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Analytical Study on Fundamental Analysis and Behaviors of Market Price of Shares Listed in NSE, India

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Abstract: Before making any investment decision it is advised that an investor should have sufficient knowledge about the stock market. An analysis of stock market can be done by two ways viz. Fundamental Analysis and Technical analysis. The main focus in the proposed study will be on the tools of fundamental analysis in predicting the future value of company. For the purpose of this study, secondary data is collected from the Annual reports of last 5 years (from 2014 to 2018) of 5 Companies from different sectors, viz., TCS, NTPC, L&T, Mahindra & Mahindra and HDFC Bank. The data collected was used to evaluate the EPS, P/E Ratio, etc. The paper also focuses on calculating the intrinsic value of shares. The intrinsic value so calculated is compared with market price of shares and if such intrinsic value is found to be greater than market value the share is said to be undervalued, whereas if intrinsic value is less than market value the share is said to be overvalued. On the basis of share valuation: TCS, Mahindra & Mahindra and NTPC is undervalued as its intrinsic value is higher than its market value and suggested to buy the share since the price of the same may increase in future. In contrast, L & T and HDFC Bank Ltd. are overvalued as their market value is higher and preferred to sell the share as the share price may fall.

Keywords: Fundamental Analysis, Investment decision, Intrinsic Value, Share price.

1. INTRODUCTION:

Stock markets have become highly complex markets that allow investors to buy shares in companies or in funds that aggregate companies or industries together. Most stock markets today are primarily electronic networks, although they often maintain a physical location for buyers, sellers and market makers to interact directly.

The study is done for the purpose of conducting fundamental analysis of leading securities in the stock market. In the stock market share price of companies are determined by the demand and supply forces operating in the market. These demand and supply forces in turn are

influenced by a number of fundamental factors as well as certain psychological or emotional factors. The combined impact of all these factors is reflected in the share price movement. The price movements of securities follow systematic and certain consistent patterns. Past movements in the prices of shares help to identify trends and pattern. It is useful for the prediction of future price movements.

The main focus in the proposed study will be on the tools of fundamental analysis in predicting the future value of company. The earnings of the company, the growth rate and the risk exposure of the company have a direct bearing on the price of the share. The factors in turn rely on a host of other factors like economic environment in which they function, the industry they belong to, and finally the companies' own performance. Fundamental analysis consists of an appraisal of the intrinsic value of shares through.

With globalization and innovation in the financial markets at its peak - it is very essential to study the market risks and requirements. Over the years, the Indian stock market has undergone major changes to remain at par with the global peers. With global trade and finance getting more dynamic day by day, the Indian stock market is not far behind to experience these developments. This has helped the financial structure of India get more innovative. Fundamental analysis maintains that markets may incorrectly price a security in the short run but that the "correct" price will eventually be reached. Profit can be made by purchasing the wrongly priced security and then waiting for the market to recognize its "mistake" and re-price the security.

Statement of Problem: Much of economic and financial theory is based on the notion that individuals act rationally and consider all available information in the decision-making process. However, researchers have uncovered a surprisingly large amount of evidence that this is frequently not the case. Dozens of examples of irrational behavior and repeated errors in judgment have been documented in academic studies. Hence, investors need a strategy that they can adopt while training in stock market and for this fundamental analysis is the solution. Fundamental Analysis is the strong tool that guides the investors about the strategies of investment in stock market by letting the investor know how to study the fundamentals of the company, the study also reveals the importance for the investment decision which acts as guidance and helps them in decision making and predicting the figure price of the stocks.

2. LITERATURE REVIEW

Leena Lassi and Shubham Solanki (2017) in her study on fundamental analysis of Pharmaceutical Sector emphasized the need of fundamental analysis to help the investor for taking informed investment decisions. They mostly focussed on fundamental analysis of pharmaceutical sector. Their research is helpful to the investors in making investment decision so as to maximize return from the security. The study focuses on all three aspects of fundamental analysis i.e:-economic analysis, industry analysis and company analysis.

Manicka Mahesh and Saravana Kumar (2016) in their study attempted to apply fundamental analysis on six selected scrips from FMCG industry from 2004–05 to 2014–15. It is the attitude of people to look for either capital appreciation or regular income from their investment. In order to attain that objective, one of the best way to get higher return in long term, is obviously stock market. Investors cannot get higher rate of return in all the companies in various sectors of stock market. Sustainability of pricing of the scrips is not dependent on the euphoria built among the market participants but the valuation of the securities and market perfectly. To value the market properly, fundamental analysis has to be done. The main focus of their study is to value the share prices of the selected FMCG companies through fundamental analysis.

