

THE ANALYSIS OF THE RESULT PER SHARE– MEASUREMENT INDICATOR FOR THE PERFORMANCES OF THE ENTERPRISE

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The result per share is one of the indicators most often used in the financial analyses drawn up for the financial record of the enterprises, mainly the Anglo-Saxon ones, which can operate as a basis for comparison of the financial performance for the enterprises listed, which run their activity within the same sector and it can be a useful complementary indicator in following the prospective profits in the field. This indicator does not provide though the possibility to compare all the enterprises which compute it due to the difficulties in interpreting the differences noticed from one enterprise to another, differences which can result from the different number of shares issued by each of them and from the different categories of shares issued. The paper has in view the description and exemplification of the computing model of the Result per share indicator.

Key words: indicators, result on action, performance.

The enterprises quoted on the Stock Exchange and due to be quoted, when presenting their financial activity, they use among the financial indicators the Result per share, too, an indicator providing the investors information regarding the profit obtained on the investment made and which is computed according to The International Accounting Standard IAS 33.

Result per share = Net profit of the financial year / Number of shares issued

An enterprise can issue two types of shares: ordinary shares and preferential shares, both being issued and sold in order to attract capital, yet those who invest in the preferential shares have institutional objectives different from those investing in ordinary shares.

- **Ordinary shares** are capital instruments which give the right to participate to the profit (dividends) only after the distribution of the net profit afferent to the other types of shares (preferential) Due to the fact that usually only the ordinary shares grant the right to vote, they represent a modality to control the enterprise.
- **Preferential shares** have priority before the ordinary shares in many regards: priority when dividends are paid, priority when the assets of the enterprise are distributed in case of winding up, convertibility and option of revocation (pay off). The priority of the preferential shares as compared to the ordinary shares regarding the dividends payment can be explained as it follows: the holders of the preferential shares must cash in a certain amount as dividends before allocating the dividends to the ordinary shareholders. This amount is set up in monetary units on share or as a percentage of the nominal value of the preferential shares.

According to IAS 33, the performance indicator “Result on action” is computed in two ways, that is: the result per basic share and the result per share– diluted.

The result per basic share (R/A-basis)

For the fundamental computation of the profit per share one usually starts from the net profit or loss of the period, computed according to Standard IAS 8 « The net profit or loss of the period », from which the preferential dividends are deducted. If the result of the period is a loss, the preferential dividends engaged are added to the loss before the computation of the profit per share.

The result per basic share (**R/A-basis**) is computed by reporting the net profit of the financial year, according to the ordinary shares (PnAC), to the weight average of the circulating ordinary shares in that particular financial year (MpACc) :

$$R/A\text{-basis} = PnAC / MpAC$$

The net profit of the financial year corresponding to the ordinary shares (PnAC) is determined by deducting from the net result of the financial year (RnEx) the value of the preferential dividends afferent to the financial year (Dpref):

$$PnAC = RnEx - Dpref$$

The value of the preferential dividends contains: the dividends afferent to the non-cumulative preferential shares declared in that particular financial year, the dividends owed in that financial year, afferent to the cumulative preferential shares, no matter if these dividends have been declared or not.

The value of the preferential dividends afferent to the financial year does not include the value of the dividends afferent to the cumulative preferential shares, paid or declared in the current financial year for the previous financial years.

The weight average of the circulating ordinary shares in that particular financial year (MpACc) is determined as follows:

$$MpACc = (Si + AE - AR) \times FP$$

Where:

- Si = number of circulating ordinary shares at the beginning of the financial year
- AE = number of shares issued
- AR = number of paid off shares
- FP = ponderation factor: $FP = NZc / NZt$
- NZc = number of days when the shares circulated
- NZt = total number of days of the period

The moment of the inclusion of the ordinary shares in the computation of the weight average is determined by the specific clauses and conditions, associated to their issue, this being usually the date of their issue. The ordinary shares which are issued only when complying to certain conditions, called *contingent shares*, are considered circulating and are included in the computation of the result per share – basis from the date all the necessary conditions are complied with.

The weight average of the circulating shares is adjusted in case of some events (others than the conversion of the potential ordinary shares) which have changed the number of the circulating ordinary shares, without determining an appropriate change in the size of resources. Such events are: a capitalization or an issue of free shares; a diminishing of the nominal value of the shares; an annulment of the diminishing of the nominal value of the shares; facilities in the case of the issue of subscription rights. The adjustment is made both for the weight average of the particular financial year as well as for the weight averages computed for all the periods presented in the financial statements.

