Part (c)	**Evaluate and comment on the PE valuation performed by the financial manager in determining the value of UBA.** **Do not re-perform the calculations or the PE valuation.**	**Marks**
1	The **perspective of the valuation** should be considered, either performed on UBA only, because the purpose of the valuation was to determine whether the purchase price offered to the former shareholders reflected the value of their shareholding, or to determine whether the valuation is reasonable considering the potential synergies, or from the sellers perspective.	1
2	**Synergies** should not be included if calculating a minimum value to be accepted by shareholders of the selling company. However, if shareholders in the target are aware of the synergies, they may insist on a share of the synergy being allocated to them, therefore include. The valuation should include only earnings in the form of **maintainable income/expenses** in the profit figure.	1 1
3	In determining the value of the shares from the viewpoint of the former shareholders, an **adjustment for control** should be taken into account, as the PE valuation is a minority valuation. There is **no indication** of how the synergistic earnings or the premium for **control were determined**. This needs to be justified.	1 1
4	The **PE ratio of Oneity** should not have been used as the nature of business is different to that of UBA. The **PE ratio of a similar listed** company should have been used, **adjusted for specific risks** and the fact that UBA's shares have limited transferability and marketability.	1 1 1
5	**Synergies have been double counted**. First by including "After tax synergies expected" on the maintainable income, and then by adding the **control premium at the end**. This should only be included once.	1 1
6	The profit on the sale of the asset (warehouse), which is a **non-recurring item**, should have been deducted from the earnings figure (after tax), (and/or Patent R1.9m).	1
7	The annual **rental of the warehouse** should be added back as this will not be incurred in the future. A present value calculation of the **remaining one year's** payments (2019) may be considered.	1 1
8	The **contingent liability** should be considered as an adjustment to the calculated value as a reduction.	1
9	The value of the **shareholder loan should not be deducted** from the value in the end. The loan is regarded as long term as it has no specific date of repayment. If the **interest is already included** in the earnings (which it should be), then the loan has already been accounted for, and deducting it again would be double counting. The loan can be considered to be **quasi equity** due to its terms.	1 1 1
10	The **interest on the shareholder loan** should also not be added back to the earnings figure. It is **part of the earnings figure** to be multiplied with the PE ratio (adjustments could have been made to the PE ratio for a difference in capital structure).	1
11	The **EBITDA multiple** could have been considered as UBA is not a capital-intensive business. Using EBITDA would also avoid comparables having a **different asset intensity, different capital structure**, or different depreciation/amortisation rates and policies from the valuation target.	1 1
12	The PE valuation is still used widely as a **sanity check**, quick and easy to do. The PE ratio is less reliable as it is based on accounting earnings, and therefore **use should be cautioned**. Criticism of the PE ratio as being **empirically disproved**, where low PE outperform, and high PE underperform.	1 1 1
	Available	**24**
	Maximum	**11**
	Communication skills – appropriate style	**1**
	Total for part (c)	**12**

Part (d) Use the free cash flow valuation to estimate the equity value of UBA as at the end of FY2018 as if the acquisition of Oneity had not taken place. Provide the key assumptions you used in performing your valuation.				Marks
Free cash flows				
	FY2019 R'000	**FY2020 R'000**	**FY2021 R'000**	
Net movement in cash	11 729	(6 669)	4 543	
Adjustments				
Interest income on surplus cash	(1 225)	(315)	(315)	1
Finance cost	1 655	1 655	1 655	1
Lease income (valued separately)	(785)	(855)	(932)	1
Taxation - interest and investment income	99	(136)	(114)	2C
Distribution to shareholders	1 413	0	1 625	1
Proceed from sale of fixed asset *(not added back as it is part of normal operating activities)*	0	0	0	1
Movement in surplus cash	(7 500)	13 000	0	2C

FY2018 R'000	FY2019 R'000	FY2020 R'000	FY2021 R'000
700	1 225	315	315
10 000	17500	4 500	4 500

	FY2019 R'000	FY2020 R'000	FY2021 R'000	Marks
Free cash flows	5 386	6 680	6 462	1C
*The free cash flows should be that of UBA only without any synergies as a **minimum value** has to be determined.*				1
***No adjustments should be made for the depreciation and profit on the sale** of the fixed asset or the sponsorship fee (note 4.1), as these amounts were included in EBIT (the depreciation and profit on the sale of the fixed asset would already have been removed to calculate the cash flows supplied).*				1
Continuing value				
((6 462 + 2 000) x 1,05) / (0,1293 - 0,05) (Or forecast further year) 1 For including terminal value, 1 for growing amount (5 or 7% as this is penalized next), 1 for adding R2,000 once off or additional year, 1 for WACC.			112 044	3C
Use growth rate of 5% as this is the growth pertaining to UBA				1
Inclusion of **lease income**, assuming that the lease with Oneity is renewed or that building will now be leased to another party as UBA has always leased out the building *Alternatively,* still not part of normal operations, and should therefore still be valued separately				1

Valuation		
	R'000	
PV of free cash flows for 2019 to 2021 at 12,93%	14 494	1C
Use WACC of UBA		
PV of continuing value at WACC	77 797	1C
Less: Market value of debt	(15 000)	1
Add: Surplus cash	10 000	1
Add: Investment property	6 550	1
Value of 100% of equity	93 841	
	Available	**22**
	Maximum	**21**
	Communication skills – appropriate style	*1*
	Total for part (d)	**22**
TOTAL FOR PART II		**34**