

Technical analysis of cement industry in india economics essay



**ASSIGN
BUSTER**

People invest in stocks to make their money grow. And to help investors identify the suitable and the appropriate way to invest, there are various modes of analysis. A number of approaches have been developed over time. One most important analytical approach among them is EIC analysis (E for economy, I for industry and C for company). EIC analysis is also sometimes referred to as Fundamental Analysis or the Top Down approach to Fundamental analysis. . In this approach, the investment decisions are taken on the basis of the strength of the economy, industry and company. The major objective of undergoing a project on EIC analysis or top down approach to fundamental analysis is to answer the question as “ What to buy”.

At economy level, fundamental analysis will focus on the economic indicators of the country to assess the present and future growth of the economy.

Major economic indicators include the GDP growth rate, inflation, imports, exports, monetary and fiscal policies, foreign exchange reserves, IIP, etc. The basic assumption is that if the economy grows, companies would do well.

At the industry level, apart from economy other factors like government attitude, entry barriers, competition level, threat of potential entrants, substitute products, cost structure, foreign entrants, also affect the way an industry evolves in time and hence affects the stock prices of companies in that particular industry. This industry analysis will also include Porters five force model (wherever applicable) which will give a better approach to it.

The next task to be done in the project is to identify and analyze two companies i. e. ACC and Ultratech cement Ltd. For that a number of factors

will be taken into consideration, say, the company's SWOT analysis and the financials of the company. Thus, on the foundation of some major factors, this EIC analysis will analyze the overall economy, industry and company which will give a clear picture and practical approach of stock identification.

The second part of the project is Technical analysis which is a method of evaluating securities by analyzing the statistics generated by market activity, such as past prices and volume. Technical analysis looks at the price movement of a security and uses this data to predict its future price movements. Thus a technical analyst approaches a security from the charts.

2. ECONOMIC ANALYSIS

EIC analysis is not just about balance-sheets or analysis of a company's financial performance. It is also crucial to look at the broader picture- the macro-economic factors that may directly or indirectly affect the economy, industry and stocks of the company. Economic Analysis is the First Step in a three step security analysis process. An economic slowdown has implications for the earnings and margins of companies. At economy level, fundamental analysis will focus on the economic indicators of the country to assess the present and future growth of the economy. It aims at analyzing the overall Economy and identifying the general direction, in which the economy is heading. Although there are many macroeconomic indicators that are relevant to markets, given below are some must-track-indicators

GROSS DOMESTIC PRODUCT

The GDP (Gross Domestic Product) growth rate is the most important macroeconomic indicator of a nation's economic health. If the GDP is

growing, so will economy, businesses, jobs and personal income. If GDP is slowing down, then businesses will hold off investing in new investments and hiring new employees, waiting to see if the economy will improve. If the GDP growth rate actually turns negative, then it means the economy is in a recession. Thus, on the basis of the GDP data, we can analyze the economy and interpret the future of India's economy up to some extent. Given below is the data of real GDP growth rate from the year 2006 till the year 2010.

In the year 2008, India's GDP growing at 7.9%, was the lowest in three years and was indicative of slowdown in Indian economy. Recorded for the months of April-June 2008, India's economic growth rate was 7.9% which was less than what it was at the same time last year. The economy had expanded by 7.6 per cent in the July to September quarter of 2008. India's economic growth slowed to just 5.3 per cent in the last three months of 2008, its slowest pace of expansion in the last six years, as the global financial crisis took its toll on local manufacturers and farm output fell.

The International Monetary Fund has forecast India's economy to grow at 6.75 percent in 2009-10 and 8 percent in 2011-12 on the back of an expected pick-up in private consumption and investment. Indian economy grew 8.6 percent from January to March of 2010, keeping in line with governmental projections. During the quarter, mining and quarrying, manufacturing and trade, hotel, transport and communication saw year-on-year growth of 14 percent, 16.3 percent and 12.4 percent. The country strives to attain 8.5 percent growth of GDP in fiscal year 2010-2011 with the aim of realizing 9 percent growth in the following year.

INFLATION

Inflation is no stranger to the Indian economy. It is an increase in the price of a basket of goods and services that is representative of the economy as a whole. Inflation is an upward movement in the average level of prices.