Result per share – diluted (R/A-diluted)

When the enterprise has a complex structure of the capital, there occurs the necessity to reflect it in the financial statements, along the information regarding the result per share – basis and the information regarding the result per share – diluted.

The result per share diluted is computed to provide the users of the financial statements an indication regarding the way in which the profit per share would evolve if certain plans to attract the capital or to make the employees loyal based on the potential issue of the ordinary shares materialised in the reporting period.

In order to compute the result per share diluted, the net profit assigned to the ordinary shares (**PnAC**) and the weight average of the circulating shares in a certain period must be adjusted for the diluting effect of all the *potential ordinary shares: debentures and preferential shares convertible into ordinary shares, warranties and options, plans for the employees* which allow them to receive ordinary shares as part of their remuneration, shares which are issued only after the compliance with certain conditions resulting from the contracting clauses.

It is adjusted with the influences of all the *potential ordinary shares* considered *diluting*. The potential ordinary shares are considered *diluting* when their conversion into ordinary shares leads to the lowering of the value of the net result per share indicator. Otherwise, when the conversion of the potential ordinary

shares has the effect the increasing of the value of the result per share indicator, these are considered *anti-diluting* shares and are not taken into consideration for adjustment. The value of the net profit or of the net loss afferent to the financial year, corresponding to the ordinary shares is adjusted by the influence of taxation, too determined by the conversion of the diluting potential ordinary shares.

Relation of calculus:

$$R/A\text{-diluted} = (PnAC + Dob + DivEn)_{\pm} / (MpACc + MpACs)$$

To compute the result per share-diluted, the net profit corresponding to the ordinary shares will be majored with the net interests:

- **Dob - Interest** – the gross value corrected with the tax on profit afferent to the potential ordinary shares (such as, for example, the shares convertible into ordinary shares)
- **Div** – the dividends to be due on the preferential shares
- Adjusted with \pm :
- **En** = other net elements (revenues or expenditure consisting in fees, discounts, bonuses etc.) which would have not affected the result of the financial year afferent to the ordinary shares if potential ordinary shares had not been issued, thus establishing the *diluted result*.

The weight average of the circulating ordinary shares will be majored with the weight average of the supplementary ordinary shares which would result from the conversion of all the potential ordinary shares.

We state that the potential ordinary shares which have been transformed into ordinary shares during the financial year are taken into consideration for the result per share – diluted from the beginning of the financial year to the date of conversion. It is obvious that, from this date on to the end of the financial year, the shares obtained through conversion being ordinary shares are taken into consideration both for the result per share – basic indicator as well as for the result per share – diluted indicator.

Example of computation of the result per share – basic and of the result per share – diluted

To demonstrate the way to compute the two indicators the following example is provided:

In the financial year N-1 two issues of convertible debentures have been made, that is:

- 3,000 convertible debentures, nominal value 100 lei/title, interest rate, 2%, each debenture can be converted into an ordinary share (1/1);
- 2,000 convertible debentures, nominal value 150 lei/title, interest rate 1%, each debenture can be converted into to ordinary shares (2/1).

In the financial year N-1 there were in circulation: 50,000 convertible debentures issued in the *financial year N-2* in the following conditions: the nominal value 120 lei/title, interest rate 1%, 100 debentures can be converted into 120 ordinary shares. (120/100)

At the beginning of the financial year N the company “X” has:

- 350,000 circulating shares out of which: 10,000 preferential shares. The dividend on the referential share was set up at 2 lei/title.
- Each preferential share (10,000) is convertible into 1.5 ordinary shares (1.5/1).

During the financial year N the following operations take place:

- on 10 April the company issued: 100,000 new ordinary shares.
- on 20 June the conversion was made into ordinary shares of 40,000 convertible debentures which have been issued in the financial year N-2. As a result, the company issued 48,000 new ordinary shares (40,000 x 120/100).
- on 30 October the company paid off 88,000 circulating ordinary shares.

The net result of the financial year N is of 950,000 lei, the tax quota per profit 16%.

