Analysis

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Assignment 11 Transfer Pricing With ABC Summary The case study focused on Teva Ltd., which is a pharmaceutical company operating in Israel, but also extended its business in U. S. Operating in a very competitive environment on which traditional transfer prices approaches could not determine better operating performance, Teva Ltd. implemented an ABC (activity based costing) method.

The advantages of applying this method were cost reduction and production efficiency in manufacturing plants, and most importantly it is a tool in the making decision process by helping managers in deciding which manufacturing facility is considered most appropriate for type of product.

Learning Outcome

This article considered an application of ABC method in practice. As the case study related, Teva Ltd. benefitted from considering this method over more traditional ones because it helped her to reduce the unused capacity and finally to improve its production.

11. 2 What Is EVA, and How Can It Help Your Company?

Summary

EVA (economic value added) can be defined as an indicator of financial performance, and is computed by the difference between operating profits and a capital charge. It can be sustained that EVA is a true measure of economic profit, which takes into account all costs, implying also the cost of capital.

Another measure is MVA (market value added), and it is an indicator of the wealth of the company. It is computed as the difference between market value of common stock, preferred stock, debt and the total capital. Basically, it is the difference of the amount investors can take out and the amount invested by them.

Considering EVA in valuation has also drawbacks. One of them is the fact that EVA does not consider the growth opportunities of the company. To solve this issue, management should take into account the MVA method.

Learning Outcome

The article discussed the use of EVA and MVA in valuation of a company's investments. Although, probably in practice an NPV and IRR methods are easier to implement, EVA could be a more appropriate indicator to measure performance and to make the appropriate decisions when running a company.

11. 3 Greening with EVA

Summary

To recap, EVA is the difference between net operating profit and capital charges, whilst MVA is the difference between market value and invested capital. EVA is preferred to MVA mainly because it is more amenable to periodic performance management.

Using EVA in valuation brings benefits such as resolving budgeting issues, easiness of the making decision process, and accountability of management for all economic outlays. Basically, EVA solves some of the conflict of interest between management and shareholders by encouraging managers to think in the best interest of shareholders.

Learning Outcome

In my opinion, EVA is a method that should be considered more in valuation due to its advantages, from which the most important one is the alignment of management and shareholders decisions.