



MACRO ECONOMICS FACTORS AFFECTING VALUATION OF SHARES

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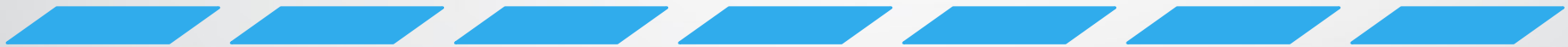
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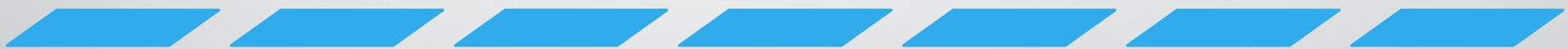


Valuation of Shares

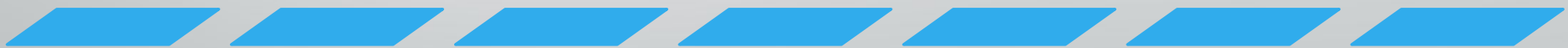
Valuation of shares involves the use of financial & accounting data



Depends on the valuer's judgement, experience & knowledge.



Any valuation based purely on quantitative data is not realistic.



Need for Valuation

Need

- For the shares not listed in Stock Exchange
- For the listed shares when there is no transactions
- Market quotation of listed shares may not show true value
- Valuations statutory required
- Shares of Private Limited Companies
- Large block of shares under transfer

