



THE MOST CLOSELY WATCHED STATISTIC ON WALL STREET - EPS

Earnings per share (EPS) is an important indicator of the success or failure of a company.

EPS is a carefully scrutinized metric that is often used as a barometer to gauge a company's profitability per unit of shareholder ownership.

It is a portion of a company's profit allocated to each outstanding share of common stock.

AS -20 "Earning Per Share" has come into effect in respect of accounting periods commencing on or after 01-04-2001 and is mandatory in nature from then.



OBJECTIVE

There may be two types of EPS :

- Earning per share is a financial ratio that gives the information regarding earning available to each equity shareholder.
- To improve comparability as between two or more companies and as between two or more accounting periods.

Basic

Considers only common shares outstanding

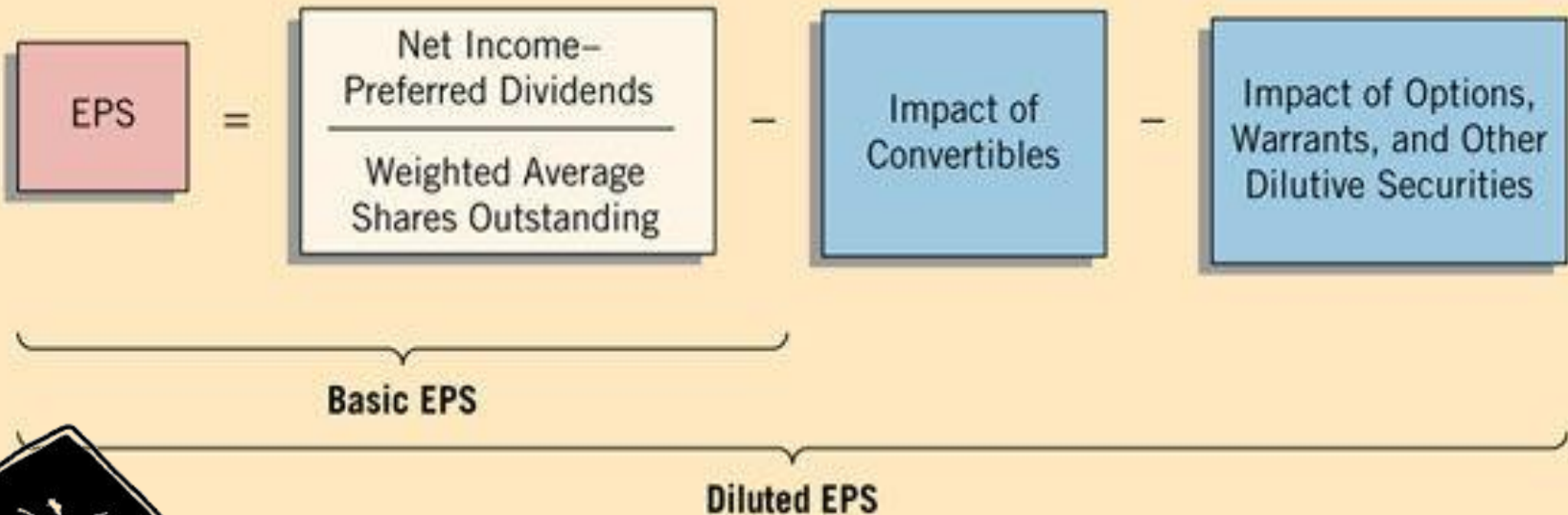
Diluted

Reflects the maximum potential dilution from all possible stock conversions that would have decreased EPS.

- There is no rule of thumb to interpret earnings per share. The higher the EPS figure, the better it is. A higher EPS is the sign of higher earnings, strong financial position and, therefore, a reliable company to invest money.



Relation between Basic and Diluted EPS



CAPITAL STRUCTURE DETERMINES REPORTING

- Many companies will report basic earnings per share only.
- Other companies must report BOTH basic and diluted earnings per share
- It depends on whether the capital structure is
 - Simple, or
 - Complex

A simple capital structure consists of just **common stock**.



The corporation has only common and nonconvertible preferred stock.

It has no convertible securities, stock options, warrants, or other rights outstanding.

Capital Structures



Complex Capital Structure:
The corporation has one or more instruments outstanding that could result in issuance of additional common shares.

Convertible
Preferred

Convertible
Bonds

Stock
Options

Diluted earnings per share (Diluted EPS) takes the **basic earnings** per share figure one step further. Basic EPS only takes into account the number of shares outstanding at the time. Diluted EPS, on the other hand, estimates how many shares could **theoretically exist after** all stock options, warrants, preferred stock and / or convertible bonds have been exercised.

CALCULATION OF NET PROFIT/LOSS FOR THE PERIOD ATTRIBUTABLE TO EQUITY SHAREHOLDERS

Particulars	Amount
Net Profit/loss for the period including prior period terms and extraordinary item	XXX
Deduct tax Liability (Current + Deferred)	(XXX)
Deduct preference share dividend & any attributable tax on Pre. Dividend	(XXX)
* Dividend on non cumulative preference share is deducted if dividend is provided	
* In cumulative pre. Share if dividend is not provided than also it will be deducted	
Note:- If an enterprise has more than one class of equity shares, net profit or loss for the period is apportioned over the different classes of shares in accordance with their dividend rights	

A QUESTION FOR YOU ALL

- When Bonus issues or stock split, etc occurs after the date on which Financial Statements are approved by the BOD, will they be considered for calculation of EPS ?

