# Part A : Valuation of Share of a Closely Held Company ( including Debt)

# Part B : Valuation under Various Legislations

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# Part B : Valuation under Various Legislations

## Contents

## 1. Background of the Case and Purpose

M/s K Electro-Chemicals Private Limited, (KECPL), New Delhi, India incorporated in New Delhi in April, 1991 is a joint venture between M/s S GmbH, Germany and Indian promoters holding 49% and 51% respectively, of the total paid up equity share capital of the JV Company. The business of the Company is manufacturing, development and marketing of electroplating and special /other chemicals for cleaning, pretreatment, finishing and post-treatment and other related applications.

The Company had incurred losses since the joint venture was done for many years as the technology for manufacture of pre treatment chemicals offered by the foreign collaborator did not succeed in Indian market. In last few years, Indian Promoter developed a process which was giving good results, specially in export markets.

Conflict had arisen between the parties as Indian Promoters wanted to explore and focus on Export markets with his Indian technology whereas the foreign collaborator wanted this JV Company to confine to Indian Market only as he already had JVs/ WOS in many parts of the world using his technology. Indian JV Company going abroad with Indian technology was in direct conflict with the interests of the foreign collaborator abroad in many countries.

M/s S GmbH has offered to sell its entire 49% equity share holding in the Company comprising of 147,000 equity shares to the Indian promoters. The Indian Promoter Mr. YPB is willing to acquire the stake.

The Indian Promoter Mr. YPB has approached us for carrying out a valuation of Equity Share of the Company in connection with the aforesaid proposal of disinvestment of equity shares by foreign investors and proposed acquisition of the stake by him.

## 2. The Valuation Assignment / Engagement

### Client and Valuer

Client : Mr. YPB of New Delhi, India, the majority owner ( 51%) of KECPL and Potential Buyer of minority stock (49%) in KECPL.

Valuer : Group of Individuals consisting of Manoj Aggarwal, Tarun Sharma, Jitesh Bhugra and Megha Almadi ( all Chartered Accountants) of New Delhi.

### Date of Retention

We have been retained by Mr. X in terms of our engagement letter w.e.f. 21st December, 2008, the date engagement letter is signed by him, requiring our assistance in determining the value of equity shares of KECPL, on Non Marketable Minority basis for possible acquisition of minority stock of KECPL by him.

### Definition of Property to be Valued

Business Entity
KECPL, incorporated in New Delhi, is a closely held private company.

Subject Interest to be Valued
Non-Marketable Minority Value (NMV) for 49% interest in the Closely held Private Company namely KECPL's Equity Share Capital.

### Ownership Characteristics

Control or Minority
Minority value is sought.
49% shares are held by the foreign collaborator and the balance 51% shares are held by Indian promoter.

Marketability
KECPL is a closely held Private Limited Company. Both the parties have the right of first refusal in case the any party wants to exit and sell its block of shares. There are no options to buy or sell.

### Effective date of Valuation

The effective date of valuation is 31st December,2008.

## Purpose of Valuation

For Transaction- Possible acquisition of minority stock in KECPL.

## Standard ( Definition) of Value

The Standard of Value is " Fair Market Value". As defined by Statement on Standards for Valuation Services Issued by the AICPA, "the Fair Market Value is-

•the price, expressed in terms of cash equivalents
• at which property would change hands
• between a hypothetical willing and able buyer and a hypothetical willing and able seller
• Acting at arms length in an open and unrestricted market,
•when neither is under compulsion to buy or sell and
•when both have reasonable knowledge of the relevant facts."

## Premise of Value

The Premise of Value is "as a going concern"

## 3. Revenue Ruling 59-60

According to Internal Revenue Service's Revenue Ruling 59-60, the following are the 8 main tenets of value to be considered in valuing shares of the capital stock of closely held corporations:

1. The nature of the business and history of the enterprise from its inception.
2. The economic outlook in general and condition and outlook of the specific industry in particular.
3. The book value of the stock and the financial condition of the business.
4. The earning capacity of the company.
5. The dividend-paying capacity of the company.
6. Whether the enterprise has goodwill or other intangible value.
7. Sales of the stock and size of the block to be valued.
8. The market prices of stock of corporations engaged I the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over the counter.

These eight factors are fundamental to any appraisal of closely held securities. They are not, however, all-inclusive. All other factors relevant to the subject valuation must also be considered.

## 4. Valuation Methodologies and Approach

We have considered the following methodologies in this case :

A. Adjusted Net Asset Method ("NAV")

B. Discounted Cash Flow- APV Approach

C. Relative Valuation- Public Guideline Company Method

D. Statutory Valuations
- D.1 CCI
- D.2 FEMA

## A. Adjusted Net Asset Method ("NAV")

### Methodolgy

It is a method within the Asset Approach whereby all assets and liabilities (including off-balance sheet, intangible and contingent) are adjusted to their fair market values. The net of adjusted asset minus liability values is the indicated value of equity.

### Control Vs. Minority

This method generally produce a control value since minority interest holders have no direct claim on the asset and can not force their disposition or utilization. Furthermore, the asset approach typically provides a value indication stated on marketable basis.

If this method is used in valuing a minority interest of a closely held company, the value indication derived will have to be adjusted from control to minority and depending on the facts and circumstances, from a marketable to non marketable. It follows that asset value usually must be discounted for both lack of control and lack of marketability.

## Valuation

We have used this method to compute NMV as follows :

| | Premise of Value : Going Concern<br>Standard of Value : FMV | Amount As at 31.3.08 (Audited) ( Book Values) | Amount Valuation Adjustments | Amount As Adjusted FMV |
|---|---|---|---|---|
| | | Rs/lacs | Rs/lacs | Rs/lacs |
| **A.** | **Immovables Fixed Assets** | | | |
| 1 | Factory Land & Building | 44.87 | 28.03 | 72.90 |
| 2 | Office premises | 1.08 | 8.67 | 9.75 |
| | Sub Total | 45.95 | 36.70 | 82.65 |
| **B.** | Other fixed Assets( at book value) | 13.90 | 0 | 13.90 |
| **C.** | Total Fixed Assets ( A+B) | 59.85 | 36.70 | 96.55 |
| **D.** | Current Assets, Loans & Advances | 97.61 | 0 | 97.61 |
| **E.** | Total Assets (C+D) | 157.46 | 36.70 | 194.16 |
| **F.** | Current Liabilities & Provisions | 38.93 | 0 | 38.93 |
| **G.** | Unsecured Borrowings | 68.36 | 0 | 68.36 |
| **H.** | Deferred Tax liability, Net | | | |
| | On Increase in Immovable Assets | | 12.47 | |
| | Less : Deferred Tax Assets on Unabsorbed Losses etc. | | (6.63) | |
| | Net Deferred Tax Liability | 0.00 | 5.84 | 5.84 |
| **I.** | **Net Assets (E-F-G-H)** | **50.17** | **30.86** | **81.02** |
| | **Represented By :** | | | |
| | Share Capital | 30.00 | 0 | 30.00 |
| | Share premium | 58.80 | 0 | 58.80 |
| | Less Debit Balance in Profit & Loss a/c | (38.63) | 30.86 | -7.77 |
| **J.** | **Net worth** | **50.17** | **30.86** | **81.03** |
| **K.** | No. of Equity Shares ( Rs. 10/- per | 300,000 | | 300,000 |

| | | | | |
|---|---|---|---|---|
| | share) | | | |
| **L.** | **Value per Share ( Rs./ Share)** | **16.72** | | **27.01** |

**UNDERLYING ASSUMPTIONS :**

1. Market Value of Factory Land & Building and Office Premises has been taken based on Valuation Reports of an approved Valuer
2. Deferred Tax Liability on increase in value of immovable properties has been taken @ 33.99% (being the income tax rate on companies).

## Discounts

- **DLOC**

  49% is the largest minority block of stock and is sufficient to suppress a merger, liquidation or restructure, to block any special resolution and sufficient to affect the Board of directors. The remaining interest/ownership in the Company is, however, concentrated in one hand.

  As such, a smaller discount (DLOC) of 15% is applied, subjectively derived and based on judgement.

- **DLOM**

  Considering the following factors-
  Large block of stock,
  Ease of information access and reliability, and
  Absence of any restrictions on transfer ( Control owners have just a right of first refusal),

  A discount of 25% (below average discount of 35%), subjectively derived and based on judgement, is considered appropriate.

## Value Indication

Total discounts works out to 36% and the Non-Marketable Minority Value (NMV) indication, as per the aforesaid method, is Rs. 51.65 lacs.

## B . Discounted Cash Flow Method ( Income Approach)

The income approach is the the most widely recognized and utilized approach to valuing an entity.

### Cost of Capital Approach Vs. Adjusted Present Value Approach

In the Cost of Capital Approach, we begin by valuing the firm, rather than equiy. The future expected net cash flows to the firm are discounted at the WACC to obtain the present value of the firm which when reduced by the market value of outstanding debt yields value of equity. An implicit assumption here is that debt ratios stay unchanged forever.

In the Case Study, KECPL has a foreign currency (Euro) outstanding debt repayable in 5.5 years in equal yearly installments. The outstanding debt will reduce every year and become zero after 5.5 years. In this situation, Cost of Capital approach will not work and we need to use Adjusted Present Value Approach.

### Adjusted Present Value Approach (APV)- Methodolgy

APV approach is more practical when firms are evaluating an absolute amount of debt while the Cost of Capital approach is easier to use when firms are analyzing debt proportions.

In this approach, Valuation is done in pieces as follows :

(i) First, Value of Unlevered firm is estimated as if it had no debt. This is done by discounting the future expected net cash flows to the firm at the unlevered cost of equity.

(ii) Calculate present value of expected tax benefit that flow from a given amount/level of debt. Pre tax market cost of debt is used as a Discount rate.

(iii) Calculate Present value of expected bankruptcy cost.

(iv) Value of Firm = Value of Unlevered firm+ PV of Tax benefits – PV of Expected Bankruptcy cost.

We have used this APV Approach in determining the Value Indication.

### Normalization of Historical results and Averaging

(a)Normalized three years Historical results.

(b)Since there is no discernible trend in the profits during the past years, the weighted average of historical results ( EBIT) for the last 3 years have been taken.

## Forecasting future cash flows to invested capital (Free Cash Flow) :

Growth Rates : Initial Growth rate ( Short term) – 20% in EBIT for 6 years and thereafter till perpetuity ( Long term Growth rate) – 5%. Blended Growth rate works out to 11.34%.

Initial and Terminal Growth rates have been assumed /estimated based on historical and projected growth rates of the subject Company according to the Company's management, as well as the estimated growth rate of the chemical industry and the economy (considering present GDP growth rate of about 7% and Inflation rate of about 7%) and based on qualitative judgment of the undersigned valuers.

| **Free Cash Flow** | | | | |
|---|---|---|---|---|
| | **2008-09 Expected Cash Flow** | **2007-08 Normalized Rs/lacs** | **2006-07 Normalized Rs/lacs** | **2005-06 Normalized Rs/lacs** |
| Revenue | | 190.00 | 139.33 | 118.60 |
| Less Costs | | 155.65 | 114.99 | 85.91 |
| EBITDA | | 34.35 | 24.34 | 32.69 |
| Less Depreciation | | 7.00 | 7.62 | 8.42 |
| EBIT | | 27.35 | 16.72 | 24.27 |
| **Weights assigned** | | 3 | 2 | 1 |
| **Products** | | 82.05 | 33.44 | 24.27 |
| **Weighted Average** | **23.29** | | | |
| **Expected EBIT taking growth of 20%** | **27.95** | | | |

| | | | | |
|---|---|---|---|---|
| Less : Tax assumed @ 33.99% | **9.50** | **9.30** | **5.68** | **8.25** |
| **Earnings after Taxes** | **18.45** | **18.05** | **11.04** | **16.02** |
| Less : Interest & Finance Charges ( Net of Tax) | 3.39 | 2.87 | 2.90 | 3.29 |
| **PAT** | **15.06** | **15.18** | **8.13** | **12.73** |
| Less : ( Capex- Depreciation) | 1.00 | -6.53 | | |
| Less : Increase in Working Capital | 1.50 | 8.35 | | |
| Less : Debts repaid | 11.04 | 4.37 | | |
| **Net Cash Flow to Equity** | **1.52** | **8.99** | | |

**Estimating Unlevered Beta**

**Steps :**

(a) Collect a group of publicly traded comparable firms, preferably in the same line of business, but more generally, affected by the same economic forces that affect the firm being valued.