Methods of Valuation

Asset based

- Net Assets Method

Profit based

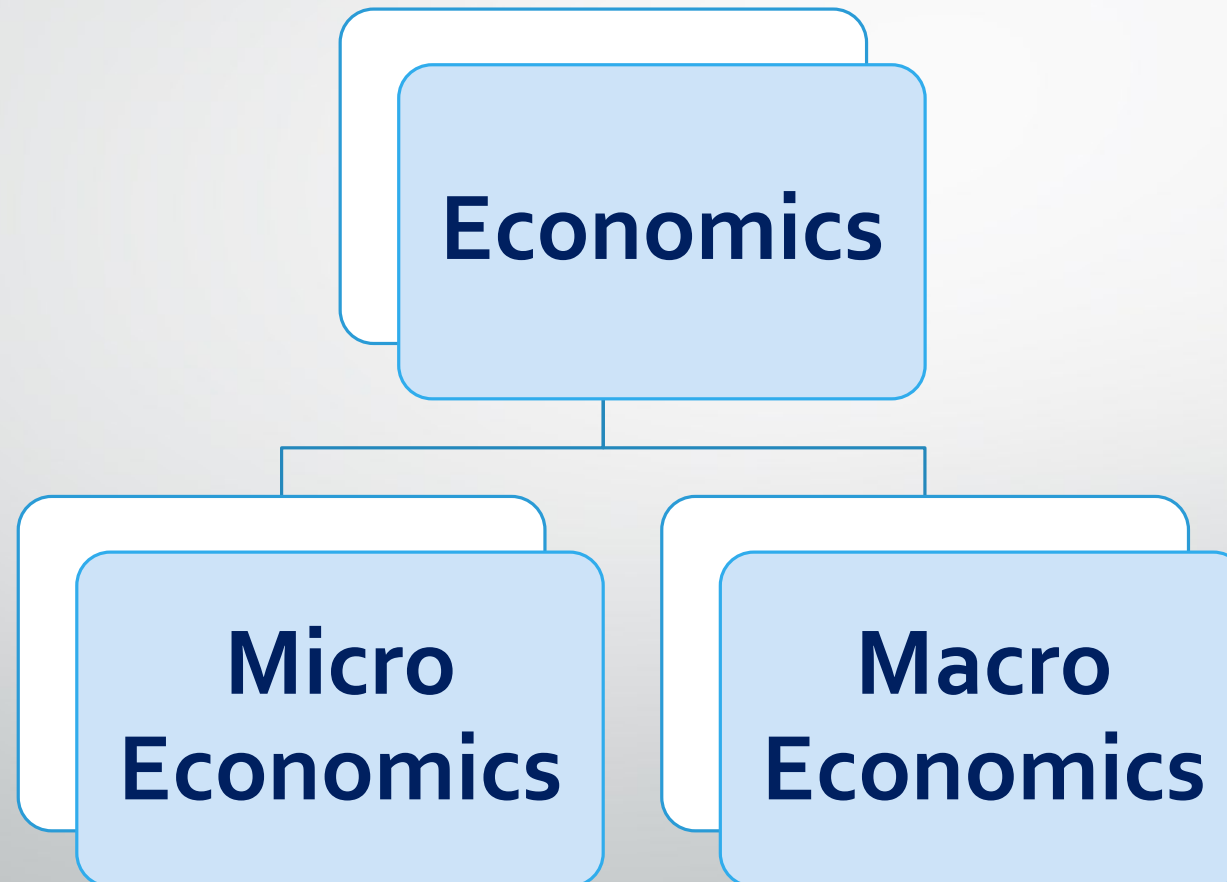
- Yield Method

Asset & Profit based

- Fair Value Method

Economics:

Economics is a study of the allocation of scarce means capable of alternative uses, among competing ends for the attainment of a maximum result in the achievement of these ends.