Because inflation is a rise in the general level of prices, it is intrinsically linked to money. It denotes too much money chasing too few goods.

High rates of inflation can have critical effects on economy. It is characterized by depreciation in the value of money. Economists attribute a number of factors to inflation that can be broadly categorized under supply side factors like increased production costs and demand side factors like excessive demand created by tax cuts, cheaper borrowings etc. High rates of inflation can have serious consequences for the economy in general.

Therefore, for governments all over the world, reducing movements of prices to a minimum is seen as a primary economic objective.

The above effects can be exemplified by taking the current scenario of the Indian economy. Annual Inflation in India in May 2008 was 7.4% which was the highest since November 2004. As a result Industrial production growth declined to 8.6% in February 2008 as compared to 11% in February 2007. Thus, high inflationary rate is harmful because the value of the money falls, cost of living rises, reduces the value of savings, discourages future investment and savings and slows down the overall growth of the economy. The India's economic story can be traced by seeing the general trend of inflation rate in the year 2008.

In the Year 2008, RBI had revised its key rates several times to maintain the liquidity in the banking system. The lower interest rates will allow the banks to cut their benchmark lending rates, though the deposits will also see the reduction in interest rates. Lower commodity prices and crude oil prices is driving the Inflation on a downside. This will be wonderful as the lower inflation means, lower cost of credit, which drives the economy on the upside. For 2009, Indian inflation stood at 11.49% Y-o-Y.

On March 19, 2010, the Reserve Bank of India raised its benchmark reverse repurchase rate to 3.5% percent, after this rate touched record lows of 3.25%. The repurchase rate was raised to 5% from 4.75% as well, in an attempt to curb Indian inflation. The inflation rate in India was 13.73 percent in June of 2010. This is because of the prices of pulses were up by 34.40 per cent from a year ago, milk by 21.12 per cent, fruits by 13.67 per cent, cereals by 5.41 per cent, rice by 6.76 per cent and wheat by 3.97 per cent. On 19th August, cheaper vegetables pull down inflation to 10.35%.

UNEMPLOYMENT RATE

India has been facing huge problem of unemployment and underemployment from years. Unemployment is much higher in urban areas than in rural areas and too women face the unemployment more. Various problems like enormous increase in the population, age, vocational unfitness and physical disabilities, technological and economic factors have caused this problem. Other problems also contribute towards unemployment.

Several socio-economic problems like poverty, malnutrition, antisocial and criminal activities, drug and substance abuse, etc. are the result of ill effects of unemployment. Underemployment, Disguised unemployment, regional

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imbalances in the unemployment scenario in India are another important factor. The decline in job creation in agriculture has been identified as one of the important reasons behind the increasing unemployment in India. But players like TCS, BSNL & WIPRO have announced their plan to hire more and more people in 2010.

IMPORTS

India's merchandise imports witnessed a growth of 44.9 per cent during April-September 2008, and thereafter it showed a deceleration, reflecting the slowdown in industrial activities due to global economic crisis. The overall imports during April 2008-January 2009 at US\$ 241.5 billion, recorded a lower growth of 24.4 per cent than 30.9 per cent recorded a year ago. POL imports during April 2008-January 2009 at US\$ 82.1 billion, however, maintained broadly a similar growth of 30.6 per cent (31.9 per cent a year ago) reflecting the high pace of crude oil prices. Imports during January 2009 at US\$ 18.5 billion also declined by 18.2 per cent for the first time during the current year 2008-09 so far, as against an increase of 64.0 per cent in January 2008, mainly due to sharp decline in oil imports. The overall imports during April 2008-January 2009 at US\$ 241.5 billion, showed a growth of 24.4 per cent lower than that registered during the comparable period of previous year (31.0 per cent) on account of deceleration in both oil and non-oil imports.

India's imports during March, 2010 were valued at US \$ 27733 million (Rs. 126175 crore) representing a growth of 67.1 per cent in dollar terms (48.4 per cent in Rupee terms) over the level of imports valued at US \$ 16597 million (Rs. 85022 crore) in March, 2009. Oil imports during March, 2010

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were valued at US \$ 7730 million which was 85. 2 per cent higher than oil imports valued at US \$ 4175 million in the corresponding period last year. Non-oil imports during March, 2010 were estimated at US \$ 20003 million which was 61. 0 per cent higher than non-oil imports of US \$ 12422 million in March, 2009.