(b) Calculate the unlevered beta for all the firms by using the formula :

Beta unlevered = Beta Levered / (1 + (1 - tax rate) (Debt/Equity))

(c) Compute Airthmatic Mean of Unlevered Betas.

(d) Estimate an Unlevered cost of equity based upon this beta.

| S No. | Company Name | Levered Beta | Debt | Equity (Market) | D/E Ratio | Unlevered Beta Tax @ 33.99% |
|---|---|---|---|---|---|---|
| 1 | Grauer & weil | 1 | 666.34 | 531.33 | 1.25 | 0.55 |
| 2 | Alkhli Metals | 0.7 | 255.47 | 170.56 | 1.50 | 0.35 |
| 3 | Ciba India | 0.5 | 240.66 | 266.4 | 0.90 | 0.31 |
| 4 | Gulshan | 0.5 | 336.69 | 712.86 | 0.47 | 0.38 |
| 5 | Jayant Aqro | 0.9 | 1161.75 | 614.25 | 1.89 | 0.40 |
| 6 | Panama | 1.1 | 67.43 | 342.86 | 0.20 | 0.97 |
| 7 | Pidilite | 0.6 | 5025.98 | 27913.3 | 0.18 | 0.54 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 8 | Transpek | 0.4 | 369.76 | 270.3 | 1.37 | 0.21 |
| 9 | United Phosphorus | 0.8 | 15348.20 | 25538.6 | 0.60 | 0.57 |
| | | 6.50 | | Total | | 4.29 |
| | | **0.72** | **Unlevered Beta - Airth.Mean** | | | **0.48** |

Beta less than I implies that the total return for the subject security moves in the same direction as the market but with less magnitude.

If there are no reasonably similar companies whose betas could be used as a proxy for the small closely held company, then the Build Up method may be the best to use. However, if betas are reasonable and can be used, then MCAPM may be considered as well. Each of these situations is facts and circumstances specific and could differ depending on the type of company, the industry and the size of company.

Considering the fact that aforesaid guideline public companies may not be sufficiently comparable and some of them are diversified too and large in size as compared to the subject company, we have taken a beta of 1.0 based o qualitative judgment of the valuers. It means that the total return for the subject security moves in tandem with the total return of the market.

When Beta is 1.0, then Modified CAPM model of cost of equity becomes identical with Build Up Model.

### Estimating Unlevered Cost of Equity

We have used Modified CAPM (or Build Up Model as the Beta is 1.0) as follows :

| | |
|---|---|
| Risk Free return<br>( return on a 10 years 8.24% 2018 Govt. Bonds | 7.00% |
| Expected return on a well diversified Market Portfolio<br>( cumulative average BSE 500 return since inception) | 14.00% |
| Unlevered Beta | 1.00 |
| Risk Premium for Small Size ( assumed) | 4.00% |
| Company Specific risk Premium ( assumed) | 4.00% |
| Cost of Equity<br>( being return required by an investor) | **22.00%** |

## Valuation of Debt

KECPL has a foreign currency (Euro) outstanding debt of Euro 98,895 ( INR Rs. 68.36 lacs) repayable in 5.5 years in equal yearly installments of Euro 21,240. The outstanding debt will reduce every year and become zero after 5.5 years.

## Computation of Cost of Debt

The actual rate a business entity pays on interest-bearing debt is the pretax cost of debt, assuming the firm is borrowing at market/current rates. If there is some long term debt at rates different from the prevailing market, market rates may be estimated by risk analysis of the subject compared with yields on public debt of comparable risk. In this situation, simply calling a banker often works as well. Since interest on debt is tax deductible, after-tax cost of debt ( market rate multiplied by one minus the Company's tax rate) is a relevant cost to the company.

We have computed Cost of Debt as follows :

| | | |
|---|---|---|
| Interest rate in Euro | | 5.334% |
| Spot Rate | Rs./Euro | 69.1275 |
| Forward ( one year) | Rs./Euro | 70.5584 |
| Interest rate in INR using Interest Rate Parity Theorem | | 7.5144% |
| Forward cover premium cost | | 2.18% |
| Pretax Actual Cost of Debt | | 7.5144% |
| Current Market Cost of Debt | | 10% |
| Tax Rate | | 33.99% |
| Market Cost of Debt ( After Tax) | | **6.60%** |

## Computation of Market Valuation of Debt :

The Actual Cash flows to the Debt –holders (principal as well as interest) are discounted at the pretax Cost of Debt (at market rate) to arrive at the present market value of debt. We have computed market value of debt in this case as follows:

| Principal Outstanding -INR | 68.36 | **31.3.09** | **31.3.10** | **31.3.11** | **31.3.12** | **31.3.13** | **31.3.14** |
|---|---|---|---|---|---|---|---|
| Payments to Debt Holders | | | | | | | |
| Principal Repayments | | 11.04 | 11.62 | 12.24 | 12.90 | 13.59 | 6.97 |
| Interest Payments ( Gross) | | 3.65 | 3.06 | 2.44 | 1.78 | 1.10 | 0.37 |
| Other Costs ( Forex Variations) payment | | 1.49 | 1.25 | 1.00 | 0.73 | 0.45 | 0.15 |
| Total Cash Flows received by Debt Holders | | 16.17 | 15.93 | 15.68 | 15.41 | 15.13 | 7.49 |
| Discount Factor ( being Pretax Actual Cost of Debt) | 7.51% | 0.93 | 0.87 | 0.80 | 0.75 | 0.70 | 0.65 |
| Present Value | | 15.04 | 13.78 | 12.62 | 11.53 | 10.53 | 4.85 |
| Total Present Value of Debt | 68.36 | | | | | | |
| Discount Factor ( being Pretax Market Cost of Debt) | 10.00% | 0.91 | 0.83 | 0.75 | 0.68 | 0.62 | 0.56 |
| Present Value | | 14.70 | 13.17 | 11.78 | 10.53 | 9.40 | 4.23 |
| **Total Present Market Value of Debt** | **63.80** | | | | | | |

## APV Value of Firm

| **Step 1 : Compute Unlevered Value of firm** | | **31.3.09** | **31.3.10** | **31.3.11** | **31.3.12** | **31.3.13** | **31.3.14** | **Perpetuity** |
|---|---|---|---|---|---|---|---|---|
| NOPLAT | | 18.45 | 22.14 | 26.57 | 31.88 | 38.26 | 45.91 | 48.21 |
| Less : ( Capex- Depreciation) | | 1.00 | 2.00 | 3.00 | 4.00 | 5.00 | 5.00 | 10.00 |
| Less : Increase in Working Capital | | 1.50 | 1.80 | 2.16 | 2.59 | 3.11 | 3.73 | 3.92 |
| Net Cash Flow to Invested Capital ( FCFF) | | 15.95 | 18.34 | 21.41 | 25.29 | 30.15 | 37.18 | 34.29 |
| Terminal Value | | | | | | | | 201.70 |
| Discount Factor | 22.00% | 0.82 | 0.67 | 0.55 | 0.45 | 0.37 | 0.30 | 0.30 |
| Present Value | | 13.07 | 12.32 | 11.79 | 11.42 | 11.16 | 11.28 | 61.17 |
| Total Present Value ( Value of Firm) | 132.21 | | | | | | | |
| **Step 2 : Compute Tax benefits of Debt** | | | | | | | | |
| Interest cost on Debt | | 5.14 | 4.31 | 3.43 | 2.51 | 1.54 | 0.52 | 0.00 |
| Tax Benefit /Shield | 33.99% | 1.75 | 1.46 | 1.17 | 0.85 | 0.53 | 0.18 | 0.00 |
| Discount Factor ( being Pretax Market Cost of Debt) | 10.00% | 0.91 | 0.83 | 0.75 | 0.68 | 0.62 | 0.56 | 0.00 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Present Value | | 1.59 | 1.21 | 0.88 | 0.58 | 0.33 | 0.10 | 0.00 |
| Total Present Value of Tax Shield | 4.68 | | | | | | | |
| **Step 3 : Compute Value of Firm** | 136.89 | | | | | | | |
| Less :Market Value of Debt | 63.80 | | | | | | | |
| **Value of Operating Equity (Rs. /Lacs)** | **73.09** | | | | | | | |
| **Value per Share ( Rs./ Share)** | **24.36** | | | | | | | |

## Terminal Value

The terminal value refers to the present value of the business as a going concern beyond the period of projections up to infinity. The cash flows of 6th year have been used to determine the terminal value. The terminal growth rate has been taken as 5% for the Company beyond the projection period of 6 years. Based on these assumptions, the terminal value has been calculated at Rs. 201.70 lacs and its present value at Rs. 61.17 lacs.

Value of Firm = Value of Unlevered firm+ PV of Tax benefits – PV of Expected Bankruptcy cost.

**Value of Firm = 132.21 +4.68 = 136.89**
**Value of Operating Equity = Value of Firm minus Market Value of Debt**
**= 136.89 – 63.80 = Rs. 73.09 Lacs**

## Discounts

- **DLOC**
  The cash flows of KECPL do not have any control adjustments and the Company is run to the benefit of all shareholders. This may be treated as Minority Cash Flow which produces Marketable Minority Value (MMV). However, the Value is considered as Control stand alone and not MMV as policies of current owners can change and/or new owners can come in. Hence possible adjustment for DLOC is considered appropriate to reflect the risk of potential future changes in either the owner or the policies or both.

  As such, a smaller discount (DLOC) of 5% (instead of 15% in Asset Approach) is applied, subjectively derived and based on judgement.

- **DLOM**

  Because the discount rates are derived from highly liquid public market transactions, DLOM should be considered. DLOM attributable to minority interests usually are substantial – 20% to 50% is common.

  Considering the following factors-
  Large block of stock,
  Ease of information access and reliability, and
  Absence of any restrictions on transfer (Control owners have just a right of first refusal),

  A discount of 25% (below average discount of 35%), subjectively derived and based on judgement, is considered appropriate.

### Value Indication

Total discounts works out to 29% and the Non Marketable Minority Value (NMV) Value indication, as per the aforesaid method, is Rs. 52.08 Lacs.

## C. Relative Valuation- Guideline Public Company Method

### Methodology

Market multiples i.e. market value of a company's equity ( resulting in Market Value of Equity Multiple) or invested capital ( resulting in Market Value of Invested Capital or Business Enterprise Value Multiple) divided by a company measure (or company fundamental financial variable) – earnings, book value or revenue- of comparable listed companies are computed.

These multiples are adjusted based on dfifferences in subject company's growth (blended expected perpetual growth rates), size or any company specific risk vis-à-vis as those of guideline company.

Adjusted Market multiples are applied to the appropriate fundamental financial variable of the subject company to derive the indicated value.

### Market Value of Equity ( MVE) Multiples

Earnings- Price/Earning, Price/Gross Cash Flow and Price/Pretax Income
Book Value- Price/Book value
Revenue- Price/Sales

Market Value of Equity (MVE) is calculated by multiplying the share price by the total fully diluted outstanding common shares of the entity.