According **to Shilpa K S. et al (2017)**, every investor is advised to have enough knowledge about the stock market before making any investment decisions. Analysis of capital market can be done either through fundamental analysis or technical analysis. The authors aimed to study on Fundamental analysis of selected IT companies listed on NSE. Fundamental analysis constituted 3tier approach. Economic analysis dealing with fundamental factors like GDP, IIP, fiscal deficit, inflation, current account deficit etc. Industry analysis of Indian IT sector analyzed based on entry barriers, type of industry, government interference, Porter's five force model. Finally, Company analysis deals with various ratios such as dividend payout ratio, EPS, P/E ratio, Debt -Equity ratio are used. It also focuses on the calculation of 'Intrinsic Value' of shares and compared with 'Market Value'. If intrinsic value is greater than market value the share is said to be undervalued whereas if market value is greater than intrinsic value, the share is overvalued. From the study Wipro, TCS and Infosys shares are undervalued and suggested to buy and hold the shares.

3. RESEARCH METHODOLOGY

For the purpose of this study, descriptive research methodology is used and secondary data is collected from the Annual reports of last 5 years (from 2014 to 2018) of 5 Companies from different sectors, viz., TCS, NTPC, L&T, Mahindra & Mahindra and HDFC Bank. The data collected will be used to evaluate the EPS, P/E Ratio, etc. Further the data will be collected from websites of the above companies.

4. OBJECTIVE OF THE STUDY

The following are the objective of the study:

- To study the Fundamental Analysis for five company scrips to recommend for better choice of investment.
- To analyze the Intrinsic value of the selected companies.
- To forecast the future value of selected companies through fundamental analysis.
- To suggest the best strategy of investment i.e. to buy, sell or hold the security.

5. TOOLS AND TECHNIQUES

In this study, the future share prices of the selected five companies are predicted on the basis of following tools:

- Earnings per share- EPS
- Price to book – P/B
- Dividend Payout ratio
- Earning Yield Ratio
- Return on equity

6. DATA ANALYSIS

In this paper, an attempt is being made to predict the future value of the shares of TCS, L&T, Mahindra & Mahindra, NTPC and HDFC Bank Ltd.. For this purpose various ratios were calculated viz., Earnings per share, Price to Book value, Dividend Payout Ratio, Earning Yield Ratio and Return on equity ratio.

6.1 Earnings per Share

This ratio indicates the profits available to equity shareholders per share, this helps to determine the market price of equity shares. Earnings per share (EPS) is the portion of a company's profit allocated to each share of common stock. It is calculated as follows:

Earnings per Share = Profit after Tax / No. of equity shares

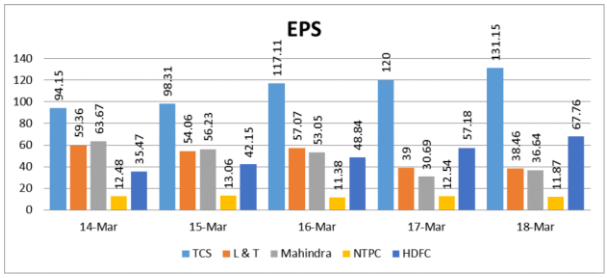


Fig. 1 Earnings per Share of 5 selected companies

Source: Moneycontrol.com

The higher the EPS, the more will be will be the worth of stock because investors are willing to pay more for higher profits. Fig. 1 shows that the EPS of TCS and HDFC has increased gradually from March 2014 to March 2018. EPS is a good parameter for investors as well as for the expansion of firm. The most obvious way for a company to grow its earnings is to grow its revenue.

6.2 Dividend Payout Ratio

The D/P ratio is the ratio between the DPS and EPS of the firm, i.e., it refers to the proportion of the EPS which has been distributed by the company as dividends. The dividend payout ratio is the fraction of net income a firm pays to its stockholders in dividends. Dividend payout ratio may be calculated as follows:

Dividend Payout Ratio = DPS / EPS x 100

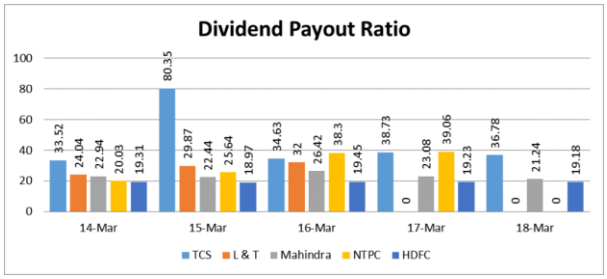


Fig. 2 Dividend Payout Ratio of 5 Selected Companies

The dividend payout ratio of **TCS** for March 2014 is 33.52 and it rise Up to 80.35 in march 2015, a higher payout ratio indicates that a company is sharing more of its earnings with stockholders. Rest of the companies like L&T, Mahindra, NTPC and HDFC have shown a stable returns. A payout ratio of more than 100% means that a company's dividend payments are exceeding its net income.