EXPORTS

India's merchandise exports, after recording a steady growth of 35. 3 per cent during April-August 2008, declined in all the subsequent months so far, during the current year, viz., (-12. 1 per cent in October), (-9. 9 per cent in November), (-1. 1 per cent in December) and (-15. 9 per cent in January 2009) on account of global financial turmoil and economic slowdown. With the result, the overall exports during April 2008-January 2009 at US\$143 billion increased by 12. 4 per cent as compared with 24. 1 per cent during the corresponding period of the previous year. Exports of labor intensive sectors such as, textiles, gems and jewelers, agricultural and allied products, ores and minerals, leather products have registered decelerated growth as these sectors have been adversely affected under the impact of demand recession, mainly in the developed regions, viz., the US and the EU. Exports in 2009- 2010 is 90573 crore as compared to 66169 crore in 2008-09, hence showing a growth of 36. 9%.

EXCHANGE RATE

Since the international business environment has no universal medium of exchange, exchange rates is a necessity for international trade. Presently, both translation and conversion of foreign currency involve the use of

exchange rates. Therefore, in order to gain a more thorough understanding of <https://assignbuster.com/technical-analysis-of-cement-industry-in-india-economics-essay/>

foreign currency translation, it is important to examine the nature of exchange rates and the critical role they play in the international economy. The recent Asian currency crisis demonstrates how critically exchange rates impact economic developments. Economic factors affecting exchange rates include hedging activities, interest rates, inflationary pressures, trade imbalances, and market activities.

The political factors influencing exchange rates include the established monetary policy along with government action or inaction on items such as the money supply, inflation, taxes, and deficit financing. Psychological factors also influence exchange rates. These factors include market anticipation, speculative pressures, and future expectations.

MONETARY AND FISCAL POLICY

. Fiscal Policy

Riding on the path of fiscal consolidation, in February 2008, the world economy was hit by three unprecedented crises — first, the petroleum price rise; second, rise in prices of other commodities; and third, the breakdown of the financial system. The combined effect of these crises of these orders is bound to affect emerging market economies and India was no exception. The first two crises resulted in serious inflationary pressure in the first half of 2008-09.

Series of fiscal measures both on tax revenue and expenditure side were undertaken with the objective of easing supply side constraints. These measures were supplemented by monetary initiatives through policy rate changes by the Reserve Bank of India and contributed to the softening of

domestic prices. Additional budgetary resources of Rs. 1, 50, 320 crore was provided as part of stimulus package and various committed liabilities of Government including rising subsidy requirement, implementation of Central Sixth Pay Commission recommendations and Agriculture Debt Waiver and Debt Relief Scheme for Farmers contributed to the higher fiscal deficit of 6 per cent of GDP in RE 2008-09 as compared to 2. 5 per cent of GDP in B. E. 2008-09.

The measures taken by Government to counter the effects of the global meltdown on the Indian economy, have resulted in a short fall in revenues and substantial increases in government expenditures, leading to a temporary deviation from the fiscal consolidation path mandated under the FRBM Act during 2008-09 and 2009-2010. The fiscal policy for the year 2009-2010 is continued to be guided by the objectives of keeping the economy on the higher growth trajectory amidst global slowdown by creating demand through increased public expenditure in identified sectors.

Monetary policy

India has rapidly integrated into the global system and has linkages with the rest of the world not just through trade channels, but also through two-way movements of capital and finance. As an integral part of a globalizing world, India cannot be expected to remain immune to a global crisis and in responding to the crisis, India has to share the uncertainty on the way forward just like the rest of the world.

Both the Government and the Reserve Bank have acted to protect the economy from the adverse impact of the crisis since mid-September 2008.

While the Government has announced three major fiscal stimulus packages, the endeavor of the Reserve Bank has been to provide ample rupee liquidity, ensure comfortable dollar liquidity and maintain a monetary policy environment conducive for the continued flow of credit to productive sectors. Towards this endeavor, the Reserve Bank has adopted both conventional measures such as, for example, reduction of the cash reserve ratio (CRR), as well as unconventional measures such as, for example, the dollar swap facility for banks.