MVE on an operating basis is calculated by multiplying the share price by the total fully diluted outstanding common shares of the entity minus short term investments and other non operating assets plus non operating liabilities

## Market Value of Invested Capital ( MVIC) or Business Enterprise Value (BEV) Multiples

Earnings- MVIC/EBIT, MVIC/EBITDA
Book Value- MVIC/Book value of Invested Capital
Revenue- MVIC/Sales
MVIC (or Firm value) is the sum of the market value of equity, preference shares and interest bearing debt.

Business Enterprise Value (BEV) is defined as the sum of the market value of equity, debt, preference shares minus short term investments and other non operating assets plus non operating liabilities and minority interest.

## Valuation

We have searched and selected comparable companies based on Industry , computed their multiples. We selected the median public companies value multiples. We have also adjusted these multiples to control the differences in size and company specific risks. The equity capitalization rate for the subject company has been kept larger by 8% ( 4% for size difference and 4% for Company specific risks) than the comparable rates for guidelines company. Accordingly, selected multiples have been adjusted. Weights were then assigned to Guideline companies multiples. Heavier weights were given to multiples having low coefficient of variation.

| | Market Value of Equity ( MVE) Multiples | | | | | Market Value of Invested Capital (MVIC) Multiples | | | |
|---|---|---|---|---|---|---|---|---|---|
| Company Name | MV Eq/ Book Eq. | MV Eq/ Pretax Earnings | MV Eq./ Net Income | MV Eq/ Gross Cash Flow | MV Eq /Sales | MVIC/ EBITDA | MVIC/ EBIT | MVIC/ Sales | MVIC/ Tangible Asset Value |
| | | | | | | | | | |
| Grauer & weil | 0.83 | 2.95 | 3.97 | 3.11 | 0.27 | 4.19 | 4.81 | 0.61 | 1.87 |
| Alkhli Metals | 0.50 | 1.90 | 2.15 | 1.75 | 0.28 | 3.39 | 3.96 | 0.69 | 1.28 |
| Ciba India | 0.09 | 0.81 | 1.30 | 0.98 | 0.06 | 1.23 | 1.48 | 0.11 | 0.17 |
| Gulshan | 2.14 | 7.53 | 9.50 | 6.51 | 0.72 | 5.80 | 7.17 | 1.06 | 3.25 |
| Jayant Agro | 0.91 | 7.07 | 11.96 | 8.43 | 0.10 | 8.32 | 9.26 | 0.30 | 2.64 |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Panama | 0.67 | 2.10 | 2.40 | 2.34 | 0.15 | 1.93 | 1.96 | 0.18 | 0.80 |
| Pidilite | 4.34 | 12.67 | 15.17 | 12.54 | 1.82 | 11.79 | 13.67 | 2.14 | 5.13 |
| Transpek | 0.65 | 13.57 | 25.36 | 4.46 | 0.25 | 5.62 | 10.01 | 0.60 | 1.54 |
| United Phosphorus | 1.43 | 32.68 | 33.49 | 17.84 | 1.66 | 15.88 | 21.46 | 2.65 | 2.29 |
| Mean | 1.29 | 9.03 | 11.70 | 6.44 | 0.59 | 6.46 | 8.20 | 0.93 | 2.11 |
| Median | 0.83 | 7.07 | 9.50 | 4.46 | 0.27 | 5.62 | 7.17 | 0.61 | 1.87 |
| Standard Deviation | 1.29 | 10.02 | 11.31 | 5.64 | 0.68 | 4.80 | 6.37 | 0.89 | 1.47 |
| Coff of Variation | 100.25 | 110.92 | 96.70 | 87.66 | 115.40 | 74.27 | 77.71 | 96.39 | 69.65 |

## Value Summary- Based on Median Multiples of aforesaid Guideline companies

| Equity Multiples | Selected Multiple (Median) | X | KECPL Funda- -mental | = | Indicated Value | - | Debt | = | Indicated Equity Value | X | Weight | = | Weighted Value |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| MVE/ net income | 9.50 | | 15.18 | | 144.21 | | 0 | | 144.21 | | 0.05 | | 7.21 |
| MVE/gross cash flow | 4.46 | | 22.18 | | 98.94 | | 0 | | 98.94 | | 0.10 | | 9.89 |
| MVE/earnings before taxes | 7.07 | | 23.00 | | 162.72 | | 0 | | 162.72 | | 0.05 | | 8.14 |
| MVE/net sales | 0.27 | | 190.00 | | 51.54 | | 0 | | 51.54 | | 0.05 | | 2.58 |
| MVE/book equity | 0.83 | | 50.17 | | 41.68 | | 0 | | 41.68 | | 0.05 | | 2.08 |
| **Invested Capital Multiples** | | | | | | | | | | | | | |
| MVIC/ EBITDA | 5.62 | | 34.35 | | 193.01 | | 68.36 | | 124.65 | | 0.20 | | 24.93 |
| MVIC/EBIT | 7.17 | | 27.35 | | 196.09 | | 68.36 | | 127.72 | | 0.20 | | 25.54 |
| MVIC/net sales | 0.61 | | 190.00 | | 116.17 | | 68.36 | | 47.81 | | 0.10 | | 4.78 |
| MVIC/net tangible asset value | 1.87 | | 50.17 | | 93.95 | | 68.36 | | 25.59 | | 0.20 | | 5.12 |
| | | | | | | | | | | | 1 | | 90.27 |

## Value Summary- Based on Adjusted Multiples of Closest Comparable Guideline company in terms of similarity of products, namely Grauer & Weil

| Equity Multiples | Multiple of Grauer & weil | Adjusted Multiple | X | KECPL Funda- -mental | = | Indicated Value | - | Debt | = | Indicated Equity Value | X | Weight | = | Weighted Value |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| MVE/ net income | 3.97 | 3.01 | | 15.18 | | 45.77 | | 0 | | 45.77 | | 0.05 | | 2.29 |
| MVE/gross cash flow | 3.11 | 2.49 | | 22.18 | | 55.19 | | 0 | | 55.19 | | 0.10 | | 5.52 |
| MVE/earnings before taxes | 2.95 | 3.86 | | 23.00 | | 88.67 | | 0 | | 88.67 | | 0.05 | | 4.43 |
| MVE/net sales | 0.27 | 0.21 | | 190.00 | | 0.00 | | 0 | | 0.00 | | 0.05 | | 0.00 |
| MVE/book equity | 0.83 | 0.63 | | 50.17 | | 31.63 | | 0 | | 31.63 | | 0.05 | | 1.58 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Invested Capital Multiples** | | | | | | | | |
| MVIC/ EBITDA | 4.19 | 3.64 | 34.35 | 125.20 | 68.36 | 56.84 | 0.20 | 11.37 |
| MVIC/EBIT | 4.81 | 4.11 | 27.35 | 112.45 | 68.36 | 44.09 | 0.20 | 8.82 |
| MVIC/net sales | 0.61 | 0.46 | 190.00 | 88.15 | 68.36 | 19.79 | 0.10 | 1.98 |
| MVIC/net tangible asset value | 1.87 | 1.42 | 50.17 | 71.29 | 68.36 | 2.93 | 0.20 | 0.59 |
| | | | | | | | 1 | 36.57 |

## Control Vs. Minority

The value obtained using this method often is considered non controlling liquid value (or Marketable Minority Value). This is however, a controversial area. Many analysts contend that when this method is applied to closely held companies, the resulting value does not only represent a minority position, since many public companies are run very efficiently and a control buyer would not pay any more for the business unless he could realize synergies; thus minority and control values are equal. As such, if the market multiple e.g. PE is applied to control cash flows of a private co., this may result in a control value.

Others argue that Valuation multiples are nothing more than inverted capitaization rates derived from public market. As such, thev underlying theory about minority/control being iin the cash flows for the income approach should also apply to market approach. If that is true, then the application of market multiples would be neutral and control/minority would, like the income approach, be an adjustment to the earnings' parameter to which the valuation mutilples are applied

## DLOC

Minority Discount or control premium should be considered on a case by case basis.

Minority interest- To what extent might the private company minority stockholders be disadvantaged compared with public company stockholders (e.g. money otherwise available for dividends siphoned off in excess compensation to control stockholders and friends)?
Controlling interest – What could a controlling interest stockholder do to make the control interest more valuable (e.g. improve management)?

As the cash flows of KECPL do not have any control adjustments, based on the reasoning given under Income Approach, a smaller discount (DLOC) of 5% (instead of 15% in Asset Approach) is applied, subjectively derived and based on judgment.

### DLOM

When valuing a private company, DLOM is usually appropriate for minority interests and in some cases even for controlling interests.

There is a continuing controversy about whether DLOM should be applied to controlling interests particularly 100%.This method assumes such marketability or liquidity which does not exist in controlling interest in a private company. Therefore, some level of discount (smaller than DLOM for minority interests) may be appropriate. Many analysts believe that DLOM for controlling interests generally range from 0 to 20%.

Based on the reasoning given under Income Approach, a discount of 25% (below average discount of 35%), subjectively derived and based on judgment, is considered appropriate.

### Value Indication

Total discounts works out to 29% and 100% Non Marketable Minority Value (NMV) Value indication, as per the aforesaid method based on Median multiples of Guideline companies is Rs. 64.32 Lacs. Based on a Closest comparable company (Grauer & Weil), it is Rs. 26.06 lacs.

## D. Statutory Valuations

### As per erstwhile CCI formula

Methodology has been described in detail in Part B- Valuation under various Legislations.

NAV is computed as follows:

| | | Amount As at 31.3.08 (Audited) ( Book Values) Rs/lacs |
|---|---|---|
| **A.** | **Immovables Fixed Assets** | |
| 1 | Factory Land & Building | 44.87 |
| 2 | Office premises | 1.08 |
| | Sub Total | 45.95 |
| **B.** | Other fixed Assets( at book value) | 13.90 |
| **C.** | Total Fixed Assets ( A+B) | 59.85 |
| **D.** | Current Assets, Loans & Advances | 97.61 |
| **E.** | Total Assets (C+D) | 157.46 |
| **F.** | Current Liabilities & Provisions | 38.93 |
| **G.** | Unsecured Borrowings | 68.36 |
| **H.** | Deferred Tax liability, Net<br>On Increase in Immovable Assets<br>Less : Deferred Tax Assets on Unabsorbed Losses/Depreciation etc.<br>Net Deferred Tax Liability | 0.00 |
| **I.** | **Net Assets (E-F-G-H)** | **50.17** |
| | **Represented By :** | |
| | Share Capital | 30.00 |
| | Share premium | 58.80 |
| | Less Debit Balance in Profit & Loss a/c | (38.63) |
| **J.** | **Net worth** | **50.17** |
| **K.** | No. of Equity Shares ( Rs. 10/- per share) | 300,000 |
| **L.** | **Value per Share ( Rs./ Share)** | **16.72** |

Profit Earning Capacity Value Method is computed in the manner given below:

| | | **Amount 2007-08 (Audited) Rs/lacs** | **Amount 2006-07 (Audited) Rs/lacs** | **Amount 2005-06 (Audited) Rs/lacs** |
|---|---|---|---|---|
| Revenue | | 190.00 | 139.33 | 118.60 |
| Less Costs | | 162.65 | 122.61 | 94.33 |
| Earnings before Interest & Taxes | | 27.35 | 16.72 | 24.27 |
| Less : Interest & Finance Charges | | 4.35 | 4.40 | 4.99 |
| **Earnings before Taxes** | | **23.00** | **12.32** | **19.28** |
| Weights Assigned | | 3 | 2 | 1 |
| Product | | 69.00 | 24.64 | 19.28 |
| **Weighted Average Earnings after Taxes** | **18.82** | | | |
| Less : Tax @ 33.99% | 6.40 | 7.82 | 4.19 | 6.55 |
| **Earnings after Taxes** | **12.42** | **15.18** | **8.13** | **12.73** |
| Capitalisation Rate | 15% | | | |
| Capitalised Future Maintainable Profits | 82.82 | | | |
| No. of Equity Shares ( Rs. 10/- per share) | 300,000 | | | |
| **Value per Share ( Rs./ Share)** | **27.61** | | | |

Fair Value as per erstwhile CCI formula is as follows :

| **Method of Valuation** | **Value of Share Rs./Share** |
|---|---|
| Net Assets Value Method | 16.72 |
| Profit Earning Capacity Value Method | 27.61 |
| Average | 22.17 |
| Less : Discounting by 15% to account for restricted mobility ( being unlisted share) | 3.32 |
| **Fair Value** | **18.84** |

Fair Value as per erstwhile CCI formula is however not applicable in case of transfer of shares from Non residents to residents. We, therefore, did not utilize this method in determining the NMV of share.

