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THE IMCOME METHOD OF THE VALUATION OF COMPANY CAPITAL

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Abstract. This article describes the scientific and theoretical aspects of using the income method in determining the capital value of a company. It also reveals the possibilities of using the income method in estimating the value of capital. In addition, the focus is on the use of this method in determining the market value of a company's capital.

Keywords: Income method, dividend, discount rate, EBIT, FCF, enterprise value

These days, The International Committee for Valuation Standards identifies three approaches for evaluating any asset: a direct market comparison approach, an income approach and a cost approach. There are valuation methods in each approach including some methods. The income approach is based on two methods: the capitalization method and the discounted cash flow method. The comparative approach consists of three methods: the capital market method, the transaction method and the sectorial coefficient method. The cost approach is based on two methods: the net assets method and the residual value method.

Income approach - a set of methods for assessing the value of the appraised object, based on the determination of the expected income from the use of the appraised object. In the income approach, the value of the company is determined based on expected future earnings and bringing them by discounting to the present value that the assessed company can bring.

Marjorie Grice-Hutchinson who was the representative of the Salamanca school first developed the present value theory[1]. This is one of the key principles of modern financial theory. The discounted dividend model is fundamental to the discounted cash flow model. John Williams first proposed the discounted dividend model after the US crisis in the 1930s[2].

The formula for the discounted dividend model is as follows:

$$\boldsymbol{PRICE} = \sum_{t=1}^{n} Div * \frac{(1+g)^t}{(1+R)^t} \qquad (1)$$

Where,
Price - share price
Div - dividends
R - discount rate
g - growth rate of dividends.

However, now, dividend payments are very rarely used to measure the fair value of share capital. Why? Because if you use dividend payments to estimate the fair value of share capital, then almost all shares in the stock markets around the world will seem overvalued to you for very simple reasons:

- Dividend payments are very low and virtually dividend yield rarely exceeds 3% per year.
- Some companies do not pay dividends at all. For example, Apple does not pay dividends, but its market cap is $ 372 billion in 2018 year.

Thus, the DDM is more used today to assess the fundamental value of a company's preferred stock.

Stephen Ryan, Robert Hertz and others in their article say that the DCF model has become the most widespread, as it has a direct connection with the theory of Modigliani and Miller, since free cash flow is a cash flow that is available to all holders of the company's capital as holders debts and shareholders[3]. Thus, using DCF, both the company and the share capital can be valued.

The formula of the DCF model is identical to formula (1); the only thing is that instead of dividends, free cash flow is used. This formula is as follows:

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[1] Marjorie Grice-Hutchinson, the School of Salamanca Reading in Spanish Monetary Theory 1544-1605. Oxford University Press, 1952.

2 John Burr Williams, the Theory of Investment Value. Harvard University Press 1938; 1997 reprint, Fraser Publishing.

[3] Stephen G. Ryan, Chair; Robert H. Herz; Teresa E. Iannaconi; Laureen A. Maines; Krishna Palepu; Katherine Schipper; Catherine M. Schrand; Douglas J. Skinner; Linda Vincent, American Accounting Association's Financial Accounting Standards Committee Response to FASB Request to Comment on Goodwill Impairment Testing using the Residual Income Valuation Model. The Financial Accounting Standards Committee of the American Accounting Association, 2000.

$$Value = \sum_{t=1}^{n} FCF * \frac{(1+g)^t}{(1+R)^t} \qquad (2)$$

Where,

FCF- Free Cash Flow.

Since we have moved on to the DCF model, let us take a closer look at the concept of cash flow. In our opinion, A. Damodaran shows the most classification of cash flows for assessment purposes[1]. Damodaran identifies two types of free cash flows that need to be discounted to determine the value of the company:

- Cash flow for a firm (company) (FCFF - free cash flow to firm) is a cash flow that is available to all holders of invested capital.
- Cash flow to equity (FCFE - free cash flow to equity) is the cash flow available to the company's shareholders.

In order to move forward, we already need to show the difference in company value and shareholder value. The company operates at the expense of invested capital, and the invested capital may include both equity capital and different proportions of equity and borrowed capital. The formula for the free cash flow to firm model is as follows:

$$FCFF=EBIT*(1-T)+DA-\Delta WCR-Investments \qquad (2)$$

Where,

EBIT-Earnings before Interest and Taxes;

T-income tax rate;

DA – depreciation;

ΔWCR – changes in required working capital.