To improve the flow of credit to productive sectors at viable costs so as to sustain the growth momentum, the Reserve Bank signaled a lowering of the interest rate structure by significantly reducing both its key policy rates - the repo rate and the reverse repo rate. The statutory liquidity ratio (SLR) has also been reduced by one percentage point releasing funds to banks for credit deployment. In the space of just one quarter, the repo rate has been reduced from 9.0 per cent to 5.5 per cent and the reverse repo rate from 6.0 per cent to 4.0 per cent, thereby bringing down both of them to historically lowest levels.

The Reserve Bank of India lowered its benchmark repurchase rate to 7.5 percent from 8 percent. At the same time the central bank also reduced the cash reserve ratio to 5.5 percent from 6.5 percent, and cut the amount of money lenders are required to keep in government bonds to 24 percent from 25 percent.

But the measures taken by government and the Reserve Bank will continue to maintain vigil, monitor domestic and global developments, and restore the economy to its potential growth path.

INDUSTRY ANALYSIS

INDUSTRY SNAPSHOT

The Indian Cement Industry with a capacity of around 125 Million Ton Per Annum (MTPA) is the fourth largest in the world after China, Japan and USA. However, the per capita consumption in the country is only around 90 kgs as compared to the world average of approx. 250 kgs. The Cement Industry is highly fragmented comprising of more than 50 players operating from more than 125 plants. The Cement Industry is cyclical and capital intensive.

Cement is a key infrastructure industry. It has been decontrolled from price and distribution on 1st March, 1989 and delicensed on 25th July, 1991.

However, the performance of the industry and prices of cement are monitored regularly. The constraints faced by the industry are reviewed in the Infrastructure Coordination Committee meetings held in the Cabinet Secretariat under the Chairmanship of Secretary (Coordination). Its performance is also reviewed by the Cabinet Committee on Infrastructure.

The Cement Industry witnessed a slow start in the FY 2005 due to change in the Government at the centre; slow down in infrastructure spending during the transition and adversities of drought like conditions in the South and West. The subsequent regaining of momentum enabled the industry clock a dispatch growth of 7% for the full year. The Cement sector appears to be on a sustainable growth path, given the strong outlook for the housing sector

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and the renewed momentum in infrastructure spending. The Cement sector appears to be on a sustainable growth path, given the robust outlook in Government infrastructure spending. It is expected that the industry would grow at an average 8% annual growth in the long run.

The industry has witnessed consolidation in the recent years which is likely to increase with the entry of global players. Cement being an energy intensive industry; power and coal are the major cost contributors. Logistics also form a significant portion of the cost. The looming coal shortage will not only affect the cost, but also the quality of coal. Cement prices are expected to firm up across regions in the medium term on account of a better demand- supply balance and greater consolidation. The induction of advanced technology has helped the industry immensely to conserve energy and fuel and to save materials substantially. India is also producing different varieties of cement like Ordinary Portland Cement (OPC), Portland Pozzolana Cement (PPC), Portland Blast Furnace Slag Cement (PBFS), Oil Well Cement, Rapid Hardening Portland Cement, Sulphate Resisting Portland Cement, White Cement etc.

GROWTH PROSPECT

The one Indian industry which is set for growth over the coming years is the Cement Industry. The industry is heavily dependent on 3 sectors; coal, power and transport. Energy and freight are the two major cost components. Over the last few years, while the proportion of energy cost has increased marginally, freight costs have declined.

Increasing government expenditure on infrastructure sector and rising demand for commercial and residential real estate development has resulted in higher demand for cement in the country. According to a report by the ICRA Industry Monitor, the installed cement capacity is expected to increase to 241 million tones per annum by the end of 2010. It also expects that driven by higher domestic demand and increasing utilization, India's cement industry may record an annual growth of 10% over the coming years.

Taking cue of the global economic slowdown which was affecting cement companies in India last year, Governments initiative to re-impose counter-veiling duty and special counter-veiling duty this year will help provide a level playing field for domestic players. Moreover, it also appointed a coal regulator to facilitate timely and proper allocation of coal blocks to the important sectors like cement. As coal is one of the prime raw material used in cement production, this seems to be a positive move.

