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NIFTY 500 ANALYSIS WITH EPS YARDSTICK

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Abstract *In this research paper, we identify the relationship between the sectoral constitution of the Nifty 500 population and the 50 top-performing companies under Nifty 500. EPS, as a financial ratio, has been comprehensively used in this study. The financial statements of the selected Nifty 500 companies are used to calculate the relevant financial ratio. The EPS of the companies are expressed in terms of growth rate (R), where R = CAGR expressed to measure the EPS growth rate of each company in the Nifty 500. Rm is the average of all the EPS growth rates of the Nifty 500 companies, expressed as a benchmark of Nifty 500. R-Rm is the deviation between R and Rm. The relevant secondary data, which includes five years' observations, have been extracted from the Money Control and NSE database for the period 2012 to 2017. Based on the overall analysis, the study revealed that the sectors among the 50 top-performing companies of Nifty 500, which have the least deviation compared to the benchmark of Nifty 500, are the sectors with a majority proportion in the Nifty 500 population. The sectoral constitutions of the 50 top-performing companies under Nifty 500 are significantly different compared to the 50 bottom-performing companies. When we compare the internal sectoral proportions among the various sectors of the 50 top-performing companies there is no substantial difference among them. However, the internal sectoral proportions among the various sectors of the 50 bottom-performing companies have a significant difference among them.*

Keywords: *Nifty 500, EPS, EPS Growth Rate, National Stock Exchange of India Limited (NSE)*

JEL: *G11, G15, G19*

INTRODUCTION

Nifty 500 represents the top 500 companies based on full market capitalisation that are traded on the National Stock Exchange (NSE) of India. Nifty 500 consists of about 94% of the free-float market capitalisation of the stocks listed on NSE as on March 31st, 2016, and has 18 sectors. It depicts the economic and fundamental growth of the top 500 companies listed in India and contributes to the Annual Growth Rate (AGR) of the national Gross Domestic Product (GDP). Nifty 500 consists of various Indices such as Nifty 50, Nifty Next 50, Nifty Large Cap (1-100 stocks), Nifty Mid Cap (101-250 stocks), and Nifty Small Cap (251-500 stocks). These Indices also act as a benchmark in calculating the relative performance of financial assets such as Mutual Funds, Hedge Funds, ETFs, and so on. Nifty is owned and managed by India Index Services and Products (IISL), which is a wholly owned subsidiary of the NSE Strategic Investment Corporation Limited.

The selection criteria for Nifty 500 states that a company should be within the top 800 based on the average daily turnover and average daily full market capitalisation for at least six months. The company should also have been trading for a minimum of 90% of the days, from the date of evaluation, during the past six months. Apart from this, Nifty broad-based Indices are reviewed semi-annually, ending on 31 January and 31 July, respectively. A few factors that affect Nifty 500 are inflation, interest rates, micro factors such as economic policies, political conditions, and capacity utilisation, and macro factors such as currency movements and global demand.

National Stock Exchange of India Limited (NSE) majorly represents the Indian Stock market, which is the leading stock exchange in the country. The NSE was established in 1992. The BSE, which was earlier known as the Bombay Stock Exchange, is another stock exchange in India. NSE was the first exchange in India to provide a modern, fully automated screen-based electronic trading system to the investors spread across the length and breadth of the country. The NSE facilitates business. It offers wealth creation opportunities to investors, along with ownership of companies. It provides liquidity in the stock market as well.

Earnings per Share (EPS) is one of the tools in financial management to gauge the performance of a company on

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absolute terms. The relevance of EPS and EPS growth supporting the Valuation Methodology in modern days has been recognised by authors such as Chen, Jorgensen, and Yoo (2004); Ohlson and Juettner-Nauroth (2005); and Taboga (2011). EPS shows the profitability of the company, while keeping other factors a constant.

According to the International Accounting Standards (IAS) 33, "An entity that trades equity instruments on public markets is required to disclose EPS as part of its financial statements" (BDO, 2014; IFRS, 2014).

