

CORPORATE VALUE ESTIMATION OF PT SRI REJEKI ISMAN TBK

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Abstract. Indonesia has the second largest export market share among Southeast Asia Region on textile exports which is 28.5% or 4.6 billion US dollar and 18.3% or 7.7 billion US dollar on garment exports. One of the biggest textile and garment factories is PT Sri Rejeki Isman Tbk. PT Sri Rejeki Isman Tbk had strategy to expand its business in the following year. The strategies will drive greater sales with the consequences that expenses go up as well. The Company needs to do corporate valuation due to know the company share price so the company can choose the appropriate strategy to expand the business. The valuation methods used in this research are Asset based method, Market approach, and Discounted Cash Flow valuation. The outcome of this research is that the share price of PT Sri Rejeki Isman Tbk is undervalued based on valuation method. The assets-based approach showed the book value price per share is US\$ 0.0158 (IDR 195.99). Market based approach showed the book value price per share is US\$ 0.0131 (IDR 162.91). Comparing to the current market value price per share at the end of 2014, which is IDR 163, the stock performance is undervalue. And also based on Discounted Cash Flow method, the market price is undervalued. PT Sri Rejeki Isman Tbk, should increase the free cash flow and decreasing the cost of capital. PT Sritex should increasing the operating income and/or decreasing change in net working capital and net capital expenditure.

Keywords: valuation, company valuation, textile, garment, share price, discounted cash flow, asset based approach, market approach

Introduction

Southeast Asia is the third world's largest textile exporter and the second largest garment exporter region. It is respectively responsible for 5.2% and 8.8% of all exports in textiles and garments in 2013. According to WTO (World Trade Organization) data, textile and garment exports from Southeast Asia have been increased significantly since 2009 because the demand from developed countries has increasing the CAGR (compound aggregate growth rate) of textiles by 11.7% and garment by 11.8% between 2009 and 2013.

The textile and garment industry is still an important sector of the Indonesia economy, especially since it is capable of employing around 1.54 million workers, and since it contributed USD 4.2 billion to the 2013 trade balance according to the Indonesia Textile Association (API). One of the biggest textile factories is PT Sri Rejeki Isman Tbk. PT Sri Rejeki Isman Tbk also known as PT Sritex is one of main player of the textile and garment sector in Indonesia. PT Sritex is one of the most vertically integrated and largest textile producers in the Southeast Asia with a significant competitive advantage. PT Sri Rejeki Isman Tbk. (Sritex) has managed to obtain fresh funds of IDR 1.344 trillion from the IPO (initial public offering) on 10-12 June 2013. Sritex has managed to sell 5.6 billion shares at a price of IDR 240.

In the current year (2015), PT Sritex has some strategies that they will execute, such as to continue the capital expenditure program, and including its financing program which was launched in 2014 and expected to end in 2016; to continue the following strategies executed in 2014 in gradually

expanding production capacity, making production more efficient, diversifying products, and expanding the customer network; to increase the Company's income using higher level of gross profit margin resulting from expansion programs, so that the Company will be more competitive internationally and yield higher profits; to perform cost savings measures across all production lines for such expenses as electricity or maintenance. The Company will also implement financial cost-savings measure and to improve communications and information disclosure relating to Good Corporate Governance.

The combination of those strategies drives greater sales and profits –with the consequences that expenses go up as well. The Company needs to do corporate valuation due to find the worth of assets of the Company. The process of corporate valuation will determine a value that essentially influenced by some factors such as inflation, interest rates, growth in gross domestic product, corporate profits or business risk that already or will happen. By doing valuation, company can know the company share price compared with its market, company cash flow, and asset.

Literature Review

Valuation is the process of measuring the value of asset. Determine the value of asset is useful for stakeholders, such as to enhance the corporate value, choose investments, decide the price to pay or receive takeover, choose the appropriate capital structure, portfolio management, in acquisition analysis, and in corporate finance. The valuation can be estimated the worth of economic or monetary assets value. There are three approaches to estimate corporate value according to James R. Hitchner, *Financial Valuation* (2006), those are the income approach, the market approach, and the asset approach.

Jimmy Torrez (2006) on *Corporate Valuation* said that valuation consists of several tools and methods. The first tool from the basic level is discounted cash flow by assessing the net present value of expected future cash flow. Then asset based methods, it is assessing company value by connecting the current market value or book value of the assets and liabilities components. The last is market approach valuation by referencing to sales in comparison between guideline companies that have a position in public or private marketplace. Other models to measure company's value based on McKinsey on *Valuation* fifth edition, there are five models, they are enterprise discounted cash flow, discounted economic profit, adjusted present value, capital cash flow, and equity cash flow. While regarding to *Valuation* second edition by Damodaran, there are three models; discounted cash flow valuation, relative valuation, and contingent claim valuation.