## As per FEMA Guidelines

Methodology has been described in detail in Part B- Valuation under various Legislations.

| | | |
|---|---|---|
| **A.** | **Value of Equity Share based on EPS linked to Price Earning Multiple** | |
| | Earning per share (EPS)<br>( as per latest audited financial statements for the year ended 31.3.2008) | 1.98 |
| | Average P/E Multiple of BSE National ( BSE 100) Index for November, 08 | 13.41 |
| | Discounted P/E Multiple at 40% | 8.05 |
| | **PEC Price per Share ( Rs./ Share)-** | **15.93** |

| | | |
|---|---|---|
| **B.** | **Value of Equity Share based on NAV linked to Book Value Multiple** | |
| | Net Asset Value (NAV)<br>( as per latest audited financial statements<br>for the year ended 31.3.2008) | 16.72 |
| | Average Price to Book Value Multiple ( P/B) Multiple- for Nov,08 | 2.31 |
| | Discounted P/B Multiple at 40% | 1.39 |
| | **Price per Share baesd on P/B Multiple ( Rs./ Share)** | **23.18** |
| **C.** | **Higher of A & B** | **23.18** |

Value as per FEMA guidelines as applicable to transfer of shares from Non residents to Residents is Rs. 23.18 per equity share. It may be noted that DLOM is 40% and DLOC is not considered in this methodology.

## 5. Sources of Information

The analysis is based on a review of the business plan of the company provided by the Management and information relating to the specialty chemical manufacturing sector as a available in the public domain. Specifically, the sources of information include:

- Discussions with the Potential buyer
- Site Visits and Interviews
- Discussions with the Company's Management
- Company brochure and website
- Financial projections of the Company for 4 years ending 2012.as provided by the potential buyer and Company's Management.
- Audited financial statements for 2006, 2007 and 2008.
- Risk free return based on Yield of 10 years 8.24% 2018 Government bonds
- Expected return of well diversified market portfolio as cumulative average market return of the BSE 500 index since inception from the Stock Exchange, Mumbai website (www.bseindia.com)

  In addition to the above, we have also obtained such other information and explanations which were considered relevant for the purpose of the analysis.

## 6. Caveats

Provision of valuation recommendations and considerations of the issues described herein are areas of our regular corporate advisory practice. The service do not represent accounting, assurance, financial due diligence review, consulting, transfer pricing or domestic/international tax-related services that may otherwise be provided by us.

Our review of the affairs of the Company and their books and account does not constitute an audit in accordance with Auditing Standards. We have relied on explanations and information provided by the Management of the Company and accepted the information provided by the Management of the Company and accepted the information provided to us as accurate and complete in all respects. Although, we have reviewed such data for consistency and reasonableness, we have not independently investigated or otherwise verified the data provided. Nothing has come to our attention to indicate that the information provided had material misstatements or would not afford reasonable grounds upon which to base the Report.

The report is based on the financial projections provided to us by the management of the company and the potential buyer and thus the responsibility for forecasts and the assumptions on which they are based is solely that of the Management of the Company and the potential buyer and we do not provide any confirmation or assurance on the achievability of these projections. It must be emphasized that profit forecasts necessarily depend upon subjective judgement. Similarly we have relied on data from external sources. These sources are considered to be reliable and therefore, we assume no liability for the accuracy of the data. We have assumed that the business continues normally without any disruptions due to statutory or other external/internal occurrences.

The valuation worksheets prepared for the exercise are proprietary to the Valuers and cannot be shared. Any clarifications on the workings will be provided on request, prior to finalizing the Report, as per the terms of our engagement.

The scope of our work has been limited both in terms of the areas of the business and operations which we have reviewed and the extent to which we have reviewed them.

The valuation analysis contained herein is represents the value only on date that is specifically stated in this Report. This Report is issued on the understanding that the Management of the Company has drawn our attention to all matters of which they are aware, which may have an impact on our Report up to date of signature. We have no responsibility to update this Report for events and circumstances occurring after the date of this Report.

Our valuation analysis should not be construed as investment advice; specifically, we do not express any opinion on the suitability or otherwise of entering into any transaction with the Company.

## 7. Distribution of Report

The report is confidential and has been prepared exclusively for the Client namely, Mr. X. It should not be used or relied upon by, reproduced or circulated to any other person or for any purpose other than as mentioned above, in whole or in part, without the prior written consent of the Valuers. Such consent will only be given after full consideration of the circumstances at the time. We will not accept any responsibility or liability to third parties to whom our report may be shown or into whose hands it may come without our prior written consent.

Neither all nor any part of the contents of this report shall be disseminated to the public through advertising, public relations, news, sales or other media without our prior written consent.

## 8. Correlation and Reconciliation of Valuation Methods and Values

The process of correlation and reconciliation is the analysis of alternative indications of value to arrive at a final value indication. Relative strengths and weaknesses of each method relative to appraisal objective, conceptual conformance to definition of value sought and adequacy (quantity and quality) of data, is assessed.

The following methods are used to correlate and reconcile values:
(a) Straight average of the indications of value,
(b) Numerical weights assigned to each of the value indications,
(c) Qualitative judgment in selection of value.

### Summary of Value Indications

| S.No. | Method of Valuation | Value derived methods (Rs./Lacs) | Less DLOC | Less DLOM | Total Discount | 100 % Non Marketable Minority V. (Rs./Lacs) | Value Per share Rs. |
|---|---|---|---|---|---|---|---|
| 1 | Adjusted Net Assets Method | 81.03 | 15% | 25% | 36% | 51.65 | 17.22 |
| 2 | DCF Method - APV Approach | 73.09 | 5% | 25% | 29% | 52.08 | 17.36 |
| 3 | Guideline Public Company M | | | | | | |
| | -Relative to Selected Comps. | 90.27 | 5% | 25% | 29% | 64.32 | 21.44 |
| | -Relative to Grauer & Weil | 36.57 | 5% | 25% | 29% | 26.06 | 8.69 |
| 4 | CCI | 66.50 | 0% | 15% | 15% | 56.52 | 18.84 |
| 5 | FEMA Guidelines | 115.89 | 0% | 40% | 40% | 69.54 | 23.18 |

### Value Indication by Adjusted Net Asset Method ( Asset Approach)

According to conceptual conformance to definition of value, if valuing a minority interest, the methods that reach minority value directly without having to start with control value and estimate minority discount, should be preferred.

This method was not chosen as the best indication of value as it generally produce a control value since minority interest holders have no direct claim on the asset and can not force their disposition or utilization.

For this reason, though this method has been considered for valuation analysis but we did not utilize the Asset Approach in determining the NMV of share of KECPL. This method, however, provided some corroboration for our conclusion of value determined under other method.

## Value Indication by DCF Method (APV Approach) (Income Approach)

We have a high level of confidence in the KECPL projections and believe that this method provides the best, the most reliable and the most relevant indication of value based on our qualitative judgment.

The Guideline Public Company Method and the Adjusted Net Asset Method support this value.

## Value Indication by Guideline Public Company Method (Market Approach)

This method was also not chosen as the best indication of value and therefore, though considered but not utilized in determining the Non Marketable Minority Value (NMV) of share of KECPL for the following reasons :

a. Lack of adequately similar or sufficiently comparable guideline public companies with the subject company.
b. Many public companies are not " pure plays" in the "Chemical–Specialty" industry of interest.
c. Most public companies are much larger than the subject company.
d. Many public companies have higher potential growth ( Expected growth rate is an implicit assumption in the guideline price multiple) than the subject company, which may require a difficult adjustment in comparison.
e. The closest comparable company ( Grauer & weil), considered in the Valuation analysis, is in fact, a diversified company.
f. There is significant difference in valuation as per Median Multiples of guideline companies considered vis-à-vis valuation as per adjusted multiple of the closest comparable company ( Grauer & weil.

This method was, however used as a reasonableness test/sanity check for the Income approach. The Market approach (frequently referred to as "Comps" or "Multiples") is also more useful as an overall vital "sanity check" (a check to verify that no obvious mistakes have been made) to see if a given value is "in the ballpark". As observed from Table of value Indications, this method supports the value determined under the Income Approach.

## Value Indication by CCI Method

In relation to NAV, in the absence of revaluation of fixed assets, the balance sheet values of assets are far divorced from the current market price.

In relation to PEC Value, Finance theory asserts that companies with substantial leverage (high debt/equity ratio) should be capitalized at higher rates reflecting higher degree of risk. The CCI's formula docs not explicitly consider leverage at all in determining the capitalization rate. Capitalization rates are pre fixed and not market driven. Further, the operative part of the guidelines largely confines itself to the average of the last three to five years profits as per audited accounts to be the future maintainable profits. There is an implied assumption that the recent past will replicate itself into perpetuity. Earnings are capitalized in this method and not the net cash flow.

In relation to discounts, DLOM is only a small 15% fixed in the CCI formula as against average 35% in case of valuation of share of a closely held company. There is no scope of DLOC.

Last but not the least, this method is not statutorily applicable in case of transfer of shares from non resident to resident.
For the aforesaid reasons, though this method has been considered for valuation analysis but we did not apply in determining the Non Marketable Minority Value (NMV) of share of KECPL and hence discarded the same.

## Value Indication by Method prescribed in FEMA Guidelines

This method has been prescribed as an optional method. This method is based on Market approach (relative valuation). Historical EPS and Book Value as per latest balance sheet are respectively multiplied by average PE and BV multiple of BSE 100 Index respectively. A fixed discount of 40% is to be then applied. Higher of the two valuation is chosen. There is no scope of DLOC. Multiples of comparable companies are not taken, instead only of BSE 100 index. Normalization of financial statements are not done.

Multiples are not adjusted relative to risk, growth or size of the subject company.

For the aforesaid reasons, though this method has been considered for valuation analysis but we did not utilize in determining the Non Marketable Minority Value (NMV) of share of KECPL and hence discarded the same.

## 9. Value Conclusion

Based on our analysis and on the information contained in this report, we have concluded that the fair market value of 49% of the common stock of KECPL, a closely held company, on a Non Marketable Minority ownership Interest basis, on a going concern premise, as of 31st December,2008 for the purpose of possible acquisition of minority stock, based on 3,00,000 equity shares issued and outstanding, is approximately Rs.17.36 per share ( Rs.52.08 Lacs/ 300,000).

| | |
|---|---|
| Per Share Value | Rs. 17.36 |
| Value 147,000 shares | Rs. 25,51,726.00 |

This valuation is subject to the certifications presented in Appendix A and to the assumptions and limiting conditions presented in Appendix B.

We trust the above meets your requirements. Please feel free to contact us in case you require any additional information or clarifications.