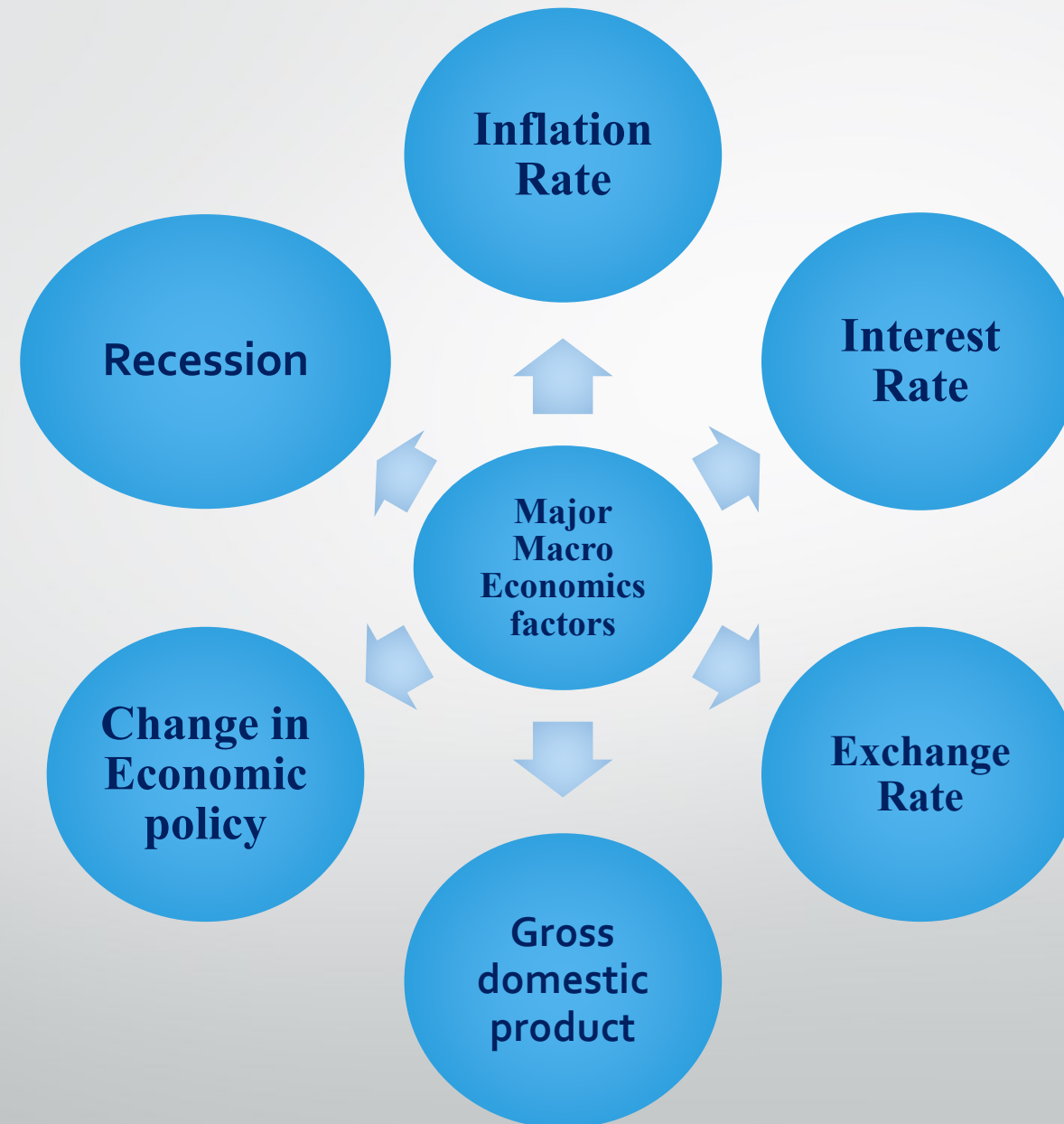
Micro Economics

Micro Economics is basically the study of the behavior of different individuals and organizations within an economic system. In other words, Microeconomics examines how the individual units (consumers or firms) make decisions as to how to efficiently allocate their scarce resources.

Macro Economics

Macro-Economics is the study of the behavior of the large economic aggregates, such as, the overall levels of output, total consumption, total saving and total investment and also how these aggregates shift over time.

In other words, Macro Economics is the study of the overall economic phenomena of the economy as a whole, rather than its individual parts.