Growth potential of cement industry can be judged by the fact that the per capita cement consumption (156 kg) in India is still well below the global average consumption (396 kg). This gap can be expected to be covered in the coming years. Besides, housing sector accounts for almost 50% of the total cement consumption in the country and the large young population will ensure that the demand for infrastructure stays put.

The rising cost of energy, transportation raw material continues to pressure the industry as a whole. To sustain profitability, companies will have to explore alternate source of energy while at the same time enhance their operational efficiency.

Industry experts opine that the cement industries should now increase their focus on investing adequately in developing human resources that will be capable enough to address the professional needs of construction industry including advanced technologies and construction practices, project management construction and litigation. We expect that the cement production and consumption both will grow substantially over the years.

PORTER'S FIVE FORCES MODEL

Rivalry among Competing Firms

Inter firm rivalry is very high in this sector. Reasons for this are mainly large number of players in the market, intermittent overcapacity, marginal product differentiation, high storage cost and high exit barriers in the form of huge capital investment.

Potential Entry of New Competitors

In cement Industry technology and manpower are easily available but still entry of new firms is not that viable. This is because of huge capital investment, broad distribution network and oversupplied market.

Potential Development of Substitute Products

Only bitumen in road and engineering plastics in building offer some element of competition otherwise no close substitutes are popular in India.

Bargaining Power of Suppliers

The bargaining power of suppliers of raw materials and intermediate goods is very high. Because of monopolistic control of external cost elements i. e.

coal, power, transportation and taxes suppliers are enjoying high bargaining power with the government.

Bargaining Power of Consumers

Rising share of retail purchase, declining share of bulk purchase by government has taken away the bargaining power of customers.

SWOT ANALYSIS

Strengths

Second largest in terms of capacity- In India there is approximately 124 large and 300 mini plants with installed capacity of 200 million tonnes.

Low cost of production- Because of easy availability of raw material and cheap labor.

Weakness

Demand supply gap, overcapacity- the capacity additions distort the demand supply equilibrium in the industry thus affecting the profitability.

Increasing cost of production due to increase in coal prices.

High interest rate on housing- increase in interest rate from 7% to 12% has resulted in slowdown in residential property market.

Opportunities

Increase in infrastructure projects- Infrastructure accounts for 35% of cement consumption in India. And with increase in government focus on infrastructure spending such as roads, highways and airports, the cement demand is likely to grow in future.

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Growing middle class- There has been a increase in purchasing power of emerging middle class with rise in salary and wages, which results in rising demand for better quality of life that further necessitates infrastructure development and hence increase yhe demand for cement.

Technological changes- At present 93% of the total capacity in industry is based on modern and environmental friendly dry process and only 7% is based on old wet and semi dry process technology. The induction of advanced technology has helped the industry immensely to conserve energy and to save materials substantially and hence reduce the cost of production.

Threats

Excess overcapacity can hurt margins as well as prices.

COMPANY ANALYSIS

ACC LIMITED

Established in 1936, has been a pioneer and trend setter in cement and concrete technology. A prominent overseas presence and figuring on the elite list of consumer super brands of India but most importantly acc has been amongst the first Indian companies to make environment protection as cornerstone of its corporate objectives. The historic merger of ten existing companies has led to the established of acc- melding into a cohesive organization in 1936. It offers the services of ready made concrete and consultancy services. This company is listed by Bombay stock exchange, National stock exchange and in London.

During year 2007 company acquired 100% equity stake in Lucky Minmat Private limited for Rs 35 crores and also acquired 43% stake in Shiva Cement Limited. Meanwhile the company divested its entire equity shares in Almatiss ACC limited to the Almatiss group. The overseas contact with YANBU Cement Company in the kingdom of Saudi Arabia is successfully ongoing relationship from last 28 years and has been renewed up to Feb 28, 2011.

The company's various manufacturing units are backed by a central technology support services centre - the only one of its kind in the Indian cement industry. ACC has rich experience in mining, being the largest user of limestone. As the largest cement producer in India, it is one of the biggest customers of the domestic coal industry, of Indian Railways, and a considerable user of the country's road transport network services for inward and outward movement of materials and products.

The company has developed comprehensive expansion plans to meet the requirement of its agenda for growth with a view to attain leadership position in the cement industry, for that company made a project for augmentation of clinkering and cement grinding. Also it implements projects for augmenting grinding capacity at Madukkaria by 0. 225 MTPA and New Wadi at 0. 60 MTPA.

