Foreign Exchange Policy Department
Bangladesh Bank
Head Office
Dhaka
www.bb.org.bd

FE Circular No. 32 Date: August 31, 2014

All Authorized Dealers in
Foreign Exchange in Bangladesh

Dear Sirs,

<u>Repatriation of sale proceeds of non-resident owned equity in unlisted companies purchased by residents</u>

Paragraph 3(B), chapter 9 of the Guidelines for Foreign Exchange Transactions-2009 currently states that the sale proceeds of non-resident equity investment in unlisted companies and private limited companies are repatriable abroad with prior Bangladesh Bank approval to the extent of net asset value of the shares as on the date of sales, based on latest audited financial statements.

02. It has now been decided that in such cases Bangladesh Bank will accept fair value of the shares as on the date of sale based on appropriate combination of three valuation approaches (viz. net asset value approach, market value approach and discounted cash flow approach) depending on the nature of the company.

03. Application for repatriation of sale proceeds of shares shall be submitted to Foreign Exchange Investment Department at head office of Bangladesh Bank with a Valuation Certificate of shares issued by a Merchant banker licensed by BSEC or a Chartered Accountant experienced in company valuation. Annexure-A to this circular provides indicative guidelines for arriving at fair value.

04. The valuation certificates by eligible valuers will have to be supported by full explanation justifying the fair value arrived at. Full set of audited financial statements of the company will have to be submitted to Bangladesh Bank along with application for remittance approval. If not fully satisfied about appropriateness of the valuation arrived at, Bangladesh Bank reserves the right to obtain second opinion from another qualified valuer of its choice.

Please inform all your concerned constituents accordingly.

Yours faithfully,

Enclosure: As stated

(Md. Abdul Mannan)
Deputy General Manager
Phone: 9530319

Annexure-A

Indicative guidelines on determination of fair value of shares of unlisted company

Bangladesh Bank has decided to consider the market value approach and discounted cash flow approach alongwith currently used net asset value approach in determining the repatriable value of shares of an unlisted company. Following is an illustrative example in determining the fair value of shares of an unlisted company using the three mostly used approaches:

Asset Based Approach

The underlying principle of asset-based approach is equivalent to the fair value of its assets less the fair value of its liabilities. This method is considered most appropriate for resource firms, financial services firms, investment companies (real estate investment trusts, closed-end investment companies) and small businesses with limited intangible assets or early stage companies.

In this approach, net asset value of the target unlisted company (net assets after meeting all the liabilities) is estimated as the fair value.

Asset based approach often indicates the most conservative valuation as it does not take into account the value of intangible assets (such as goodwill).

For 'The Sample Company', asset based approach gives us a fair value of BDT 22,370 million derived from the Balance Sheet as follows:

Balance Sheet (BDT million)	**20AC**
Current Assets	
Cash & Cash Equivalent	981
Accounts Receivable & prepayments	3,561
Inventories	3,091
Total Current Assets	**7,633**
Total Long Term Investment	**5,103**
Total Fixed Assets	**14,520**
Total Assets	**27,256**

Balance sheet (cont'd)

Balance Sheet (BDT million)	**20AC**
Current Liabilities	
Accounts Payable	**7**
Liabilities for other expense	**1,426**
Short Term Bank Loan	**1,302**
Current Portion of Long Term Debt	**540**
Total Current Liabilities	**3,275**
Total Non-Current Liabilities	**1,611**
Total Liabilities	**4,886**
Shareholder's Equity	
Share Capital (BDT 10 each)	3,708
Share Premium	2,035
Reserve	826
Retained Earnings	15,801
Total Shareholder's Equity	**22,370**
Total Liabilities & Shareholder's Equity	**27,256**

Net Asset Value of Equity = Total Assets – Total Liabilities
= BDT 27,256 m – BDT 4,886 m = BDT 22,370 m
Net Asset Value per share = BDT 22,370 m / 370.8 m = BDT 60.33

Market Value Approach

Multiple based analysis or comparable analysis is one of the widely used tools in private company valuation. Comparable company trading multiples analysis utilizes the valuation multiples of similar or comparable publicly or privately traded companies to value a target unlisted company. Peers can be grouped based on any number of criteria, such as industry focus, private company size, or growth.

The multiples can be equity based multiples like Price to Earnings (P/E), Price to Book Value of Equity (P/B) etc. The multiples derived from this type of analysis are for a given point in time and generally change over time.