Inflation



○ **Inflation** is the rate at which the general level of prices for goods and services is rising and, consequently, the purchasing power of currency is falling. It is usually characterized by an overflow of money and credit.

******The root cause of inflation is the expansion of money supply beyond the normal absorbing capacity of the economy.

Causes of Inflation

- ☐ Increase in population
- ☐ Expansion of Money Supply
- ☐ Expansion of bank credit
- ☐ High indirect tax
- ☐ Deficit financing

Measurement of Inflation

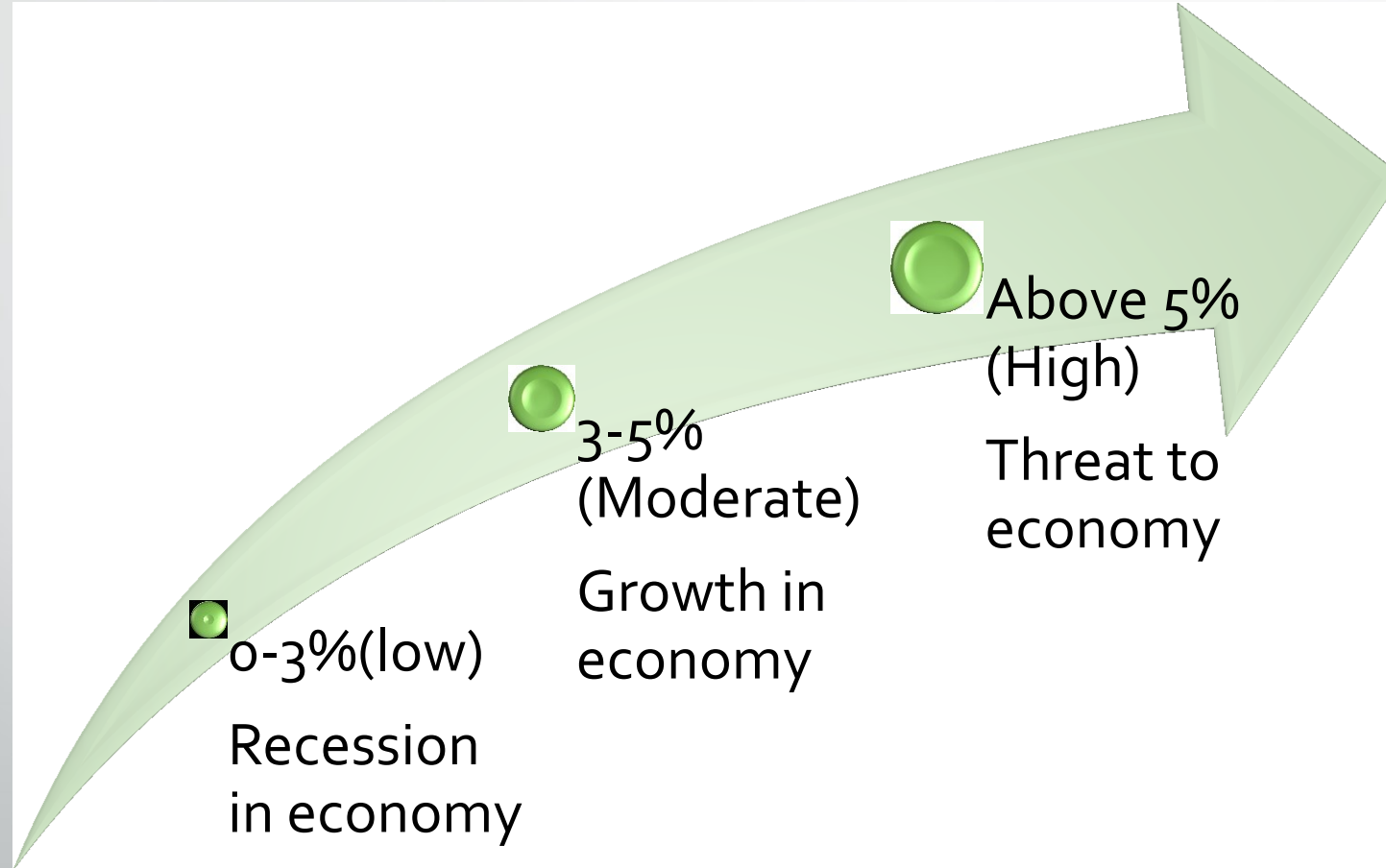
The rate of inflation is measured by the annual percentage change in the level of prices as measured by the consumer price index.