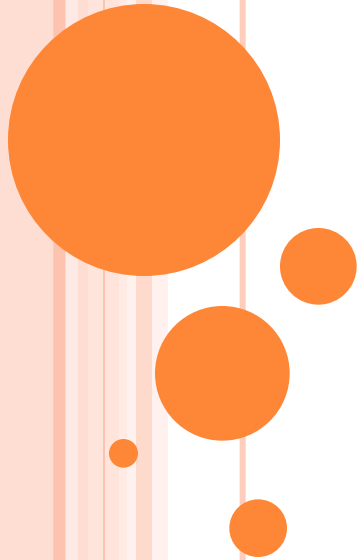
Answer : This will be considered as a prior period item and share calculations will be made considering it.





EARNINGS PER SHARE (EPS)

Is it an effective way
to Evaluate Investment
?





...Disadvantages ..

Of EPS as an Investment Indicator.....



Whaaaaaat?!?
Are you serious?!?



- EPS measure is that a company has a lot of discretion when deciding what is and so the figure is open to manipulation.
- EPS will be distorted if a company conducts a share buy-back.
- EPS takes no account of a company's debt position and financial leverage, factors that an investor needs to be aware of.
- For increasing the Income figures, management of the company can offer sales channels or retailers any incentives such as extended money back guarantee on unsold stock of goods/inventories. This way finished goods inventories move into the distribution channel and the credit sales have been registered in company books and accrued/outstanding earnings figures increased, but actual cash might never be received, because of the inventories returned as per terms of guarantee, this may increase sales in one quarter or so.



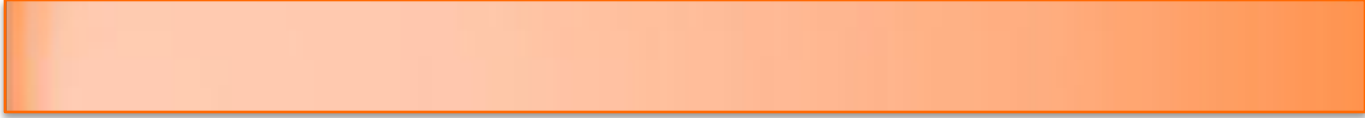
NOW YOU PROBABLY START THINKING, HOW CAN WE EVALUATE THE REAL EARNING FIGURES OF PARTICULAR COMPANY TO AVOID BEING INVESTED WITH MANIPULATED FIGURES?



Well, the solution is quite simple in comparison to the critical problem of EPS manipulation. You can always determine the actual earnings position with help of operating cash flows. Operating cash flows figure consists of net Cash inflows or outflows from operation activities, simply How much cash the company has generated from its actual business activities and not included cash flows from supplementary activities like investments etc.



6 INDICATORS USED TO ASSESS STOCKS



EPS



P/E RATIO



PRICE TO EARNINGS RATIO
TO GROWTH RATIO



PRICE TO BOOK VALUE RATIO



DIVIDEND PAYOUT RATIO



DIVIDEND YIELD



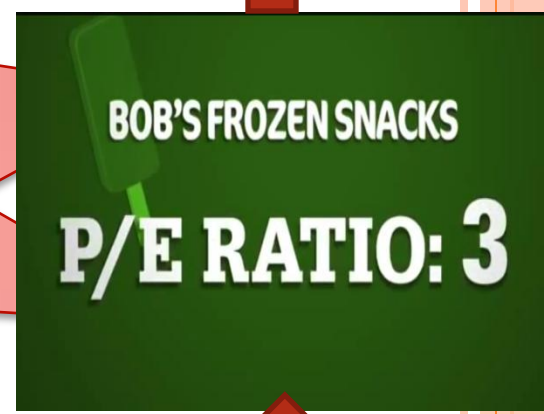
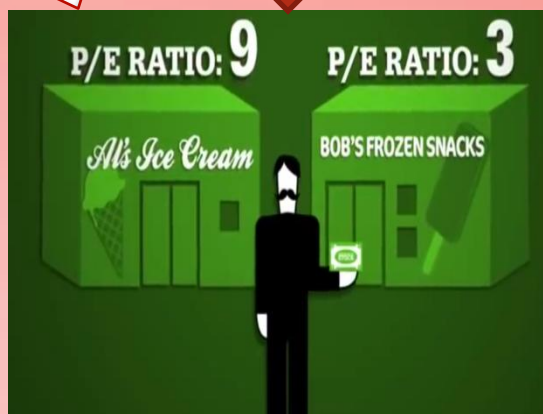
P/E RATIO =



**CURRENT PRICE
OF A STOCK**



**COMPANY'S
EARNINGS PER
SHARE**



Price to earnings ratio to growth ratio (PEG) - It's calculated by dividing the P/E ratio by the company's projected growth in earnings.

- **Example** – A stock with a P/E of 30 and projected earnings growth next year of 15% would have a PEG of 2 (30 divided by 15)

Price to book value ratio (P/B) - This compares the value the market puts on a company with the value the company has stated in its financial books. It's calculated by dividing the current price per share by the book value per share. Most of the time, the lower the P/B is, the better. That's because you're paying less for more book value.

Dividend payout ratio (DPR) - This measures what a company pays out to investors in dividends compared to what the stock is earning. It's calculated by dividing the annual dividends per share by the EPS.

- **Example** – If a company paid out \$1 per share in dividends and had an EPS of \$3, the DPR would be 33% (1 divided by 3).

Dividend yield - This measures the return on a dividend as a percentage of the stock price. It's calculated by dividing the annual dividend per share by the price per share.

- **Example** – 2 stocks each pay an annual dividend of \$1 per share. Company A's stock is trading at \$40 a share, but Company B's stock is trading at \$20 a share. Company A has a dividend yield of 2.5% (1 divided by 40), while Company B's is 5% (1 divided by 20).

CONCLUSION

- EPS is an important indicator for evaluation of an Investment but a investor should not solely rely on. After going through the above limitations of EPS, it's clear that this measure should not be used in isolation.

EPS

P/E Ratio





Thanks

Any Questions ????????????