Ready mix concrete business has been identified as area of strategic priority. ACC commissioned a Wind Energy Farm in Tamil Nadu to promote clean and green technology. The company foresees substantial scope for growth of this business in India. The company actively promotes the use of alternative fuels

and raw materials and offers total solutions for waste management including testing, suggestions for reuse, recycling and co-processing.

2009

2008

2007

2006

2005

Net Income

1, 606. 73

1, 212. 79

1, 438. 59

1, 231. 84

544. 18

Capital Expenditure

6826. 27

5835. 67

5464. 07

4861. 25

4628. 64

Depreciation

342.09

294.18

305.07

254.25

164.37

Interest

104.63

39.96

73.87

75.19

66.19

Tax Rate

0.35

0.35

0.35

0.35

0. 35

Interest(1-Tax Rate)

68. 0095

25. 9740

48. 0155

48. 8735

43. 0235

Change In Working Capital

-851. 66

12. 16

-41. 22

203. 66

-48. 13

Increase In Debt

84. 89

175. 62

-609. 57

-260. 19

-332. 9

FCFE

-3872. 89

-4139. 27

-3700. 74

-3790. 14

-4161. 84

Growth Rate

0. 108

0. 0415

0. 203

0. 799

-0. 029

Cost Of Equity

0. 079

Terminal Value

147971. 108

Value Per Share

454. 271

When we look at the values that are obtained using the DCF and the stock prices we can say that the prices of the companies stock are mispriced to a large extent. The intrinsic values for four consecutive years turned out to be negative which means that the shares are highly over priced. The investments in these stocks are very risky.

ULTRATECH CEMENT

Ultratech Cement Limited (UltraTech) is India-based one of the largest cement manufacturing company. UltraTech Cement was incorporated as a public limited company on 24th August 2000, as “ L&T Cement Limited” a 100% Subsidiary of Larsen & Toubro Limited. The name of the Company was changed to UltraTech CemCo Limited with effect from 19th November 2003. The name of the company was again changed to UltraTech Cement Limited with effect from 11th October 2004.

UltraTech Cement has an annual capacity of 18. 2 million tones. It manufactures and markets Ordinary Portland Cement, Portland Blast Furnace Slag Cement and Portland Pozzalana Cement. It also manufactures ready mix concrete (RMC).

The company has five integrated plants, six grinding units and three terminals- two in India and one in Sri Lanka. It is the country’s largest

exporter of cement clinker. The export marketspan countries around the Indian Ocean, Africa, Europe and the Middle East.

The company has an annual cement production capacity of 18. 2 million tones. It is a subsidiary of Grasim Industries Ltd. The company operates two subsidiary companies namely, Dakshin Cement Limited and UltraTech Ceylinco (P) Limited. The company is headquartering at Mumbai in India. The company reported revenues of (Rupee) INR 66, 643. 30 million during the fiscal year ended March 2009, an increase of 16. 43% over 2008. The operating profit of the company was INR 13, 678. 20 million during the fiscal year 2009, a decrease of 9. 73% from 2008. The net profit of the company was INR 9, 780. 60 million during the fiscal year 2009, a decrease of 3. 17% from 2008.

2010

2009

2008

2007

2006

net income

1, 093. 24

977. 02

1, 007. 61

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782. 28

229. 76

capital expenditure

8, 078. 14

7, 401. 02

4, 972. 60

4, 784. 70

4, 605. 38

depreciation

388. 08

323

237. 23

226. 25

216. 03

interest

117. 52

125. 51

82. 31

86. 83

89. 64

tax rate

0. 35

0. 35

0. 35

0. 35

0. 35

interest(1-tax rate)

76. 388

81. 5815

53. 5015

56. 4395

58. 266

change in working capital

54. 1

92. 65

-180. 43

-11. 48

-181. 88

increase in debt

-537. 11

401. 13

161. 87

126. 80

-79. 55

FCFE

-7, 111. 64

-5, 710. 94

-3, 331. 96

-3, 581. 45

-3, 998. 99

-23, 734. 98

growth rate

10.44%

10.44%

10.44%

10.44%

10.44%

cost of equity

7.39%

7.39%

7.39%

7.39%

7.39%

terminal v