Important measurement tools:

Consumer Price Index

Wholesale price index

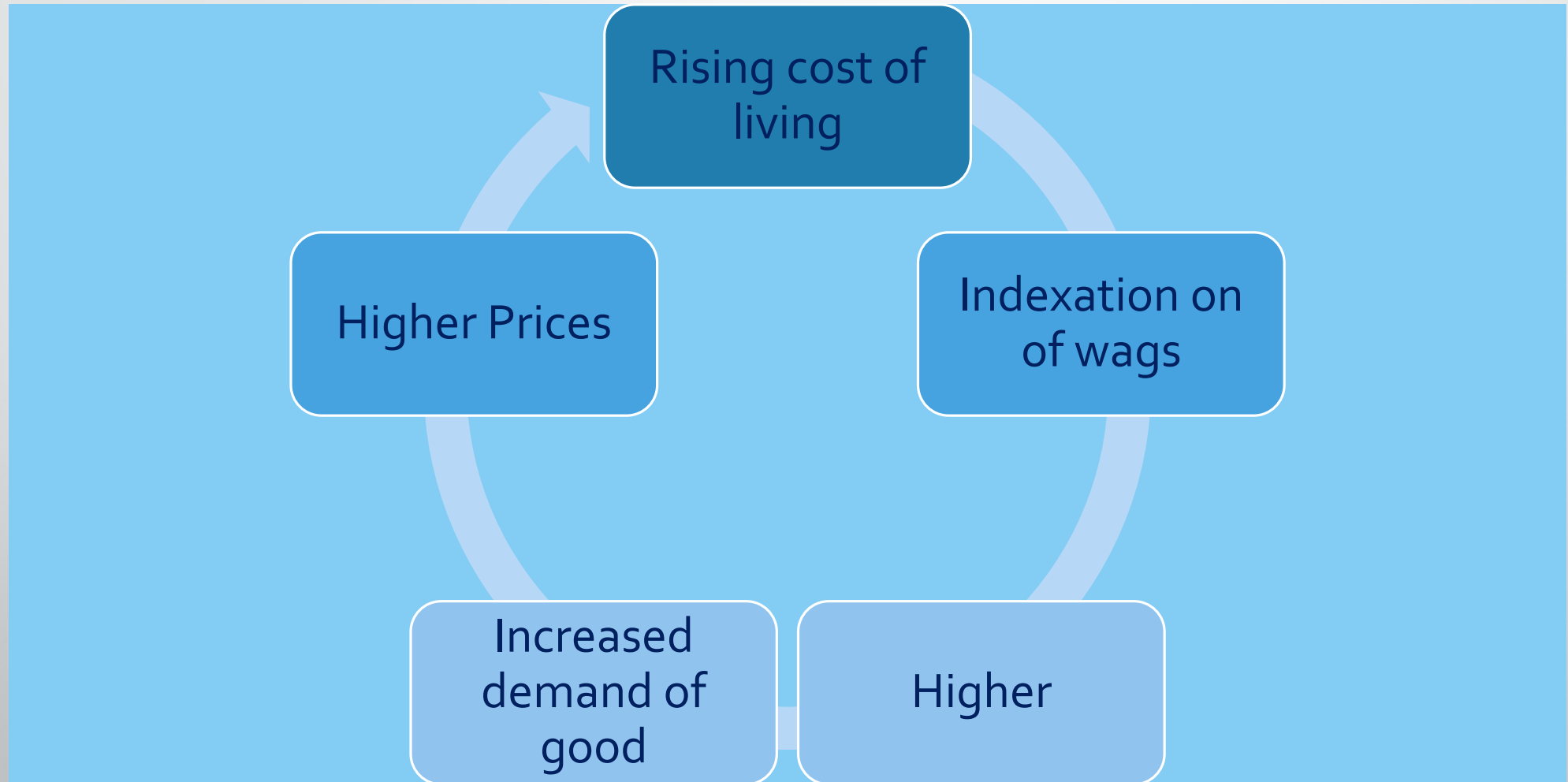
Impact of inflation



Inflation Affecting Valuation Of Shares

- Stocks are often broken down into subcategories of value and growth. Value stocks have strong current cash flows that will slow over time, while growth stocks have little or no cash flow today, but it will gradually increase over time.
- Therefore, when valuing stocks using the discounted cash flow method, in times of rising interest rates, growth stocks are negatively impacted far more than value stocks. Since interest rates are usually increased to combat high inflation, the corollary is that in times of high inflation, growth stocks will be more negatively impacted. This suggests a positive correlation between inflation and the return on value stocks and a negative one for growth stocks.

Wage Price Spiral



Impact of inflation on Economy

- Higher rate of interest charged by banks on borrowings.
- Higher rate of interest demanded by depositors.
- Early payment of borrowings.
- Decrease in investment.
- Uncompetitive exports.
- Pressure on balance of payment
- Deprecation of currency
- Loss of credibility

Impact on Companies

Diversion of efforts from productive activities to drawing strategies in coping with inflation

Enormous involvement in inventory management

Reported profits are untrustworthy

Frequent adjustment in wages

Failure of budgets and long-term plans

Loss of national productivity

Impact on investors



INTEREST RATE

- Interest rate is the price demanded by the lender from the borrower for the use of borrowed money.
- Interest is a fee paid by the borrower to the lender on borrowed cash as a compensation for forgoing the opportunity of earning income from other investments that could have been made with the loaned cash.
- Thus, from the lender's perspective, interest can be thought of as an "opportunity cost".

From a borrower's perspective, interest rate is the cost of capital.