The company declared 150,000 lei the dividends for the financial year N, out of which 20,000 lei for the preferential shares.

a) Determining the result per share – basic:

Computation of the net profit afferent to the ordinary shares (PnAC):

Net profit of the financial year 950,000 lei

- Dividends afferent to preferential shares - 20,000 lei

Net profit afferent to ordinary shares (PnAC) = 930,000 lei

Computation of the weight average of circulating ordinary shares (MpACc):

Date	Circulating period	Explanations	Shares issued	Shares paid off	Circulating shares	Ponderation factor FP
01.01.N	01.01-10.04	Si (360.000 –10.000)	340,000		340,000	100/365
10.04.N	11.04-20.06	Share issue	100,000		440,000	71/365
20.06.N	21.06-30.10	Debenture conversion	48,000		488,000	132/365
30.10.N	31.10-31.12	Own share pay off		88,000	400,000	62/365
31.12.N		Total / Final balance	488,000	88,000	400,000	

MpACc = (340,000 x 100/365) + (440,000 x 71/365) + (488,000 x 132/365) + (400,000 x 62/365) = 93,151+ 85,589 + 176,482 + 67,945 = **423,167 shares**

Result per share basic:

R/A-basic = R/A-basic = PnAC / MpACc = 930,000 lei / 423,167 shares = 2.20 lei/share

b) Determining the result per share – diluted:

Computation of diluted result:

Net profit afferent to ordinary shares (PnAC)	930,000 lei
Dob Interest afferent to convertible debentures, total	+ 43,356 lei
out of which: 3,000 titles x 100 lei / title x 2%	6,000 lei
2,000 titles x 150 lei / title x 1%	3,000 lei
40,000 titles x 120 lei / title x 1% x <u>170/365</u>	22,356 lei
10,000 titles x 120 lei / title x 1%	12,000 lei
En : Afferent tax on profit (43,356 x 16%)	- 6,937 lei
Dividends afferent to preferential shares (10,000 x 2)	+ 20,000 lei
Diluted result (PnAC+Dob+Div+En)	986,419 lei

Computation of weight average of circulating and supplementary ordinary shares:

Explanations	Number of ordinary shares
MpACc	423,167
Convertible debentures	3,000 x 1 / 1 = 3,000
Convertible debentures	2,000 x 2 / 1 = 4,000
Convertible debentures, up to 20,06.N	(40,000 x 120 / 100) x 170 / 365 = 22,356
Convertible debentures	10,000 x 120 / 100 = 12,000
Preferential shares	10,000 x 1.5 / 1 = 15,000
Total (MpACc + MpACs)	479,523

Result per share diluted:

$$\begin{aligned} \text{R/A-diluted} &= (\text{PnAC} + \text{Dob} + \text{Diy} \pm \text{En}) / (\text{MpACc} + \text{MpACs}) \\ &= 986,419 \text{ lei} / 479,523 \text{ titles} = 2.06 \text{ lei/title} \end{aligned}$$

Conclusions

The stock exchange rate of the share represents the barometer of the global performance of an enterprise, officially recognised by the public on the capital market. But the variation of the stock exchange price is determined not only by the evolution of the economic – financial results of the enterprise, but also by the investors' expectations referring to its development possibilities, the evolution and the perspectives of the sector where the firm runs its activity, as well as the national and international economic tendencies. The most important factor setting up the price of a share is the ratio between the supply and demand on the capital market.

It has been noted that some stock exchange indices, regarding the level of action, have strongly influenced the stock exchange rate. This fact demonstrates the reduced relevance of the traditional financial rates when adopting the decisions to invest-disinvest as a result of the low quality of the financial-accounting information, the issuers' lack of transparency, the delay in providing information to the investors or simply, the existence of other strong motivations to purchase some apparently unprofitable firms by important investors.

The stock exchange indices had in view, listed at the Bucharest Stock Exchange are the following:

- PER = rate stock exchange price / to profit per share (it would represent how many years you have to wait to cover the price paid for a share from the afferent profit)
- P / BV = rate stock exchange price / accounting value per share (it shows what price the investors set for the company's assets)
- DIV = (dividend / price) x 100 - the output of dividends (it shows what percentage of the price of a share the dividend that it brings represents and it is always compared to the term interests)
- P/S = rate stock exchange price / sales per share
- Stock exchange capitalization (it is the market value of a quoted company and it is obtained by multiplying the total number of shares issued with the stock exchange price of a share)
- EPS = net profit per share

The result per share, computed in the financial statements, arranged or not, can influence the exchange rate of the shares quoted on the Stock Exchange, but many times either they are more important in the investors' choice for the company's policy, the quality of the management, the company's assets, the policy of debts, cash, commercial fund, dividend policy, the quality of the shareholders, the development policy etc.

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