Yours faithfully

**Manoj Kumar Aggarwal**
(Membership No. 84769; Mobile +91-9810046153),
Tarun Sharma,
Love Mangla
Jitesh Bhugra and
Megha Almadi
(Chartered Accountants)
**(VALUERS)**

## Appendix A: Valuation Certification and Signature

We certify that, to the best of our knowledge and belief:

- the statements of fact contained in this report are true and correct.
- the reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are our personal, impartial, unbiased professional analyses, opinions, and conclusions.
- The data and information included in this valuation report have been obtained from various sources that we believe to be reliable. However, we have not performed any procedures to corroborate this data or to test the accuracy.
- We have no present or prospective interest in the property that is the subject of this report, and we have no personal interest or bias with respect to the parties involved.
- We have no bias with respect to the property that is the subject of this report or to the parties involved with this assignment.
- Our compensation is not contingent on an action or event resulting from the analyses, opinions, or conclusions in, or the use of, this report.
- No one provided significant professional assistance to the person signing this report, except as may be noted below or elsewhere in this report.

Yours faithfully

**Manoj Kumar Aggarwal**
(Membership No. 84769; Mobile +91-9810046153),
Tarun Sharma,
Love Mangla
Jitesh Bhugra and
Megha Almadi
(Chartered Accountants)
**(VALUERS)**

## Appendix B: Conditions And Major Assumptions

### Conditions

The historical financial information about the company presented in this report is included solely for the purpose to arrive at value conclusion presented in this report, and it should not be used by anyone to obtain credit or for any other unintended purpose. Because of the limited purpose as mentioned in the report, it may be incomplete and may contain departures from generally accepted accounting principles prevailing in the country. We have not audited, reviewed, or compiled the Financial Statements and express no assurance on them. The financial information about the company presented in this report includes normalization adjustments made solely for the purpose to arrive at value conclusions presented in this report. Normalization adjustments as reported are hypothetical in nature and are not intended to present restated historical financial results or forecasts of the future.

Readers of this report should be aware that a business valuation is based on future earnings potential that may not be materialized. Any financial projections e.g. Projected balance sheet, Projected profit and loss account, Projected Cash flow statement as presented in this report are included solely to assist in the development of the value conclusion. The actual results may vary from the projections given, and the variations may be material, which may change the overall value.

This report is only to be used in its entirety, and for the purpose stated in this report. No third parties should rely on the information or data contained in this report without the advice of their lawyer, attorney or accountant.

We acknowledge that we have no present or contemplated financial interest in the Company. Our fees for this valuation are based upon our normal billing rates, and not contingent upon the results or the value of the business or in any other manner. We have no responsibility to modify this report for events and circumstances occurring subsequent to the date of this report.

We do not purport to be a guarantor of value. Valuation of shares of companies is an imprecise science, with value being an estimate only and reasonable people can differ in their estimates of value. We have, however, used conceptually sound and generally accepted methods, principles and procedures of valuation in determining the value estimate included in this report.

The valuation analyst, by reason of performing this valuation and preparing this report, is not to be required to give expert testimony nor to be in attendance in court or at any government hearing with reference to the matters contained herein, unless prior arrangements have been made with the analyst regarding such additional engagement.

The analysis, opinions and conclusions presented in the report apply to this engagement only and may not be used out of context presented herein. The report is valid only for the effective date specified herein and only or the purpose specified herein.

## Assumptions

The opinion of value given in this report is based on information provided in part by the management of the Company, the potential buyer (Mr. X) and other sources as listed in the report. This information is assumed to be accurate and complete; we have not audited or attempted to confirm this information for accuracy or completeness.

We have relied upon the representations contained in the public and other documents in our possession concerning the value and useful condition of all investments in securities or partnership interests, and any other assets or liabilities except as specifically stated to the contrary in this report.

We have not attempted to confirm whether or not all assets of the business are free and clear of liens and encumbrances, or that the owner has good title to all the assets.

We have also assumed that the business will be operated prudently and that there are no unforeseen adverse changes in the economic conditions affecting the business, the market, or the industry. This report presumes that the management of the Company will maintain the character and integrity of the Company through any sale, reorganization or reduction of any owner's / manager's participation in the existing activities of the Company.

We assume no hidden or unapparent conditions regarding the subject assets, properties or business interests.

We assume there is full compliance with all applicable central, state or local regulations and laws unless the lack of compliance is stated, defined, and considered in the valuation report.

We have been informed by management that there are no environmental or toxic contamination problems, any significant lawsuit or any other undisclosed contingent liabilities which may potentially affect the business, except as may be disclosed elsewhere in this report. We have assumed that no costs or expenses will be incurred in connection with such liabilities, except as explicitly stated in this report.

# Part B : Valuation under Various Legislations

## Contents

# 1. Valuation of Equity Shares According to Guidelines Issued by the Erstwhile Controller of Capital Issues

## A. Applicability

The aforesaid guidelines are made applicable under FEMA for pricing of shares in case of an unlisted companies for the purpose of –

(a) Issue of Shares to Non Residents under FDI Scheme, and

(b) Transfer of Shares from a resident in India to a non resident.

## B. Methodology In Brief

### Compute Net Asset Value

The NAV is nothing but the traditional book value per share computed on the basis of the latest audited annual accounts.

**(a)** Calculation of Net Worth as per the latest audited accounts
- Subtract any contingent liabilities likely to impair the net worth
- Revaluation of Fixed assets – normally not to be considered in Reserves
- Intangible assets and Miscellaneous Expenditure not written off- not considered in Assets.

**(b)** Add the face value of the fresh issue of capital proposed (including new bonus issue, if any) to the net worth as at the latest balance sheet date and then divide the resulting net worth by the enlarged capital base including the fresh issue as well as new bonus issue.

### Compute Profit Earning Capacity Value ( PECV)

The Profit Earning Capacity Value" (PECV) will be calculated by capitalizing the average of the after tax profits at the following rates:

(i) 15% in the case of manufacturing companies,

(ii) 20% in the case of trading companies, and

(iii) 17.5% in the case of 'intermediate' companies that is to say, companies whose turnover from trading activities is more than 40%, but less than 60% of their total turnover.

## (a) Computation of Average Profits

Ordinarily the averaging of profits is done for the last three to five years profits as per audited accounts. Average may be done on a weighed basis. According to it, greater weightage is given for the most recent year's performance when past profits show a steadily increasing or decreasing trend.

## (b) Taxation

In computing the average profits, provision for taxation, with some exceptions, is to be "assumed at the current statutory rate under the income tax".

## (c) Profitability of Fresh Issues

Where the fresh issue of capital is for the purpose of financing expansion or new projects, it is assumed that the fresh capital would contribute to the profits upto a maximum of 50% of the existing rate of profitability. This will be added to the existing profits after tax and the total will be divided by the *enlarged* capital base to arrive at the future maintainable earnings per share.

$$\frac{1}{2} \times \frac{\text{Fresh Capital} \quad \text{X Existing Profits after tax}}{\text{Existing Net worth}}$$

Where the fresh capital is sought to be raised for general reasons like modernization and replacement of assets , *it is not advised to assume that the fresh capital will contribute to the profitability of the business in any tangible manner in the near future.* In such cases, while the fresh issue of capital will be taken into account, no additional profits are to be assumed

## Fair Value

It is Average of NAV ad PECV as discounted by at least 15% to take care of the restricted mobility of share of an unlisted company.

## C. Case Study

### Facts

A private company G India Pvt. Ltd., New Delhi is a joint venture company having 85% stake of non residents. It has been incurring losses. To fund the operations, it has allotted further 200,000 equity shares of Rs. 10 each keeping the ratio of foreign and Indian shareholders as intact.

The Company has approached us for carrying out a valuation of Equity Share of the Company for the purpose of compliance with regulations of the Reserve Bank of India for issue of shares to non residents.

### Methodology adopted

According to FEMA guidelines, for Issue of shares and convertible debentures to persons resident outside India under the FDI Scheme, Valuation of shares is to be done by a Chartered Accountant in accordance with the guidelines issued by the erstwhile Controller of Capital Issues.

### G India Private Limited

**Table 1: Computation of Value of An Equity Share as per Net Assets Valuation Method**

| | | | Amount As at 31.3.07 (Audited) Rs/lacs |
|---|---|---|---|
| **A.** | **Fixed Assets** | | |
| | Gross Block | 2,177.46 | |
| | Less : Accumulated Depreciation | 571.65 | |
| | Net Block | 1,605.81 | |
| | Capital Advances | 15.50 | 1,621.31 |

| | | | |
|---|---|---|---|
| | **Current Assets, Loans & Advances** | | |
| **B.** | Inventories | | 0.25 |
| **C.** | Sundry Debtors | | 205.13 |
| **D.** | Cash & Bank Balances | | 63.56 |
| **E.** | Loans & Advances | | 29.80 |
| **F.** | Total Assets (A to E) | | 1,920.05 |
| **G.** | Preference Share Capital | | - |
| **H.** | Secured Loans | | - |
| **I.** | Unsecured Loans | | 813.61 |
| **J.** | Current Liabilities & Provisions | | 182.92 |
| **K.** | Deferred Tax Liability | | 17.29 |
| **L.** | Share Application Money | | 175.68 |
| **M.** | Contingent Liabilities | | - |
| **N.** | **Net Assets {F-(G+H+I+J+K+L+M)}** | | **730.55** |
| | **Represented By :** | | |
| | Equity Share Capital | 184,624,000.00 | 1,846.24 |
| | Free Reserves | | - |
| | Less :Debit Balance in Profit & Loss a/c ( Being Losses) | 111,569,280.00 | 1,115.69 |
| | Less : Miscellaneous Expenditure not written off | | - |
| **O.** | **Net Worth** | | **730.55** |
| **P.** | Add : Fresh Capital issue ( face Value) | | 200.00 |

| | | | |
|---|---|---|---|
| **Q.** | **Total** | | **930.55** |
| **R.** | **No. of Equity Shares including Fresh Issue** | | |
| | **( Face value Rs. 100/- per share)** | | |
| | Exising Equity shares as on 31.3.2007 | 1,846,240 | |
| | Fresh Issue of Equity shares on 31.3.2008 | 200,000 | |
| | | | 2,046,240 |
| **S.** | **Net asset Value per Share ( Rs./ Share)** | | **45.48** |

**Table 2: Computation of Value of An Equity Share as per Profit Earning Capacity Value Method**

| | | **Amount Year ended 2006-07 (Audited) Rs/lacs** | **Amount Year ended 2005-06 (Audited) Rs/lacs** | **Amount Year ended 2004-05 (Audited) Rs/lacs** |
|---|---|---|---|---|
| **Revenue** | | | | |
| Sales | | 1,382.29 | 1,135.65 | 1056.07 |
| Other income | | 7.30 | 6.68 | 19.93 |
| Increase\(Decrease) in Stock | | 0.22 | (0.29) | (2.24) |
| | Total | 1,389.81 | 1,142.04 | 1,073.76 |
| **Less Costs** | | | | |
| Cost of Sales | | 17.94 | 126.35 | 96.12 |
| Personnel Costs | | 896.58 | 813.64 | 679.22 |
| Administrative Costs | | 358.56 | 363.46 | 423.08 |
| Interest & Financial Charges | | 9.05 | 2.37 | 2.13 |
| | Total | 1,282.13 | 1,305.82 | 1,200.55 |
| Earnings/( Losses) before Depreciation, Write offs & Taxes | | **107.68** | **(163.78)** | **(126.79)** |
| Less : Depreciation | | 156.47 | 143.60 | 150.84 |
| Less : Preliminary Expenditure written off | | 0.00 | 0.13 | 0.13 |

| | | | | |
|---|---|---|---|---|
| **Losses before Taxes** | | **(48.79)** | **(307.51)** | **(277.76)** |
| **Average Profit/(Loss) before tax - Simple Average** | | **(211.35)** | | |
| Less : Provision for Fringe Benefit Tax & Deferred tax | | 5.64 | | |
| **Profits/( Losses) after Taxes** | | **(216.99)** | | |
| Add : Contribution to profit by fresh issue, if any | | 0.00 | | |
| **Total Profits/( Losses) after Taxes** | | **(216.99)** | | |
| **Average Profit/(Loss) before tax** | | | | |
| No. of Equity Shares including Fresh Shares ( Rs. 10/- per share) | | 2,046,240 | | |
| Earnings/(Loss) per share (EPS) | Negative Value | **(10.60)** | | |
| **Profit Earning Capacity Value @ 17.5 % Capitalisation Rate( As the Company has suffered losses in all the three years, PEC Value will have to be regarded as Nil in this case)** | | **Nil** | | |