Interest rate factors

Uncertainty

Inflation

Monetary policy

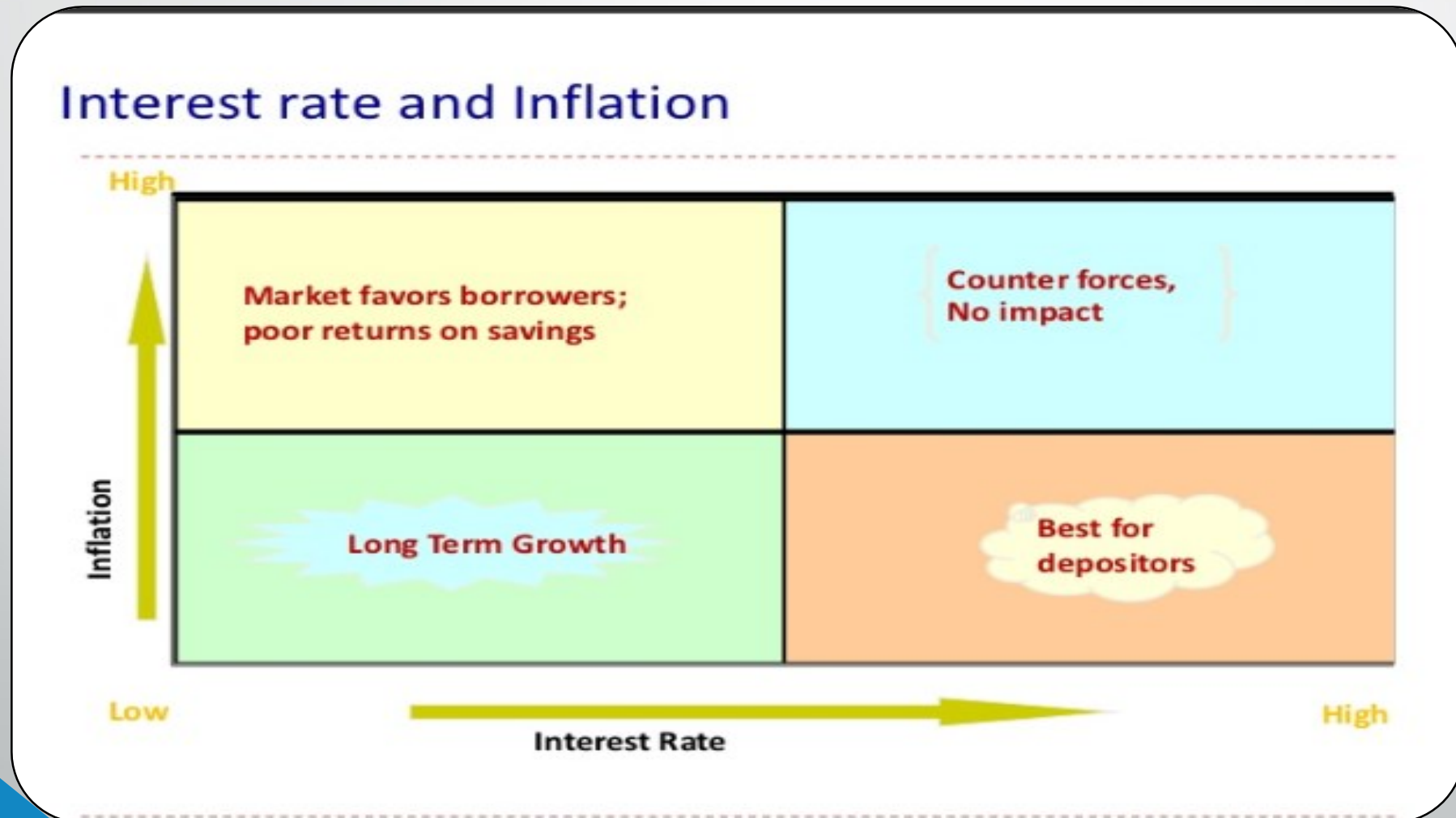
Global liquidity

Impact of Interest rate on shares value:

- If a company borrows money to expand and improve its business, higher interest rates will affect the cost of its debt.
- This can reduce company profits and the dividends it pays shareholders.
- As a result, its share price may drop. And, in times of higher interest rates, investments that pay interest tend to be more attractive to investors than stocks.

Example: The Bank of Canada can raise or lower interest rates to stabilize or stimulate the Canadian economy. This is known as monetary policy.

Relationship between interest rate and inflation:



EXCHANGE RATE

- The exchange rate is defined as "the rate at which one country's currency may be converted into another." It may fluctuate daily with the changing market forces of supply and demand of currencies from one country to another.
- A country's foreign exchange rate provides a window to its economic stability, which is why it is constantly watched and analyzed.

Key factors that affect Exchange rates:

- Inflation Rates
- Interest Rates
- Balance of payment
- Government debt
- Terms of trade
- Political stability & performance
- Recession
- Speculation

Impact of exchange rate on equity shares:

- When rupee harden in respect to other currencies, it sets a multidimensional chain reaction.
- Companies drastically affected are the ones involved in overseas operations, reason there a fall in demand for their goods in abroad.
- Revenue from exports decline, and stock prices of such companies in home country fall.
- Importing companies, on the hand, are benefitted by hardening of the rupee. They need to shell out lesser on imported goods which reduce the cost of operation. It, in turn, increases their bottom line along with raising their share price.