6.3 Return on Equity: Return on equity (ROE) is a measure of financial performance calculated by dividing net income by shareholders' equity. Because shareholders' equity is equal to a company's assets minus its debt, ROE could be thought of as the return on net assets. The ratio is calculated as follows:

Return on equity = Net Income/ Shareholders Equity

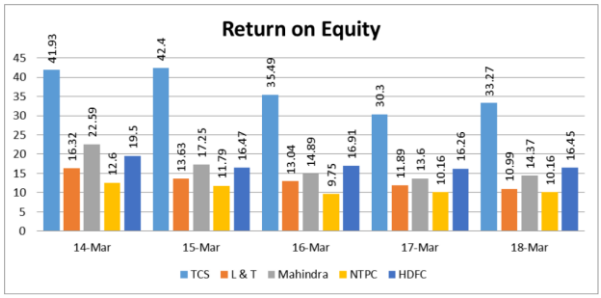


Fig. 3 Return on Equity Ratio of 5 Selected Companies

ROE is a measure of management's ability to generate income from the equity available to it. ROEs of 15-20% are generally considered good. ROE is also a factor in stock valuation, in association with other financial ratios. While higher ROE ought intuitively to imply higher

stock prices, in reality, predicting the stock value of a company based on its ROE is dependent on too many other factors to be of use by itself.

6.4 Price to Book Value Ratio

Companies use the price-to-book ratio to compare a firm's market to book value by dividing price per share by book value per share (BVPS). An asset's book value is equal to its carrying value on the balance sheet, and companies calculate it netting the asset against its accumulated depreciation. The ratio is calculated as follows:

Price to Price/Book Value Ratio = Market price per share / Book Value Share

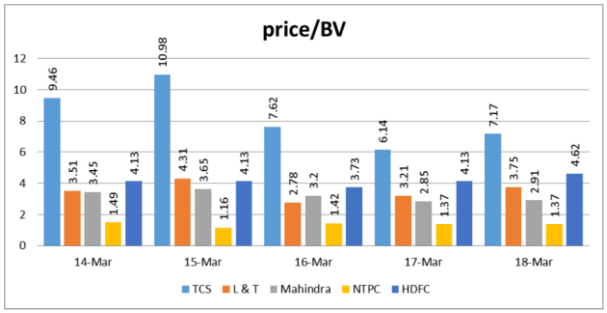


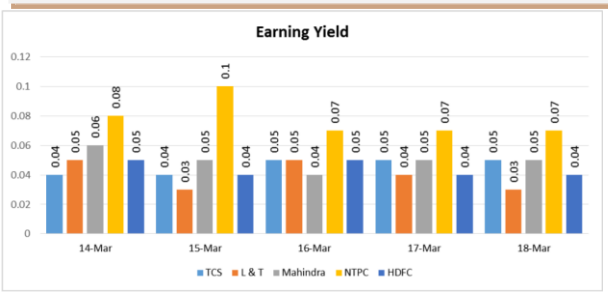
Fig. 4 Price to Book Value of 5 Selected Companies

If a company's P/BV ratio is high compared to others in its industry, then the stock might be overvalued. If its P/BV ratio is low compared to others in its industry, then it might be undervalued or the company may be performing poorly. Acquisitions can also reduce the book value of a company

6.5 Earnings Yield Ratio

The earnings yield (which is the inverse of the P/E ratio) shows the percentage of each rupee invested in the stock that was earned by the company. Earnings yield ratio is an effective restatement of price earnings ratio. It shows earnings per share as a percentage of the market value of the ordinary share. It is arrived at by dividing the earnings per share (EPS) for the last 12 months by the current market value of the share and multiplying the result by 100. It is formulated as:

Earnings Yield Ratio = Earnings per share/ Market Price per Share



The TCS has constant earning yield ratio in the year march 2014 & March 2015 that is 0.04 & it has slightly increased And constant that 0.05 in the year March 2016, 2017 & 2018. It increases due to increase in Earning per share in proportion to market price per share. The L&T has constant earning yield ratio in the year March 2014 & 2016. It slightly drops in the year march 2015, 2016 & 2018 it is constant in the year march 2015 & 2018 that is 0.03. It is also found that while comparing similar stocks, the one which gives high earnings yield should give higher returns. For Mahindra & Mahindra**, t**he earning yield is 0.06 in March 2014 it slightly declines to 0.05 and constant for the year march 2015, 2017, & 2018. Ratio of NTPC has shown an increase in initial years i.e. up to March 2015, but after that it has given constant return.

6.6 Valuation of Shares

The future value of shares is obtained from product of projected EPS and normalized Average P/E ratio. Whereas to compute the projected EPS, growth factor is considered and it is added to current EPS. However, growth is estimated from the product of Average Return on Equity and Average retention ratio. The estimation of future value of shares is explained in table 1.

Table 1 showing future value of share

	TCS	L & T	Mahindra	NTPC	HDFC
Average Return on Equity (ROE/ No. of years)	36.678	13.174	16.54	10.892	17.118
Average DPR	44.802	17.182	23.224	24.606	19.228
Average Retention Ratio (1 – DPR)	55.198	82.818	76.776	75.394	80.772
Growth on Equity (Avg. Retention Ratio *Avg. ROE)	1.504935	6.286473	4.641838	6.921961	4.718542
Normalized Average P/E Ratio	25.07	22.34	18.93	12.57	33.41
Current EPS	132.15	38.44	36.61	12.54	67.38
Projected EPS(Current EPS * (1 + Growth in equity)	134.1388	40.85652	38.30938	13.40801	70.55935
Intrinsic Value(Projected EPS * Normalized Avg. P Ratio)	3362.859	912.7347	725.1965	168.5387	2357.388
Market Value (As on May 2019	2240	1564.95	653.8	133.15	2454
Remark	**Buy**	**Sell**	**Buy**	**Buy**	**Sell**

7. DECISION

TCS: Intrinsic Value > Market Value, it is undervalued, so it is recommended to **buy** the stock as value of share may increase in future.

L & T: Intrinsic Value < Market Value, it is overvalued, so it is recommended to **sell** the stock as value of share may Fall in future.

Mahindra & Mahindra: Intrinsic Value > Market Value, it is undervalued, so it is recommended to **buy** the stock as value of share may increase in future.

NTPC: Intrinsic Value > Market Value, it is undervalued, so it is recommended to **buy** the stock as value of share may increase in future.

HDFC BANK: Intrinsic Value < Market Value, it is overvalued, so it is recommended to **Sell** the stock as value of share may decrease in future.

8. FINDINGS

With respect to EPS of the companies, the EPS of HDFC Bank has shown a constant increase every year whereas L & T, Mahindra & Mahindra, NTPC are showing increasing trend initially and then falls down. On the other hand TCS is showing increasing trend throughout the five years. In case of Dividend Payout ratio, Mahindra & L & T are showing increasing trend in opening three years and gradually decreased in next two years. TCS showed decreasing trend whereas HDFC bank is having fluctuating price earnings ratio, but NTPC is having an increasing pattern. TCS is showing decreasing trend in case of Return on equity. HDFC & L & T is having considerable line of consistency during last five years. Mahindra & Mahindra NTPC is showing decreasing trend in initial three years and increasing trend in last two years. TCS & L & T is showing fluctuating trend for price/BV ratio for 5 years, decreasing trend for Mahindra & Mahindra & nearly constant trend for NTPC & HDFC Bank. Earning yield is maintaining a consistency in each year for TCS. HDFC Bank & NTPC initially showed an increase in the Earning yield and decreased in last two years. L & T & Mahindra & Mahindra showed fluctuating trend throughout the year.

9. CONCLUSIONS

It can be concluded that Service sector & Banking sector companies are one most promising platform of investment in capital market and in turns give considerable return for the risk taken by investors. On the basis of share valuation: TCS, Mahindra & Mahindra and NTPC is undervalued as its intrinsic value is higher than its market value and suggested to buy the share since the price of the same may increase in future. In contrast, L & T and HDFC Bank Ltd. are overvalued as their market value is higher and preferred to sell the share as the share price may fall. In near future it is expected that number of investors will be flooding into the capital market that increases the relevance of fundamental Analysis of various sectors.

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