## Underlying Facts And Assumptions:

The rate of 17.5% has been taken for capitalising the profits of the Company to arrive at the value of shares of the Company. This rate of capitalisation is the rate generally employed to value the business of a intermediate company as prescribed by the erstwhile Controller of Capital issues (CCI). Since the Company is engaged in Software Development, this rate has been considered appropriate. CCI had prescribed a rate of15% & 20 % for manufacturing companies and trading companies respectively.

| Table 3 : Computation of the Fair Value of An Equity Share | | |
|---|---|---|
| | **Method of Valuation** | **Value of Share Rs.** |
| 1 | Net Assets Value Method | 45.48 |
| 2 | Profit Earning Capacity Value Method | Nil |
| | Average | 22.74 |
| | Less : Discounting by 15% to account for restricted mobility ( being unlisted share) | 3.41 |
| | **Fair Value** | **19.33** |

## Conclusion

*The fair value of the shares of the Company is computed by taking simple average of the share values derived by the NAV and PECV methods. As the Company has suffered losses in all the three years, PEC value will have to be regarded as Nil in this case. According to the CCI guidelines, where PEC value is Nil or negligible, the fair value should be limited to half of the Net Assets Value.*

*The value arrived at as aforesaid has been further discounted by 15% to take account of the restricted mobility the share (being share of an unlisted company). On the basis of the computation of the share value of the Company, the fair value of an equity share works out at **Rs. 19.33** (Refer Table 3).*

## 2. Valuation of Equity Shares According to FEMA Guidelines

### A. Applicable Methodologies

| S. No. | | Listed Companies | Unlisted Companies |
|---|---|---|---|
| A.1 | Issue/ Allotment of Shares to Non residents ( FDI) | SEBI Guidelines | Not less than Erstwhile CCI Formula |
| | | | |
| A.2 | Transfer of Shares | | |
| | -From Residents to Non Residents | Not less than Ruling Market price | Not less than Erstwhile CCI Formula |
| | -From Non Residents to Residents | at the prevailing market price on stock exchange, if effected through stock broker/merchant banker | If consideration per seller exceeds Rs. 20 lacs, at a price arrived at, at the seller's option as follows :<br>1. Higher of a price based on EPS linked to P/E multiple and on NAV linked to book value multiple, OR<br>2. the prevailing market price in small lots, OR<br>3. at a price which is lower of the two independent valuations of share |
| | | if not effected through stock broker/merchant banker, at average quotations (average of daily high and low) for one week preceding the date of application with 5 percent variation. Price may be higher up to 25% for passing the management control to residents | If consideration per seller does not exceed Rs. 20 lacs, at a price mutually agreed to between the seller and the buyer, based on any valuation methodology currently in vogue |

Pricing Guidelines , according to RBI Circular No. 16 of October 4, 2004 for transfer of shares, by way of sale under private arrangement are as follows :

### Transfer By Resident To Non-Resident (i.e. To Incorporated Non-Resident Entity Other Than Erstwhile OCB, Foreign National, NRI, FII)

Price of shares transferred by way of sale by resident to a non-resident shall not be less than

(a) the ruling market price, in case the shares are listed on stock exchange,

(b) fair valuation of shares done by a Chartered Accountant as per the guidelines issued by the erstwhile Controller of Capital Issues, in case of unlisted shares.

The price per share arrived at should be certified by a Chartered Accountant.

### Transfer By Non-Resident (i.e. By Incorporated Non-Resident Entity, Erstwhile OCB, Foreign National, NRI,FII ) To Resident :

Sale of shares by a non-resident to resident shall be in accordance with Regulation 10 B (2) of Notification No. FEMA 20/2000-RB dated May 3, 2000 which as below:

**(a)** Where the shares of an Indian company are traded on stock exchange,

i) The sale is at the prevailing market price on stock exchange and is effected through a merchant banker registered with Securities and Exchange Board of India or through a stock broker registered with the stock exchange;

ii) if the transfer is other than that referred to in clause (i), the price shall be arrived at by taking the average quotations (average of daily high and low) for one week preceding the date of application with 5 percent variation. Where, however, the shares are being sold by the foreign collaborator or the foreign promoter of the Indian company to the existing promoters in India with the objective of passing management control in favour of the resident promoters the proposal for sale will be considered at a price which may be higher by upto a ceiling of 25 percent over the price arrived at as above,

**(b)** Where the shares of an Indian company are not listed on stock exchange or are thinly traded,

i) if the consideration payable for the transfer does not exceed Rs.20 lakh per seller per company, at a price mutually agreed to between the seller and the buyer, based on any valuation methodology currently in vogue, on submission of a certificate from the statutory auditors of the Indian company whose shares are proposed to be transferred, regarding the valuation of the shares, and

ii) if the amount of consideration payable for the transfer exceeds Rs.20 lakh per seller per company, at a price arrived at, at the seller's option, in any of the following manner, namely:

- a price based on earning per share (EPS linked to the Price Earning (P/E) multiple ,or a price based on the Net Asset Value (NAV) linked to book value multiple, whichever is higher,

  or

- the prevailing market price in small lots as may be laid down by the Reserve Bank so that the entire shareholding is sold in not less than five trading days through screen based trading system

  or

- where the shares are not listed on any stock exchange, at a price which is lower of the two independent valuations of share, one by statutory auditors of the company and the other by a Chartered Accountant or by a Merchant Banker in Category 1 registered with Securities and Exchange Board of India.

*Explanation:*

i) A share is considered as thinly traded if the annualized trading turnover in that share, on main stock exchanges in India, during the six calendar months preceding the month in which application is made, is less than 2 percent (by number of shares) of the listed stock.

ii) For the purpose of arriving at Net Asset Value per share, the miscellaneous expenses carried forward, accumulated losses, total outside liabilities, revaluation reserves and capital reserves (except subsidy received in cash) shall be reduced from value of the total assets and the net figure so arrived at shall be divided by the number of equity shares issued and paid up. Alternatively, intangible assets shall be reduced form the equity capital and reserves (excluding revaluation reserves) and the figure so arrived at shall be divided by the number of equity shares issued and paid up. The NAV so calculated shall be used in conjunction with the average BV multiple of Bombay Stock Exchange National Index ( BSE 100 Index) during the calendar month immediately preceding the month in which application is made and BV multiple shall be discounted by 40 percent.

iii) For computing the price based on Earning Per Share, the earning per share as per the latest balance sheet of the company shall be used in conjunction with the average Price Earning Multiple of Bombay Stock Exchange National Index for the calendar month preceding the month in which application is made and Price Earning shall be discounted by 40 per cent.

## B. Case Study

M/s K Electro-Chemicals Private Limited, New Delhi, India is a joint venture between M/s S GmbH, Germany and Indian promoters holding 49% and 51% respectively, of the total paid up equity share capital of the JV Company. The business of the Company is manufacturing, development and marketing of electroplating and special /other chemicals for cleaning, pretreatment, finishing and post-treatment and other related applications.

The Company has been incurring losses since the joint venture was done for many years as the technology for manufacture of pre treatment chemicals offered by the foreign collaborator did not succeed in Indian market, resulting into low turnover and low profits.

M/s S GmbH has offered to sell its entire 49% equity share holding in the Company comprising of 147,000 equity shares to the Indian promoters.

The Company has approached us for carrying out a valuation of Equity Share of the Company in connection with the aforesaid proposal of disinvestment of equity shares by foreign investors.

| | | |
|---|---|---|
| **A.** | **Value of Equity Share based on EPS linked to Price Earning Multiple** | |
| | | Rs. |
| | Earning per share (EPS)<br>( as per latest audited financial statements<br>for the year ended 31.3.2008) | 1.98 |
| | Average P/E Multiple of BSE National ( BSE 100) Index for November, 08 | 13.41 |

| | | |
|---|---|---|
| | Discounted P/E Multiple at 40% | 8.05 |
| | **PEC Price per Share ( Rs./ Share)-** | **15.93** |
| **B.** | **Value of Equity Share based on NAV linked to Book Value Multiple** | |
| | Net Asset Value (NAV)<br>( as per latest audited financial statements<br>for the year ended 31.3.2008) | 20.88 |
| | Average Price to Book Value Multiple ( P/B) Multiple- for Nov,08 | 2.31 |
| | Discounted P/B Multiple at 40% | 1.39 |
| | **Price per Share baesd on P/B Multiple ( Rs./ Share)** | **28.94** |
| **C.** | **Higher of A & B**<br>**Rs.** | **28.94** |

## 3. Valuation Of Equity Shares According to SEBI Guidelines - SEBI (Substantial Acquisition of Shares And Takeover) Regulations, 1997.

### A. Regulatory Provisions

#### When the Shares of Target Company are Frequently Traded-

The offer price shall be highest of -

| | | |
|---|---|---|
| **A.** | Regulation 20(4)(a) | Negotiated price under any share purchase agreement |
| **B.** | Regulation 20(4)(b) | Price paid by the acquirer or persons acting in concert with him for acquisition, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement, whichever is higher. |
| **C.** | Regulation 20(4)(c) | the average of the weekly high and low of the closing prices of the shares of the target company as quoted on the stock exchange where the shares of the company are most frequently traded during the twenty-six weeks<br>OR<br>the average of the daily high and low of the prices of the shares as quoted on the stock exchange where the shares of the company are most frequently traded during the two weeks preceding the date of public announcement, whichever is higher. |

Where the public announcement of offer is pursuant to acquisition by way of firm allotment in a public issue or preferential allotment, the average price under clause (c) of sub-regulation (4) shall be calculated with reference to twenty-six week period preceding the date of the board resolution which authorised the firm allotment or preferential allotment.

## Where the Shares of the Target Company are Infrequently Traded-

The shares shall be deemed to be infrequently traded if on the stock exchange, the annualised trading turnover in that share during the preceding six calendar months prior to the month in which the public announcement is made is less than five per cent (by number of shares) of the listed shares.

The offer price shall be determined by the acquirer and the merchant banker taking into account the following factors:

| | | |
|---|---|---|
| A. | Regulation 20(5)(a) | Negotiated price under any share purchase agreement |
| B. | Regulation 20(5)(b) | the highest price paid by the acquirer or persons acting in concert with him for acquisitions, if any, including by way of allotment in a public or rights or preferential issue during the twenty-six week period prior to the date of public announcement |
| C. | Regulation 20(5)(c) | Other parameters including return on networth, book value of the shares of the target company, earning per share, price earning multiple vis-a-vis the industry average |

## Provision in respect of Non Compete

Sub Regulation(8) : Any payment made to the persons other than the target company in respect of non- compete agreement in excess of twenty-five per cent of the offer price arrived at under sub-regulation (4) or (5) or (6) shall be added to the offer price.

Regulation 12 : The offer price for indirect acquisition or control shall be determined with reference to the date of the public announcement for the parent company and the date of the public announcement for acquisition of shares of the target company, whichever is higher, in accordance with sub-regulation (4) or sub-regulation (5).