Discounted cash flow valuation has its foundation in the present value rule where the value of any asset is the present value of expected future cash flows on it. The idea behind market approach is that the value of a business can be determined by reference to reasonably comparable guideline companies that have taken place in either the public or private marketplace (Hitchner, 2006). The asset approach is a general way of determining a value of a business, business ownership interest, or security using one or more methods based on the value of the assets net of liabilities. Asset-based approach assigns a value to the firm by aggregating the current market value of its individual component assets and liabilities (White, 2002). Relative valuation is the tool of valuation that estimates based on the other company market price similar assets. The measurement derives from the comparable firms. Economic-profit based valuation model is one of the models that close link to economic theory and competitive strategy.

Share is a part of a large amount that is dividend among a number of people contribute a stock can be undervalued or overvalued. The share price is the price of a share of a number of shares outstanding by company. The price of the share is moving second by second and its price can be higher or lower than the first public offering price. In the term of price, share price can be

undervalued or overvalued. Undervalued stock is a stock which price is selling at the below of the industry price or its intrinsic value. A stock can experience undervalue because maybe a drop in demand by investor perceptions and it the revenue or earnings, growth projections or company balance sheet rise while the company market price is constant. While overvalued stock is a stock with price above the standard price from the sector price or over its intrinsic value after the stock is calculated by valuation method. Overvalued stock is a stock with market price is assumed too high for its fundamentals. Most of investors refuse to pay for overvalued stock because it costs much money. Overvalued stocks happened because of a surge in demand by investors' perceptions and if the fundamentals decline while the market price constants.

Methodology

Valuation measurement in this research used three methods of valuation, those are Discounted Cash Flow (DCF), asset based approach, and market approach.

The income approach that will be using in this research is using discounted cash flow method. DCF or discounted cash flow method is using time value of money concept and focus on the company's performance in the future. To calculate the present value is

$$\text{Value of firm} = \sum_{t=1}^{t=n} \frac{CF \text{ to firm}_t}{(1 + WACC)^t}$$

The asset-based approach is defined as a general way of determining a value of a business, business ownership interest, or security using one or more methods based on the value of the assets net of liabilities. By compute the adjusted book value, a method within the asset approach whereby all assets and liabilities are adjusted to their fair market values. The asset-based method focuses on a Company's net asset value or the fair-market value of its adjusted value minus its total non-current liabilities divided by number of outstanding shares. The asset-based method formula as follows:

$$\text{Share price} = \frac{\text{Total adjustment value} - \text{total long term debt}}{\text{Number of outstanding shares}}$$

The market approach is using the company's earnings. Earnings are defined as net profit which is the amount of money left over after the companies pay all of its expenses. P/E ratio is calculates the value of a company through its earnings or net profit that calculate from the stock price of the company divided by earnings per share. The market approach used P/E (price to earnings) Ratio for the calculation formula as follows:

$$\text{Share price} = \frac{PER \times \text{Net income}}{\text{Number of outstanding sshares}}$$

Data Analysis

Asset Based Method

	Asset-based Method	
	Before tanslation and adjusment (IDR)	After (USD)
ASSETS		
TOTAL CURRENT ASSETS	4,014,641,912,519.00	322,091,517.00

NON-CURRENT ASSETS		
TOTAL NON-CURRENT ASSETS	<u>4,921,203,344,101.00</u>	<u>376,774,387.00</u>
TOTAL ASSETS	<u>8,935,845,256,620.00</u>	<u>698,865,904.00</u>
LIABILITIES	-	-
TOTAL CURRENT LIABILITIES	<u>779,608,111,961.00</u>	<u>60,449,971.00</u>
NON-CURRENT LIABILITIES		
TOTAL NON-CURRENT LIABILITIES	<u>5,255,748,838,510.00</u>	<u>405,399,306.00</u>
TOTAL LIABILITIES	<u>6,035,356,950,471.00</u>	<u>465,849,277.00</u>
ASSET-BASED VALUE	<u>2,900,488,306,149.00</u>	<u>233,016,627.00</u>

By computing each of the total adjusted value of PT Sritex's assets and the value of its liabilities, the total value of PT Sri Rejeki Isman Tbk based on Assed-based Method is: US\$ 698,865,904 – US\$ 456,849,247 = US\$ 233,061,627. After estimating the value of PT Sritex using asset-based method, the author calculates the company share price using the same approach which is dividing the total adjustment value by total of outstanding shares. Below is the calculation:

$$\begin{aligned}\text{Share Price} &= ((\text{Total Adjusted Value}-\text{Total Long-term liabilities}))/(\text{Number of Outstanding Shares}) \\ &= 293466598/(18,592,888,040) \\ &= \text{US\$ } 0.0158\end{aligned}$$

Regarding the calculation above, the share price of PT Sri Rejeki Isman Tbk is US\$ 0.0158 (IDR 195.99). Thus the author assumes that the company's share price experienced undervalue.