Sometimes in the literature you can find another formula for FCFF, for example, James English uses formula (3), which is identical to formula (2).

$$FCFF=CFO*Interest\ expense*(1-T)-CFI \qquad (3)$$

Where,

CFO- cash provided by operating activities;

T-income tax rate;

CFI- cash provided by investing activities.

$$FCFF=Net\ income+DA-\Delta WCR-Net\ borrowing \qquad (4)$$

Where,

DA – depreciation;

ΔWCR – changes in required working capital.

Net borrowing – this is the difference between received and repaid loans / borrowings.

Formula 5 shows how you can get the value of share capital from the value of the company.

$$Equity\ value=EV-(Debt-Cash) \qquad (5)$$

It turns out that there are two types of valuation based on DCF cash flows depending on cash flows. In formula (6), the model for assessing the company taking into account debts, and in formula (7), the model for assessing equity capital. To estimate the fundamental value of a company or equity capital, one can use both formula (6) and formula (7) together with formula (5).

$$\text{Enterprise value} = \frac{FCFF_1}{(1+R)^1} + \frac{FCFF_2}{(1+R)^2} + \cdots \frac{FCFF_n}{(1+R)^n} \qquad (6)$$

$$\text{Enterprise value} = \frac{FCFE_1}{(1+R)^1} + \frac{FCFE_2}{(1+R)^2} + \cdots \frac{FCFE_n}{(1+R)^n} \qquad (7)$$

In conclusion, it may be appropriate to perform a valuation using the income method in valuing a company’s capital. Because this method allows you too accurately, assess the value of capital, and serves to determine the value of debt and private capital in the capital structure.

[1] Асват Дамодаран, Инвестиционная оценка. Инструменты и методы оценки любых активов. Альпина Паблишер, 2010 г.

USE OF BENCHMARKING IN RETAIL TRADE

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Abstract: The article reveals the idea of the content of benchmarking as a marketing tool for interaction and its weak use, high practical significance and insufficient elaboration of the issues of methodological support of the competitiveness of retail enterprises at the present stage of development.
Keywords: Benchmarking, business, retail trade, competitiveness.

At present, the risk and uncertainty of the activities of trade organizations has significantly increased. There is an increase in competition between retailers, both among themselves and with foreign retail chains entering the market. The situation is complicated by the fact that the assortment of goods of many trade organizations does not differ much.

The trade business largely determines how desirable and competitive a product will be, the level of sales of which depends on the correctly selected market segment, assortment, price and communication policy, as well as on the quality of basic and additional services.

Thus, the marketing mechanism of trade enterprises faces the problem of finding effective methods of competitive struggle and forms of adequate response to external threats.

Competition for many retailers today is global in nature and, not accidentally, the main goal of most of them - achieving world quality standards. Benchmarking is one of best methods for this. This modern marketing technology, based on the experience of companies - market leaders, can be applied by retailers to improve their competitiveness.

In modern conditions, the use of benchmarking in retail trade becomes relevant in connection with the search for enterprises directions of increasing competitiveness. Regional retailers rarely benchmark due to the insufficient widespread use of this concept. However, in partici pate in anon-profit information exchange and use certain methods of access to knowledge. Some elements of the use of benchmarking are present in all retailers, but it is used haphazardly.

Enterprises are implicitly interested in learning experiences, which they practically do not consider as their advantage and do not appreciate the possibility of its implementation.

In marketing, there are several options for the benchmarking process. Benchmarking scheme proposed in the literature mostly general and not brought to the level its practical application in retail trade, since it was developed for industrial enterprises. Individual processes developed benchmarking at Motorola, Digital, Xerox. For benchmarking in the regional retail sector is necessary develop a model for organizing the benchmarking process in the enterprise retailers adapted to the existing level of its development.

To the main provisions of the organization of a benchmarking project regional retailer must include: planning the organization of the benchmarking process and characterization object; identification, collection and analysis of information about objects benchmarking; designing the future level of object measurements comparisons; implementation of the set goals. The benchmarking project has practical value for the top management of a trading enterprise, functional and line managers of large, medium and small retailers both domestically and international markets.

Modeling the competitive position of a regional enterprise retailers improve the scientific and efficient process formation of a competitive strategy of a retail enterprise, orients the culture of the enterprise towards values such as striving staff to train, enhance their own potential and achievements. The main goal of modeling is to predict behavior retailers in planning their competitiveness. Implementation of a marketing strategy for the formation of the competitiveness of a regional retail trade enterprise involves structuring the quality function. All of this must appear the impetus for the development process of the retailer itself and creating the prerequisites for innovative impulses for the development of new strategies and working methods.

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3.Knyazev E.A., Evdokimova Ya.Sh. Benchmarking for universities: Study guide. - M .: University book, Logos, 2006. - 208c.