EPS = Net Profit after Tax/No. of Outstanding Shares

EPS indicates the amount of profit a company earns for each share of its stock floating in the market. It is a widely used metric to calculate the precise corporate profits. EPS derives a company's profit per ordinary share (Vaidya, 2014). It indicates profitability by measuring the entity's performance relative to share capital employed to generate returns (Koppeschaar, Sturdy, Du Toit, Deysel, Rossouw, Van Wyk, Gaie-Booysen, Papageorgiou & Van der Merwe, 2013).

It is an important component to arrive at Price-to-earnings (P/E) Valuation Ratio, where E in P/E refers to EPS. P/E is a tool to gauge whether the price of a stock exceeds its earnings. It also determines if a company is "overvalued" or "undervalued", based on the relative analysis with its respective sector and its peer companies. EPS is of two types, namely Basic EPS and Diluted EPS. The main difference between Basic and Diluted EPS is that the latter considers Stock Options, Warrants, Convertible Debentures, and so on, which can be converted to equity after a specific time period. For performance presentation, EPS can be measured under three categories: Basic EPS, Diluted EPS, and Headline EPS (BDO, 2014). Brigham and Ehrhardt (2007) concluded that EPS signals the prospects to current and potential investors. EPS has thus become an investment decision-making tool for investors, as it indicates future prospects and growth in market share (Mlonzi, Kruger & Ntoesane, 2011).

Compound Annual Growth Rate (CAGR) is the ratio of earnings growth to the time factor related to the change in EPS.

CAGR expressed to measure the EPS growth rate = ((Latest EPS value/Initial EPS value) ^ (1/Time Period)) − 1.

CAGR is an accurate way to calculate the returns on any investment which varies over a time period. Investors, managers, companies, and others can explore the CAGR for alternatives to arrive at the performance of any instrument in a peer group or against a market index. However, CAGR ignores investment risk and focuses only on returns generated. It assumes that profits are reinvested at the end of each year with consistent returns, whereas, in reality, the growth rates are volatile and inconsistent.

LITERATURE REVIEW

Habibniya, H., & Dsouza, S. (2018) studied the influential behaviour of certain performance measurements on the market value represented by the share price. Three major Indian banks were considered for this study. Empirical tests of the comparative and incremental data collected during the years 2012 to 2017 were observed. The results showed that EPS is a major influential factor, with a strong correlation in the variance of the market value represented by the share price.

EPS is widely used by companies as a financial performance benchmark for its investors, partners, stakeholders, and others. A study conducted by Graham, Harvey and Rajgopal (2004) on 400 financial executives in the USA concluded that a majority were of the opinion that earnings was one of the most essential performance measurements reported to stakeholders. EPS is also used for strategic business decision making, such as valuation, succession planning, growth drivers, and M&A negotiations. Management is rewarded for positive EPS growth year-on-year, and their incentives are related to EPS growth as well. Thus they take special interest in EPS computation. Investors are mostly familiar with the P/E valuation multiple, which has EPS as the denominator.

Adkins, Matchett and Toy (2010) observed that, to a great extent, EPS summarises the earnings generated for shareholders. Their views appeal to prospective investors and management.

Rappaport (2005) concludes that EPS plays an important role in both short-term and long-term earnings performance. EPS is an important factor, especially in young companies, where future growth expectations are highly dependent on current performance, whereas in older companies, there is a consistent track record of earnings growth. In addition, it is also observed that senior management tends to focus more on EPS in the short-term, as it is related to their reputation, the risk of losing their employment, and the future share price expectation.

Brown (1999) commented that in times of severe financial stress, an underperformance in EPS can lead to significant share price erosion, in the near future, due to market expectations. Large share price movements due to surprise earnings proves the perception that short-term earnings, rather than future cash flow expectations, influence share prices significantly.

Idawati and Wahyudi (2015) studied the empirical influence of EPS and ROA on stock prices. It was concluded that EPS and ROA are positively related to the stock price, and

significantly affect the stock price variations. On comparison, EPS showed a significant effect on share price, whereas ROA did not impact the share price significantly.