Market Approach

From the calculation of P/E Ratio Company (5.45) multiple with US\$ 44,758,696 of PT Sri Rejeki Isman Tbk net income in the end of 2014, the value of the company is US\$ 243,934,893.20. And from the multiply of 7.6082 of P/E ratio industry and the company's net income in the end of 2014, the PT Sritex value would be US\$ 340,533,110.

With number of share outstanding at 2014 which is 18,592,888,040 shares, the author is able to know the price per share of PT Sritex. From the calculation, the author got the price per share based on P/E ratio company and industry average are US\$ 0.0131 (IDR 162.91) and US\$ 0.0183 (IDR 227, 42), respectively. Therefore, according to market based approach the author assumes that PT Sri Rejeki Isman Tbk's share price has fair value.

Income Approach

Scenario	Value	Share Price	
		US\$	IDR
Pessimistic	12,237,703,392.12	0.6364	7902.06
Most-Likely	12,647,381,934.72	0.6599	8193.69
Optimistic	12,791,729,816.21	0.6662	8272.06

Based on the result of calculation of discounted cash flow above, the highest value from the scenarios is come from optimistic scenario. This might happen because the author use assumption of growth rate beyond the other scenarios, it derive from textile and garment growth in Asia that gives positive sentiment to the company.

Conclusion

Conclusion

First method is assets-based approach. From this, the author found the value of the company is US\$ 233,061,627. From that amount the author is able to know the book value price per share which is US\$ 0.0158 (IDR 195.99). Second method used by the author is market based approach. According to this approach, PT Sri Rejeki Isman Tbk is generated US\$ 243,934,893.20 of company value, which means the book value price per share is US\$ 0.0131 (IDR 162.91). Besides that, from this method, the author also is able to compare the company's performance with the industry average. From the analysis, PT Sritex's performance is still below its competitor performance. Refer to the industry average, due to a lower market price per share compare to the book value, the author might said that the share price is undervalue. Comparing to the current market value price per share at the end of 2014, which is IDR 163, the book value price per share of PT Sritex is lower than the market value price per share. Thus, PT Sritex stocks performance has experience undervalue. The third method used by the author to estimate PT Sritex in this research is Income Approach, which is Discounted Cash Flow Method. According to this approach, from three different scenarios which are pessimistic, most likely and optimistic, the calculation shows different result.

Table 5.1 Discounted Cash Flow Scenarios

Scenario	Value	Share Price	
		US\$	IDR
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The highest value from the scenarios is come from optimistic scenario. This might happen because the author use assumption of growth rate beyond the other scenarios, it derive from textile and garment growth in Asia that gives positive sentiment to the company. However, all of the results shows that the company's share price is experienced undervalue. The research objective of this research which is to estimating the company value of PT Sri Rejeki Isman Tbk has fulfilled. Each of method gives different result because of the different focuses on valuing the company. To conclude the entire analysis, based on the methods used in this research, the author assumes that the company share price is undervalued.

Recommendation

In order to increase the company value, PT Sri Rejeki Isman Tbk, should increase the free cash flow and decreasing the cost of capital. Free cash flow derived from subtracting net operating cash flow and depreciation with net working capital and capital expenditure. PT Sritex should increasing the operating income and/or decreasing change in net working capital and net capital expenditure. For instance, to increase operating income, the company should push the total sales by increasing marketing campaign or expand its market to gain new customer. PT Sritex also has to reduce the unnecessary expenses that generate no growth and revenue, it will contribute in increasing the operating income as well as the free cash flow. Regarding the stock price was undervalue, the author

recommend to investors who invest in PT Sri Rejeki Isman Tbk's stock (SRIL) to apply wait-and-see strategy. Undervalued stocks should be purchased or hold by investors because the price tends to go up closer to the fair price. From that pattern, the investors likely to obtain more capital gain in the future.

At the end, the author would give recommendation for further research that relates to this research topic. For estimating the company value, the author recommend to use other approach to get more accurate and reasonable value of the company such as, economic-profit based valuation and equity cash flow model. For valuing the price of share, the author suggests to apply fundamental analysis. Fundamental analysis will predict the stock price with considering the fundamental factors that affect the price in the future and applying the correlation of these variables in order to obtain more accurate estimation of the stock price.

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