Glossary of Terms

Arbitrage opportunity is the opportunity to buy an asset at a low price and then immediately selling it on a different market for a higher price.

Base case value is the median of a range of values arrived at under DCF method.

Beta is an estimate of risk profile of the company relative to equity market. Thus, higher the beta the more riskier is the stock than the sensex. The value of beta lower than one means the stock is less volatile and hence less risky.

Business plan is a document prepared by the management of the PSU consisting of future projections, keeping in view the economic scenario, future capital investments and growth potential.

Call Option is a contract that gives the holder the right to buy a certain quantity (usually 100 shares) of an underlying security from the writer of the option, at a specified price (the strike price) up to a specified date (the expiration date).

Closing date is the day on which the closing or payment of the purchase price to Government and the completion of the sale to and purchase by the Strategic Partner of the first tranche transaction shares in accordance with the terms of the agreements, occurs.

Confidential Information Memorandum is a bid pack document, which is made available to the short listed bidders, after obtaining confidentiality undertaking from them. It contains information concerning the business, operations, prospects or other affairs of the company.

Cost of equity is the desired rate of return for an equity investor given the risk profile of the company and associated cash flows. Cost of equity = Risk free rate + (equity risk premium x β), where β (beta) of a company reflects the underlying risk of a business over and above the stock market risk.

Due diligence exercise is the task of carefully confirming all critical assumptions and facts presented to assess the desirability, value and potential of the business.

Enterprise Value is the market value of equity plus debt or total market asset value of the company.

Explicit forecast period is a period of time (say 5 to 10 years) for which a net present value of the free cash flows arising from the business under the DCF method is projected.

Expression of Interest (EoI) containing the background information about management, ownership structure, business activities including joint ventures, legal capacity of the company/consortium, participating in a privatization transaction, is to be submitted by the interested parties at the prescribed address by the stated deadline. It is normally submitted along with a statement of legal capacity and a litigation impact statement.

Flotation signifies sale of shares to individuals, financial institutions or private sector business, which can then be traded in the market.

Free cash flow (FCF) for a year is derived by deducting the total of annual tax outflow inclusive of tax shield enjoyed on account of debt service, incremental amount invested in working capital and capital expenditure from the respective year's profit before depreciation interest and tax (PBDIT) for the explicit period.

Going concern envisages continuance of operations of the business by infusion of superior technical and managerial skills besides additional capital.

Liquidation would involve selling all assets of an enterprise instead of selling it as a going concern.

Public Auction involves disinvestment of the predetermined shareholding of Government in PSU through auction in a public sale either at cut off price or at the bid price. Where disinvestment is by sale of all assets of the PSU in a public auction, it is called 'Liquidation'.

Put Option in a contract gives the holder the right to sell a certain quantity of an underlying security to the writer of the option, at a specified price (strike price) up to a specified date (expiration date).

Relative valuation method approach is used to estimate the value of an asset by looking at pricing of comparable assets relative to a common variable like earnings, cash flows, book value or sales.

Risk free rate is the yield to maturity on Government securities based on current traded value over a long-term tenor beyond the forecast period.

Shareholders Agreement (SHA) defines the rights and obligations of both the parties; it reflects the protection of employee's rights, business plans, indemnification clauses etc. SHA is entered into among the President of India (acting through Joint Secretary of the Administrative Ministry), the company and the strategic partner.

Share Purchase Agreement (SPA) describes the purchase price, mode of payment and the actions at closing time. It also lays down representations and warrantees given by both the parties. SPA is entered into among the President of India (acting through Joint Secretary of Administration Ministry), the company and the strategic partner.

Terminal Value reflects the average business conditions of the Company that are expected to prevail over the long term in perpetuity i.e. beyond the explicit period. The DCF approach assumes that by the terminal date, the business will have achieved a steady state and will be growing at a constant rate.

Trade Sale is direct sale of business in state ownership to another business. This includes joint ventures, part sales and strategic sales.

Transaction documents consist of Shareholders Agreement (SHA), Share Purchase Agreement (SPA) and Guarantee Agreement.

Weighted Average Cost of Capital (WACC) is the discount rate applied to estimate the present value of free cash flows over the explicit forecast period as also continuing value. The principal elements of WACC are cost of equity, the post-tax cost of debt and the target capital structure of the company (a function of debt to equity ratio). **WACC =** (Debt/Total Capital)*(After-Tax Cost of Debt) + (Equity/Total Capital)*(Cost of Equity)

Offer for sale is the offer of shares by existing shareholder(s) of a company to the public for subscription, through an offer document.

Public Issue is an invitation by a company to the public to subscribe to the shares offered for sale through a prospectus.

Sensitivity analysis is a simple technique to ascertain how a given model output depends upon the input parameters. This is an important method for checking the quality of a given model, as well as a powerful tool for checking the robustness and reliability of its analysis. It involves changing the value of one or more selected variables and calculating the resulting change in the Net Present Value (NPV) or Internal Rate of Return (IRR).

Abbreviations

1. BIFR- Board for Industrial and Financial Restructuring
2. BRPSE- Board for Reconstruction of Public Sector Enterprises.
3. CGD- Core Group of Secretaries on Disinvestment.
4. CCD- Cabinet Committee on Disinvestment
5. DC- Disinvestment Commission.
6. DCF- Discounted Cash Flow.
7. DOD- Department of Disinvestment.
8. DOT- Department of Telecommunications.
9. DPE- Department of Public Enterprises.
10. EBITDA- Earning Before Interest, Taxes, Depreciation and Amortization
11. EC- Evaluation Committee
12. EoI- Expression of Interest.
13. EV- Enterprise Value
14. FCF- Free Cash Flow.
15. GA- Global Advisor.
16. ILD- International Long Distance.
17. IMG- Inter Ministerial Group
18. LME- London Metal Exchange.
19. MoDI- Ministry of Disinvestment.
20. NDA- Non Disposal Agreement.
21. NIF- National Investment Fund.
22. OSF- Oil Storage Facilities.
23. OMC- Oil Marketing Companies
24. PIM- Preliminary Information Memorandum.
25. PCA- Post Closing Adjustment.
26. PSU- Public Sector Undertaking.
27. P/E- Price Earning Ratio
28. RFR- Risk Free rate of Return
29. RPO- Retail Petroleum Outlets.
30. SHA- Share Holders Agreement.
31. SP- Strategic Partner.
32. SPA- Share Purchase Agreement.
33. SRO- Sub Registrar office.
34. WACC- Weighted Average Cost of Capital.