GROSS DOMESTIC PRODUCT

- **Gross Domestic Product (GDP)** is the broadest quantitative measure of a nation's total economic activity. More specifically, GDP represents the monetary value of all goods and services produced within a nation's geographic borders over a specified period of time.
- $\text{GDP} = \text{Consumption} + \text{Government Expenditures} + \text{Investment} + \text{Exports} - \text{Imports}$

Also denotes as $Y = C + I + G + NX$

Impact of GDP on shares

- **Strong GDP** growth translates into higher corporate earnings, which bodes well for the stock market.
- **Falling GDP** means economic growth is weakening, which is negative for earnings and therefore stock prices.
- **For bond**, the direction of GDP often has the opposite effect

GDP IMPACT

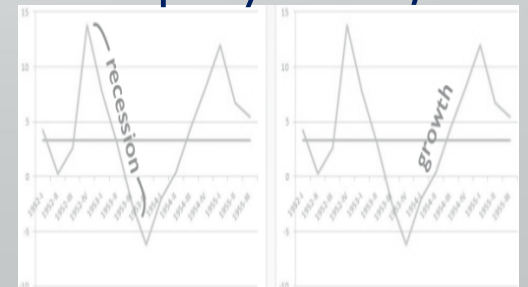
- Strong GDP growth usually means a greater demand for borrowing by businesses and is often a sign of impending inflation. This usually translates into higher interest rates, which depresses bond prices.
- Declining GDP generally means lower inflationary pressures as well as lessening demand for borrowing, which then generally means lower interest rates and higher bond prices.

RECESSION

A recession generally lasts from 6 to 18 months, but can sometimes last longer.

Recessions increase unemployment because in hard economic times when production is slowing down, firms are less willing to hire workers.

The worst global recession since WWII. The years leading up to the crisis were characterized by a boom in economic demand, but suddenly many large and well established investment & commercial banks in the United States & Europe suffered huge losses and bankruptcy. The global recession that followed resulted in a sharp drop in international trade, rising unemployment, and falling commodity prices.



Causes of Recession

High-interest rates.

Stock market crash.

Slowdown in manufacturing orders

Asset bubbles

Impact of Recession



Recession Affecting Valuation Of Shares

- A recession is a slowdown or halt to the economic growth of the country. This can lead to unemployment and lower spending by individuals and companies. All the factors in a recession are intertwined. For instance, unemployment is likely to increase as companies try to boost their margins -- when people spend less because of the increase in unemployment. The factors feed into one another in a declining spiral. Companies suffer from lower revenues, lower profits, and weaker growth in the future. All those factors come into play to determine the value of a stock on a fundamental level. As the companies' business suffers, so too does their stock price, leading the whole stock market lower.

Economic Policy

- A country's government shapes the business environment in which companies operate.
- Government policies such as changes to regulations, taxation, interest rates and spending programs therefore have a huge influence on individual companies' performance and their stock price.

Factors of Economic policies:

- Monetary policy
- Fiscal Policy
- Regulatory Policy
- Taxation

Factors of economic policy

- **Monetary Policy:** Monetary policy refers to the control of money supply in the economy and governments use it to either stimulate or cool an economy that they think is growing too slowly or is suffering from high inflation.
- **Fiscal Policy:** Fiscal policy is where the government undertakes spending programmes to stimulate the economy.
- **Regulatory Policy:** Governments are responsible for regulating certain industries such as banking, insurance and telecommunications.
- Governments sometimes change the legislation that will make it easier or more difficult for a particular sector to perform well.
- **Taxation:** Every company is subject to various forms of taxation, either directly or indirectly, and changes in taxation will affect their performance

Change in Economic policies impact on share price

- Economic policies of a country totally depend on governing government.
- Political events, influence the share price of company.
- If a new government comes into power, it may decide to make new policies.
- Sometimes these changes can be seen as good for business, and sometimes not.
- They may lead to changes in inflation and interest rates, which in turn may affect stock prices.

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thank
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