOPAT**

[i.e. EBIT (1-Tax Rate)]

(-)

(INVESTED CAPITAL* x WACC)

{* Also known as **Capital Employed.**}

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REFERENCE BOOKS

1. **Warren/Reeve/Duchac's Corporate Financial Accounting 13E and CengageNOW™v2! Market-leading Corporate Financial Accounting (ISBN-13: 978-1285868783 ISBN-10: 1285868781)**
2. **International Journal of Accounting and Finance (ISSN online:1752-8232 ISSN print: 1752-8224)**
3. **Shukla S.M. & Gupta K.L., Corporate Financial Accounting (Sahitya Bhawan Publications)**
4. **Gupta K.G., Corporate Financial Accounting (K.G.Publications)**
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6. **Maheshwari S.N., Advanced Accounting – Vol.II, (Vikas Publishing House)**
7. **Shukla M.C. & T.S.Grewal, Advanced Accountancy (Sultan Chand & Co.)**
8. **Jain & Narang, Financial Accounting (Kalyani Publishers)**

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THANKS!