## B. Case Study

### Background of the Offer

BEIL of UK has entered into a Share Purchase Agreement [Offshore SPA 1] on February 14, 2005 with Unocal International Corporation, USA [hereinafter referred to as the "Indirect Seller"], a 100% subsidiary of Union Oil Company of California, to acquire the entire equity share capital of UBL, UK which owns and holds 1,52,81,633 equity shares of Rs. 10/- each representing 26.01% in the paid up equity share capital of Hindustan Oil Exploration Company Ltd, the target company (HOEC) for cash at a negotiated acquisition price of US$ 26,010,000 [Rs. 13,71,57,200] [Exchange Rate: 1 US$ = Rs. 43.72 on February 14, 2005. Source: rbi.org.in]. The acquisition is an unconditional and absolute transfer of shares by a foreign shareholder to a foreign shareholder outside India at the holding company level and these shares are already registered in the name of BEIL in the records of UBL.

BEIL, pursuant to the provisions of Regulation 10 and 12, made an Open Offer to acquire 1,17,48,990 Equity Shares representing 20.00% of the paid up equity share capital of HOEC at a price of Rs. 92.41 per fully paid up equity share ("Offer Price").

Equity shares of HOEC were listed on BSE and NSE where they were frequently traded and at DSE, CSE and MSE where they were infrequently traded.

### Justification of Offer Price :

| **Parameters as per Regulation 20(4)** | Price per share – At NSE | Price per share – At BSE |
|---|---|---|
| The negotiated price paid by the acquirer to Unocal International Corporation for the indirect acquisition of shares held by UBL in HOEC as per Offshore SPA 1 dated February 14, 2005. | Rs. 74.41* | Rs. 74.41* |
| The price paid by the Acquirer Company and PAC for acquisitions, if any, including by way of allotment in a public or rights or preferential issue, during the 26 week period prior to the date of Public Announcement | Not Applicable | Not Applicable |
| Average of the weekly high and low of the | Rs. 83.27 | Rs. 83.21 |

| | | |
|---|---|---|
| closing prices of HOEC during the 26 weeks preceding the date of PA | | |
| Average of the daily high and low prices of HOEC during the 2 weeks preceding the date of PA | Rs. 92.41 | Rs. 92.05 |

* US $ 1.70 per share of HOEC (Exchange Rate: 1 US $ = Rs.43.72 on February 14, 2005)

| **Parameters as per Regulation 20(5)** | Price per Equity Share of Rs.10/- each of HOEC |
|---|---|
| The negotiated price paid by the acquirer to Unocal International Corporation for the indirect acquisition of shares held by UBL in HOEC as per Offshore SPA 1 dated February 14, 2005. | Rs. 74.41* |
| The price paid by the Acquirer Company and PAC for acquisitions, if any, including by way of allotment in a public or rights or preferential issue, during the 26 week period prior to the date of Public Announcement | Not Applicable |
| Other parameters based on the audited financial results for the year ended on March 31, 2004 | 1. Book Value per share Rs. 29.94<br>2. Return on Networth 12.58%<br>3. Earning Per Share Rs. 3.77<br>4. Offer P/E [Price Earning Ratio] Rs. 24.51<br>5. P/E multiple for the Industry category, i.e., “Oil Drilling / Allied Services” is 11.8 [Source: “Capital Market” dated January 31, 2005 to February 13, 2005]<br>6. Fair Value of the share keeping in view Supreme Court decision in HLL case Rs. 54.06 |
| Other parameters based on the unaudited financial results for the 9 months period ended on December 31, 2004 | Book Value per share<br>Rs. 36.92<br>Return on Networth 18.91%<br>Earning Per Share Rs. 6.98 |

| | |
|---|---|
| | Offer P/E [Price Earning Ratio] 13.24<br>P/E multiple for the Industry category, i.e., "Oil Drilling / Allied Services" is 11.8 [Source: "Capital Market" dated January 31, 2005 to February 13, 2005]<br>Fair Value of the share keeping in view Supreme Court decision in HLL case Rs. 54.06 |

Share price arrived at as per Regulation No. 20(5) of SEBI (Substantial Acquisition of Shares and Takeovers) Regulations in light of Supreme Court Judgment on Hindustan Lever case keeping in view the guidelines of erstwhile Controller of Capital Issues.

**Net Asset Value [Nav]**

Latest audited Balance Sheet available as on the valuation date is for the 12 months period ended on March 31, 2004 and forms the basis for estimating the NAV of the Company.

NAV of the Company per share is Rs. 29.94 as on March 31, 2004 and Rs. 36.92 as on December 31, 2004 [Annualized based on unaudited published financial results for the 9 months period ended on December 31, 2004.]

**Market Based Value**

The average of daily high and low prices of the shares of HOEC on National Stock Exchange [NSE] for the 2 weeks period ended on February 14, 2005 is Rs. 92.41.

The average of daily high and low prices of the shares of HOEC on Bombay Stock Exchange [BSE] for the 2 weeks period ended on February 14, 2005 is Rs. 92.05.

The average of weekly high and low of the closing prices of the shares of HOEC on NSE for the 26 weeks period ended on February 14, 2005 is Rs. 83.27.

The average of weekly high and low of the closing prices of the shares of HOEC on BSE for the 26 weeks period ended on February 14, 2005 is Rs. 83.21.

Source for share price and volume data: NSE web site and BSE website.

Note: Based on the information available, Equity Shares of HOEC are deemed to be frequently traded on BSE and NSE whereas Equity Shares are deemed to be infrequently traded on the Stock Exchanges at Delhi, Calcutta and Madras.

**Profit Earning Capacity Value [PECV]**

We have considered the last 3 years' audited financial results for the period [12 months period ended on March 31, 2002, March 31, 2003 and March 31, 2004] for assessing the profits.

It is noticed that average of NAV and PECV is less than 2 weeks average market price on NSE by more than 20% and hence PECV has been re worked at 11.5% capitalization rate with regard to 3 years' average net profit after tax as stipulated in CCI Guidelines under the head "Fair Value".

Value of the Equity Share of HOEC based on profit earning capacity would be Rs. 24.28.

**Share Valuation on Applying the Principles laid down by Supreme Court in the Judgment on Hindustan Lever Case.**

Considering Supreme Court decision in HLL Employees Union vs. Hindustan Lever Ltd (1995), 83 Com case 30, wherein the Hon'ble Court opined that Fair Value for a listed company could be assessed based on the following weightages:

- Net Asset Value 1
- Market Based Value 2
- Earning Based Value 2

Considering above:
Estimated Fair Value of Equity Share of HOEC is Rs. 50.40 as on March 31, 2004 and Rs. 51.79 as on December 31, 2004 [Annualized] whereas Estimated Fair Value of Equity Share of HOEC based on re worked PECV is

Rs. 52.66 as on March 31, 2004 and Rs. 54.06 as on December 31, 2004 [Annualized].

Accordingly, Fair Value of Equity Share of HOEC as per Regulation No. 20(5) of SEBI Takeover Regulations is Rs. 54.06 being the highest of above.

Fair value of the shares of HOEC for the purpose of open offer as per Regulation No. 20(5) of SEBI [Substantial Acquisition of Shares and Takeovers] Regulations, 1997 and subsequent amendments thereto is Rs. 54.06 per share.

## Justification for offer price

As per the parameters set out in Regulation 20(4) of SEBI Takeover Regulations, applicable for companies whose shares are frequently traded, the minimum offer price works out to Rs. 92.41 as illustrated above and the open offer price of Rs. 92.41 is the highest of the parameters as specified in Regulation 20(4) of SEBI Takeover Regulations.

As per the parameters set out in Regulation 20(5) of SEBI Takeover Regulations, applicable for companies whose shares are infrequently traded, the minimum offer price works out to Rs. 54.06 as illustrated above and the open offer price of Rs. 92.41 is the highest of the parameters as specified in Regulation 20(5) of SEBI Takeover Regulations.

## 4. Valuation of Equity Shares/ FCDs/ PCDs In their Preferential Issue According to SEBI Guidelines - SEBI (DIP) Guidelines, 2000.

### A. Guidelines for Preferential Issues

The preferential issue of equity shares/ Fully Convertible Debentures (FCDs)/ Partly Convertible Debentures (PCDs) or any other financial instruments which would be converted into or exchanged with equity shares at a later date, by listed companies whose equity share capital is listed on any stock exchange, to any select group of persons under Section 81(1A) of the Companies Act 1956 on private placement basis shall be governed by these guidelines.

13.1 Such preferential issues by listed companies by way of equity shares/ Fully Convertible Debentures (FCDs)/ Partly Convertible Debentures (PCDs) or any other financial instruments which would be converted into / exchanged with equity shares at a later date, shall be made in accordance with the pricing provisions mentioned below:

#### 13.1.1 Pricing of the issue

13.1.1.1 Where the equity shares of a company have been listed on a stock exchange for a period of six months or more as on the relevant date, the issue of shares on preferential basis shall be made at a price not less than higher of the following:

i) The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the six months preceding the relevant date;

OR

ii) The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange during the two weeks preceding the relevant date.

13.1.1.2 Where the equity shares of a company have been listed on a stock exchange for a period of less than six months as on the relevant date, the issue of shares on preferential basis can be made at a price not less than the higher of the following:

i) The price at which shares were issued by the company in its IPO or the value per share arrived at in a scheme of arrangement under sections 391 to 394 of the Companies Act, 1956, pursuant to which the shares of the company were listed, as the case may be;

OR

a. The average of the weekly high and low of the closing prices of the related shares quoted on the stock exchange during the period shares have been listed preceding the relevant date;

OR

b. The average of the weekly high and low of the closing prices of the related shares quoted on a stock exchange during the two weeks preceding the relevant date."

Provided that on completing a period of six months of being listed on a stock exchange, the company shall recompute the price of the shares in accordance with the provisions mentioned in sub-clause (i) of clause 13.1.1.1 and if the price at which shares were allotted on a preferential basis under clause 13.1.1.2 was lower than the price so recomputed, the difference shall be paid by the allottees to the company.)

Explanation:

a) "**relevant date**" for the purpose of clauses 13.1.1.1 and 13.1.1.2) means the date thirty days prior to the date on which the meeting of general body of shareholders is held, in terms of Section 81(1A) of the Companies Act, 1956 to consider the proposed issue provided however that in respect of shares issued on preferential basis pursuant to a scheme approved under the Corporate Debt Restructuring framework of Reserve Bank of

India, the date of approval of the Corporate Debt Restructuring package shall be the relevant date.

b) "**stock exchange**" for the purpose of clauses 13.1.1.1 and 13.1.1.2) means any of the recognised stock exchanges in which the shares are listed and in which the highest trading volume in respect of the shares of the company has been recorded during the preceding six months prior to the relevant date.

### 13.1.2 Pricing of shares arising out of warrants, etc.

13.1.2.1

(a) Where warrants are issued on a preferential basis with an option to apply for and be allotted shares, the issuer company shall determine the price of the resultant shares in accordance with Clause 13.1.1.1 above.

(b) The relevant date for the above purpose may, at the option of the issuer be either the one referred in explanation (a) to Clause 13.1.1.1 above or a date 30 days prior to the date on which the holder of the warrants becomes entitled to apply for the said shares.

13.1.2.2 The resolution to be passed in terms of Section 81(1A) shall clearly specify the relevant date on the basis of which price of the resultant shares shall be calculated.

13.1.2.3

(a) An amount equivalent to at least ten percent of the price fixed in terms of Clause 13.1.1.1 above shall become payable for the warrants on the date of their allotment.
(b) The amount referred to in sub-clause (a), shall be adjusted against the price payable subsequently for acquiring the shares by exercising an option for the purpose.
(c) The amount referred to in sub-clause (a) shall be forfeited if the option to acquire shares is not exercised.

### 13.1.3 Pricing of shares on conversion

13.1.3.1 Where PCDs/ FCDs/ other convertible instruments, are issued on a preferential basis, providing for the issuer to allot shares at a future date, the issuer shall determine the price at which the shares could be allotted in the same manner as specified for pricing of shares allotted in lieu of warrants as indicated in Paras 13.1.2.1& 13.1.2.2 above.