The most popular equity based multiple is earnings multiple. The price-to-earnings (P/E) ratio, which is equal to a company's market price per share divided by its earnings per share (EPS), is the most widely used earnings multiple. It provides an indication of how much investors are willing to pay for a company's earnings. For example, a company whose P/E ratio is 15 is said to be selling for 15 times of earnings i.e. fair market value of a share = EPS * P/E Ratio.

It is often difficult to find out the right comparable listed companies. Hence, adjustments need to be made to reflect differences, such as business mix, geographic spread and capital structure. For instance, conglomerates may have unrelated lines of businesses that probably will require multiples from two different unique companies and then deriving a blended multiple. To select the comparable universe or peer group for a given unlisted company it must be ensured that its peers share similar industry, business, and financial characteristics.

Caution is also needed to get the correct valuation based on this method. It is advisable that at least three years average EPS of the target company to be used in valuation.

The fair value of 'The Sample Company' is as follows

Income Statement (BDT million)	**20AA**	**20AB**	**20AC**
Sales	**16,975**	**19,798**	**20,202**
Cost of Goods Sold	9,401	10,872	10,364
Gross Profit	**7,574**	**8,926**	**9,838**
Administrative Expenses	2,668	3,077	3,521
EBITDA	**4,906**	**5,849**	**6,317**
Depreciation	1,088	1,234	1,228
Other income	454	420	378
EBIT	**4,272**	**5,035**	**5,467**
WPPF	191	220	247
Interest Expenses (income)	310	465	357
EBT	**3,771**	**4,350**	**4,863**
TAX @ 40%	1,508	1,740	1,945
Profit After Tax	**2,263**	**2,610**	**2,918**
No. Shares (in million)	**196.20**	**264.80**	**370.80**
EPS in BDT	**11.53**	**9.86**	**7.87**
Average EPS in BDT			**9.75**

P/E ratio of comparable company at the date of sale = 12

Fair Market Value per share = average EPS * P/E Ratio
= BDT 9.75*12 = BDT 117.00

Income Approach

Valuation of unlisted companies in the income approach is highly sensitive to assumptions of future cash flows. In practice, income approach is not used in isolation and used as one of the drivers to determine the final price.

Income approach is primarily driven by three key inputs i.e. Free Cash Flow (FCF), Terminal Value and Discount rate; valuer needs to carefully verify all the inputs, validating these with rational assumptions. Making valuation for the target company involves the following steps:

1. The last recorded free cash flow in the audited financial statement is assumed to be the terminal perpetual cash flow for future. The free cash flow will be arrived at by taking operating cash flow from audited financial statement minus capital expenditure. The valuer must ensure that all overdue liabilities are deducted while arriving at free cash flow.

2. The discount rate should be the Weighted Average Cost of Capital (WACC) or the yield rate on 20-year BGTB as on the date of sale, whichever is higher.

3. Trend cash flow growth of the company (g) will be the average of annual cash flow growth over the past 3-5 years according to audited financial statements.

4. The valuation of the company would then be calculated by
   Fair value = FCF/(r-g)

   Where FCF = Operating Cash Flow – Capital Expenditure
   r = Discount rate
   g = Average growth rate of free cash flow in last available five years

Following these steps, one may determine the fair value of ‘The Sample Company’ as below:

DCF (BDT million)		20AA	20AB	20AC
EBIT*(1-TAX)	(1)	2,563	3,021	3,280
Depreciation	(2)	1,088	1,234	1,228
Capital Expenditure	(3)	600	1,200	1,250
Change in working capital	(4)	200	49	37
Net Cash Flow (1+2-3-4)	(5)	2,851	3,006	3,221
Terminal Free cash flow				3,221
Free Cash Flow (FCF)	(6)	2,851	3,006	3,221
Growth of FCF		6.00%	5.43%	7.15%
Average Growth of FCF (g)				6.19%

Discount Rate = 12.50% (WACC which is higher than the yield rate of 20-year BGTB has been applied)

Fair Value = FCF/(r-g)
= 3221/ (0.125-0.0619) = 51,046 m

Fair Value per share = 51,046/370.80 = BDT 137.66

Finally, after taking into account all three approaches, we derived three separate values for 'The Sample Company' as follows:

Asset based approach (Net asset value)	**BDT 60.33 per share**
Market value approach (Earnings to P/E)	**BDT 117.00 per share**
Income approach (Discounted cash flow)	**BDT 137.66 per share**