# Introduction to Finance

Lecture 2

# Company Types- Indian structure

| Types of Company | Number od Directors | | Capital | | No. of Shareholders (SHs) | |
|---|---|---|---|---|---|---|
| | Min | Max | Min | Max | Min | Max |
| Public Ltd | 3 | 15 | 5 lakh | No limit | 7 | No limit |
| Private Ltd | 2 | 15 | 1 Lakh | No limit | 2 | 200 |
| One person company | 1 | 15 | 1 lakh | 200 Lakh | 1 | 1 |

# Stages of formation of a company

1) Promotion

   Nature of business, objectives, capital, scale etc

2) Incorporation

   Registration , Documents , Incorporation certificatie

3)Commencement of Business

# Promoters

- A promoter can be an individual, partner, a company , or an association
- Promoters decide:
    - bring the idea for the business, nature and its objectives
    - Amount of capital needed
    - Scale of business
- Promoter will undertake all necessary process of incorporating the company
    - complete legal procedures
    - Prepare various documents on legal status, rules and regulation ( Memorandum of Association (MoA) and Articles of Association (AoA))
- Approach investors for collecting capital for the company
    - objective, level, prospective of the company to convince investors
- Promoters often nominate themselves as first director of the company and are 1$^{st}$ subscribers to MoA and AoA
- Can enter into contracts with 3$^{rd}$ parties on behalf of the proposed company
- Promoter have fiduciary duties towards the company- i.e cannot make decisions to make own profit or  act with self interest agendas

# Capital- debt v/s equity

- Capital decision- debt v/s equity
- General rule – mix of both – eg: 40% debt and 60% equity
- If you are a debenture/bond holder- lend money to the company (creditor)- you will receive interest and loan amount upon maturity of debentures/bonds – low risk for creditors- in case of loss still recieve interest and debt amount-
- If you are an equity share holder- co-ownership (investor) - which implies right to the profit –however high risk as they cannot claim anything if there is loss

# Equity capital

- A company decided to raise funds through equity capital  for incorporation.
- Capital needed = 10 crores (get permission from SEBI and Registrar of Companies (RoC))= Authorised capital
- Paid-up capital= capital received from public (Paid-up capital is a part of Authorised capital)= eg: Share issued (IPO)  is for 6 crores out of 10 crore permitted authorized capital

# Number of shares and Face value

- Equity capital required

- Face value = The assigned value of share by the company during its issue
- If FV is 1000 per share , the to collect 6 crores company need to issue 60000 shares
- If FV= 100, then no.of shares= 6 lakh
- If FV=1 , no of shares= 6 crores

# Share market

- Primary market  and Secondary market
- Primary market- (IPO)- Initial transaction between the corporation and investors
- Firms occassionly only issue shares
- Secondary Market:
- - shares traded without the involvement of corporation
- - However, sharemarket value is important for the company as it reflects the market assessed value/worth of the company- hence attract investors and creditors based on this value
- Share price is different from issue price or face value. It is determined by the demand and supply of shares

# Share market

- Indian share markets ?

# Share market

- Indian share markets – National Stock Exchange (NSE), Bombay Stock Exchange (BSE)
- what are Nifty50 and Sensex?
- \- market index of mega-cap stocks listed companies in each stock exchange
- NYSE and Nasdaq – US stock markets

# Equity capital

- Equity capital= FV * number of shares outstanding
- Shares outstanding implies shares issued
- Equity capital= 100* 6 lakh= 6 crores
- Market value= Market share price * Number of shares outstanding
- MV= 150 * 6 lakh = 9 crores
- MV= also known as market cap
- Market value of equity is known as market capitalization or market cap
- Market cap implies the valuation of the company by the investors (also based on its future perspective)
- Premium= MV-FV=50

# Financial statements

- Assessment of financial performance of the company=creditors and investors
- Balance sheet; Profit and Loss statement, Cash Flow statement etc

## GLOBAL CONGLOMERATE CORPORATION

### Consolidated Balance Sheet
### Year Ended December 31 (in $ million)

| Assets | 2022 | 2021 |
|---|---|---|
| **Current Assets** | | |
| Cash | 21.2 | 19.5 |
| Accounts receivable | 18.5 | 13.2 |
| Inventories | 15.3 | 14.3 |
| Other current assets | 2.0 | 1.0 |
| Total current assets | 57.0 | 48.0 |
| **Long-Term Assets** | | |
| Land | 22.2 | 20.7 |
| Buildings | 36.5 | 30.5 |
| Equipment | 39.7 | 33.2 |
| Less accumulated depreciation | (18.7) | (17.5) |
| Net property, plant, and equipment | 79.7 | 66.9 |
| Goodwill and intangible assets | 20.0 | 20.0 |
| Other long-term assets | 21.0 | 14.0 |
| Total long-term assets | 120.7 | 100.9 |
| **Total Assets** | **177.7** | **148.9** |

| Liabilities and Stockholders' Equity | 2022 | 2021 |
|---|---|---|
| **Current Liabilities** | | |
| Accounts payable | 29.2 | 24.5 |
| Notes payable/short-term debt | 3.5 | 3.2 |
| Current maturities of long-term debt | 13.3 | 12.3 |
| Other current liabilities | 2.0 | 4.0 |
| Total current liabilities | 48.0 | 44.0 |
| **Long-Term Liabilities** | | |
| Long-term debt | 99.9 | 76.3 |
| Lease obligations | — | — |
| Total debt | 99.9 | 76.3 |
| Deferred taxes | 7.6 | 7.4 |
| Other long-term liabilities | — | — |
| Total long-term liabilities | 107.5 | 83.7 |
| **Total Liabilities** | **155.5** | **127.7** |
| **Stockholders' Equity** | **22.2** | **21.2** |
| **Total Liabilities and Stockholders' Equity** | **177.7** | **148.9** |

# Price to book ratio (P/B ratio)

- PB ratio= Market to book ratio= Market value of equity/Bool value of equity
- Book value = Tangible assets-Liability
- Book value per share = Book value/no.of outstanding shares
- MV= Perception of market regarding the companies net worth
- PB ratio implies how many times of BV is the MV
- It signals whether the stock is overpriced or underpriced