13.1A The explanatory statement to the notice for the general meeting in terms of Section 173 of the Companies Act, 1956 shall contain:

i. the object/s of the issue through preferential offer,
ii. intention of promoters/ directors/ key management persons to subscribe to the offer,
iii. shareholding pattern before and after the offer,
iv. proposed time within which the allotment shall be complete
v. the identity of the proposed allottees and the percentage of post preferential issue capital that may be held by them.)
vi. in case of a preferential allotment to which clause 13.1.1.2 is applicable, requirements specified in proviso to clause 13.1.1.2 and proviso mentioned after sub-clause (e) of clause 13.3.1.

13.1B A listed company shall not make any preferential issue of equity shares, Fully Convertible Debentures, Partly Convertible Debentures or any other instrument which may be converted into or exchanged with equity shares at a latter date if the same is not in compliance with the conditions for continuous listing.

13.1C A listed company shall not make any preferential allotment of equity shares, FCDs, PCDs or any other financial instrument which may be converted into or exchanged with equity shares at a later date unless it has obtained the Permanent Account Number of the proposed allottees.

## B. Case Study

**NAME OF THE COMPANY**

Pricing of Securities to be **issued on Preferential Basis** as per SEBI (DIP) Guidelines

Average Price of Weekly High & Low of the Closing Prices quoted on the Stock Exchange during the last six months preceding the relevant date (12-Dec-2007)

**Alternative I**

| Weeks | From | To | Closing High | Closing Low | Average |
|---|---|---|---|---|---|
| 1. | 13-Jun-07 | 19-Jun-07 | 86.95 | 85.65 | 86.3 |
| 2. | 20-Jun-07 | 26-Jun-07 | 92.15 | 87 | 89.575 |
| 3. | 27-Jun-07 | 03-Jul-07 | 92 | 90.4 | 91.2 |
| 4. | 04-Jul-07 | 10-Jul-07 | 92.25 | 91.75 | 92 |
| 5. | 11-Jul-07 | 17-Jul-07 | 102.7 | 92.6 | 97.65 |
| 6. | 18-Jul-07 | 24-Jul-07 | 100.25 | 90.5 | 95.375 |
| 7. | 25-Jul-07 | 31-Jul-07 | 88.8 | 86.65 | 87.725 |
| 8. | 01-Aug-07 | 07-Aug-07 | 89.4 | 86.65 | 88.025 |
| 9. | 08-Aug-07 | 14-Aug-07 | 89.75 | 86.7 | 88.225 |
| 10. | 15-Aug-07 | 21-Aug-07 | 86.35 | 85.05 | 85.7 |
| 11. | 22-Aug-07 | 28-Aug-07 | 86 | 83 | 84.5 |
| 12. | 29-Aug-07 | 04-Sept-07 | 88 | 85.85 | 86.925 |
| 13. | 05-Sept-07 | 11-Sept-07 | 90.25 | 87.25 | 88.75 |
| 14. | 12-Sept-07 | 18-Sept-07 | 92.4 | 89 | 90.7 |
| 15. | 19-Sept-07 | 25-Sept-07 | 94.4 | 91.6 | 93 |
| 16. | 26-Sept-07 | 02-Oct-07 | 91.1 | 88.45 | 89.775 |
| 17. | 03-Oct-07 | 09-Oct-07 | 90.15 | 85.85 | 88 |
| 18. | 10-Oct-07 | 16-Oct-07 | 86.45 | 84.6 | 85.525 |
| 19. | 17-Oct-07 | 23-Oct-07 | 85.55 | 82.9 | 84.225 |
| 20. | 24-Oct-07 | 30-Oct-07 | 90.55 | 85.45 | 88 |
| 21. | 31-Oct-07 | 06-Nov-07 | 110.3 | 92.1 | 101.2 |
| 22. | 07-Nov-07 | 13-Nov-07 | 105.25 | 101.5 | 103.375 |
| 23. | 14-Nov-07 | 20-Nov-07 | 111.05 | 105.35 | 108.2 |
| 24 | 21-Nov-07 | 27-Nov-07 | 109.25 | 102.45 | 105.85 |
| 25. | 28-Nov-07 | 04-Dec-07 | 106.55 | 102.85 | 104.7 |
| 26. | 05-Dec-07 | 11-Dec-07 | 111.1 | 104.7 | 107.9 |
| | **Average Price** | | | | **92.78** |

Average Price of Weekly High & Low of the Closing Prices quoted on the National Stock Exchange during the last two weeks preceding the relevant date (12-Dec-07)

**Alternative II**

| **Weeks** | **From** | **To** | **Closing High** | **Closing Low** | **Average** |
|---|---|---|---|---|---|
| 1. | 28-Nov-07 | 04-Dec-07 | 106.55 | 102.85 | 104.7 |
| 2. | 05-Dec-07 | 11-Dec-07 | 111.1 | 104.7 | 107.9 |
| | **Average Price** | | | | **106.3** |

| | |
|---|---|
| Date of EGM/AGM | 11-Jan-07 |
| Relevant Date (30 days prior to EGM/AGM) | 12-Dec-07 |
| 26 Weeks High Low Average Closing Prices | 92.78 |
| 2 Weeks High Low Average Closing Prices | 106.3 |
| Applicable Minimum Price | 106.3 |

## 5. Valuation under Wealth Tax

### A. Immovable Property – (Rule 3 To 8, Schedule III, Part B)

**Determine Gross Maintainable Rent (GMR) As Follows;**

a) If property is let out :
Higher of
- Annual rent received/receivable by the owner
- Annual value as assessed by local authority

In the following cases, such actual rent shall be increased in the manner specified below :

(i) where the property is in the occupation of a tenant and taxes levied by any local authority in respect of the property are borne wholly or partly by the tenant, by the amount of the taxes so borne by the tenant ;

(ii) where the property is in the occupation of a tenant and expenditure on repairs in respect of the property is borne by the tenant, by one-ninth of the actual rent ;

(iii) where the owner has accepted any amount as deposit (not being advance payment towards rent for a period of three months or less), by the amount calculated at the rate of 15 per cent per annum on the amount of deposit outstanding from month to month, for the number of months (excluding part of a month) during which such deposit was held by the owner in the previous year.

b) If property is not let out :

| Situated within jurisdiction of a local authority | Situated outside jurisdiction of a local authority |
|---|---|
| Annual rent assessed by the local authority | Amount owner can reasonable be expected to receive as annual rent had the property been let out |

**Determine Net Maintainable Rent (NMR) As Follows :**

Deduct the following from GMR

a) Taxes levied by any local authority in respect of property (deductible on accrual basis) This deduction is available even if taxes are to be borne by the tenant; and

b) 15% of GMR

**Capitalize NMR As Follows:**

| **Property situated on** | **Multiply NMR by** |
|---|---|
| (a) Freehold Land | 12.5 |
| (b) Leasehold Land (Unexpired period of lease is 50 year or more) | 10 |
| (c) Leasehold Land (Unexpired period of lease is less than 50 year) | 8 |

## Value of property

| | Value | Exception |
|---|---|---|
| Property acquired/ constructed After 31.03.74 | Capitalised NMR as provided hereinafter or Actual Cost (including of improvement) whichever is higher | For one house used wholly for residential purposes and cost thereof up to Rs.50 Lacs (in Delhi, Calcutta, Mumbai & Chennai) or Rs.25 Lacs (on other cities), the value is Capitalised NMR |
| Property acquired/ constructed on or prior to 31.03.74 | Capitalised NMR | None |

## Adjustments to value arrived for unbuilt area of plot of land :

Where the unbuilt area of the plot of land on which the property is constructed exceeds the specified area, the value arrived at as above shall be increased by an amount as follows:

| | Increase in Value |
|---|---|
| Unbuilt area exceeds specified area by 5 % to 10% of aggregate area | 20% |
| Unbuilt area exceeds specified area by 10 % to 15% of aggregate area | 30% |
| Unbuilt area exceeds specified area by 15 % to 20% of aggregate area | 40% |
| Unbuilt area exceeds specified area by > 20% of aggregate area | Above Rule Not applicable, Value estimated by Assessing / Valuation officer |

Specified area means 60% ( in Bombay, Calcutta, Delhi and Madras) to 70% of the aggregate area.

### Adjustment for unearned increase in the value of the land

Where the property is constructed on land obtained on lease from the Government, a development authority and the Government/ authority is, under the terms of the lease, entitled to claim and recover a specified part of the unearned increase in the value of the land at the time of the transfer of the property, the value of such property as determined under rule 3 shall be reduced by the amount so liable to be claimed and recovered or by an amount equal to fifty per cent of the value of the property as so determined, whichever is less, as if the property had been transferred on the valuation date.

Unearned increase means the difference between the value of such land on the valuation date as determined by the Government or development authority for the purpose of calculating such increase and the amount of the premium paid or payable to the Government / authority for the lease of the land.

## B. Valuation of Assets of Business – (Rule 14, Part D, Schedule iii)

1. In case accounts of the business are maintained regularly, value of assets as disclosed in the balance sheet shall be taken as follows :

| **ASSETS** | **VALUE TO BE TAKEN** |
|---|---|
| a) Depreciable Assets | Written down value |
| b) Non-depreciable Assets | Book value |

| | |
|---|---|
| c) Closing Stock | Value adopted for he purpose of Income tax |

2. If value of any asset determined as per provision of schedule III exceeds value as per above table by more than 20%, than higher value shall be taken as value of the assets
3. Value of assets not disclosed in balance sheet to be determined as per provisions of Schedule III
4. Value of following assets disclosed in balance sheet not be taken into account.
   a) Advance tax paid under Income tax Act.
   b) Bad debts allowed as deduction u/s 36(1) (VII) of Income tax Act.
   c) Assets in respect of which wealth Tax is not payable.
   d) Debit balance in profit & loss account, or any other amount which dose not represent value of any asset.
   e) Asset not really pertaining to the business.
5. Value of following liabilities disclosed in the balance sheet no to be taken into account:
   a) Capital employed in the business other than attributable to borrowed money.
   b) Reserve by whatever name called
   c) Any provision made for meeting any failure or contingent liability
   d) Liability not really pertaining to the business.
   e) Debt utilized for acquiring asset in respect of which Wealth tax is not payable.

## 6. Valuation Of Equity Shares Under the Companies Act, 1956

The Companies Act provides for Mandatory Valuation of Shares under the following provisions:

(a) Schemes of Compromise and Arrangement under Sections 391 to 394 of the Companies Act, excluding:
- Scheme of Compromise and Arrangement of a wholly owned subsidiary
- Compromise with creditors not amounting to either a business combination or a spin-off

(b) All equity and equity linked investments where shareholder approval is required under Section 372(A) of the Companies Act;

(c) Purchases, combinations and restructuring entailing acquisition of business, undertaking or substantial part of an undertaking, equity and preference capital, and outstanding debt and liabilities, where Related Parties are involved

(d) Recapitalisation of companies including but not limited to situations where the company's proposed capital reduction by buy-back or petitioning the Court under Section 100 of the Companies Act.

(e) Preferential allotments made to Related Parties and Persons controlling the company under Section 81(1A) under the Companies Act, 1956.

(f) Sale of a business including investment business and disposal of a controlling interest over an undertaking or a company through disposal of shares, an undertaking or a substantial part thereof including a slump sale/itemized sale under Section 293 (1) (a) of the Companies Act.

No specific methodology has, however, been prescribed under the said Act.

Yours faithfully
**Manoj Kumar Aggarwal**
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Tarun Sharma,
Love Mangla
Jitesh Bhugra and
Megha Almadi
(Chartered Accountants)
**(VALUERS)**