EPS, which is articulated as one of the financial ratios, clearly depicts the benefits that shareholders earn per share during the holding period. However, in some literature, EPS is categorised under different types of financial ratios. Donald E. Kieso, et al. (2011) categorised EPS as a profitability ratio and stated, "A company customarily sums up the results of its operations in one important figure: Net Income. However, the financial world has widely accepted an even more distilled and compact figure as the most significant business indicator – Earning per Share". Hence, EPS becomes a measurement to net income for each ordinary share. Companies thus report earnings for ordinary shares.

A study was conducted by Robbetze, N., de Villiers, R., & Harmse (2017) on the Top 40 JSE-listed companies. Samples were selected, and the relationships between the different categories of EPS and share prices were analysed for the period 2005 to 2013. The study concluded that Basic EPS correlated significantly with the changing behaviour of share price.

EPS trends is a significant benchmark for quantifying the growth of an entity (May, 1968). Smart and Graham (2012) concluded that a company's growth rate can be determined by performance indicators such as EPS, which are reported in the financial statements according to the relevant and specific Accounting Standards applied in the respective countries.

It is evident that growth rates in earnings over a period of time can be used as a tool to predict the trajectory of future earnings. EPS thus plays a significant role in investment decision-making by the investors. It also emphasises on Scenario Analysis and Risk Mitigation carried out at the management level. These arguments are noted from (May, 1968) till recent times and noted earlier of Smart and Graham (2012).

Chang, Su, Chen and Chang (2008) also explained that EPS influences share price movements in the long run. Thus, EPS is an indication of the shareholder's wealth; an increase in EPS will definitely increase the value of the share. This has been studied extensively by Mkhonza (2007) and Balsam and Lipka (1998).

It has been observed that there is a positive and strong correlation between EPS and share price movement in a company. The effect of EPS as an independent variable on share price, which is a dependent variable, has been extensively studied for more than three decades now, e.g. Almumani (2014); Chang et al. (2008); Demsetz (1995); Haque & Faruquee (2013); Lev (1989); Menaje (2012); Menike & Prabath (2014); and Sharma (2011).

The relationship between EPS and share price has been studied locally in South Africa by Auret and De Villiers (2000), De Villiers, Hamman, Joubert, and Le Roux (2003), De Wet and Du Toit (2007), and Erasmus (2010). The results show that EPS has a significant correlation with share price movement.

SCOPE AND METHODOLOGY

The scope of this research study includes the Nifty 500 population, comprising 500 companies, during the financial year 2012 to 2017. The source for the data is the audited consolidated financial statements of the companies. The relevant secondary data, which includes five years' observations, have been extracted from the Money Control and NSE database for the period 2012 to 2017. The final data consists of a total of 500 listed companies on the Nifty 500 Index, listed sector-wise in Table 1 and Fig. 1. As indicated earlier, the objective of this study is to identify the relationship between the sectoral constitution of the Nifty 500 population and the 50 top-performing companies under Nifty 500. However, taking a subset of Nifty 500, the study needs to confirm the relationship between the sectoral constitution of the 50 bottom-performing companies and the 50 top-performing companies under Nifty 500. Further, the relationships between the proportional distribution among the sectors within the 50 top-performing companies and that among the 50 bottom-performing companies under Nifty 500 are discussed.

Table 1

Sectors	Sector-Wise (Number of Companies)	Proportion %
Financial Services	74	14.8%
Consumer Goods	69	13.8%
Industrial Manufacturing	44	8.8%
Construction	41	8.2%
Pharma	37	7.4%
Energy	35	7.0%
Automobile	31	6.2%
Information Technology	31	6.2%
Services	31	6.2%
Metals	19	3.8%
Media & Entertainment	17	3.4%
Cement & Cement Products	16	3.2%
Chemicals	14	2.8%
Textiles	14	2.8%
Fertilizers & Pesticides	11	2.2%
Telecom	9	1.8%
Healthcare Services	6	1.2%
Paper	2	0.4%
Total	501	100%

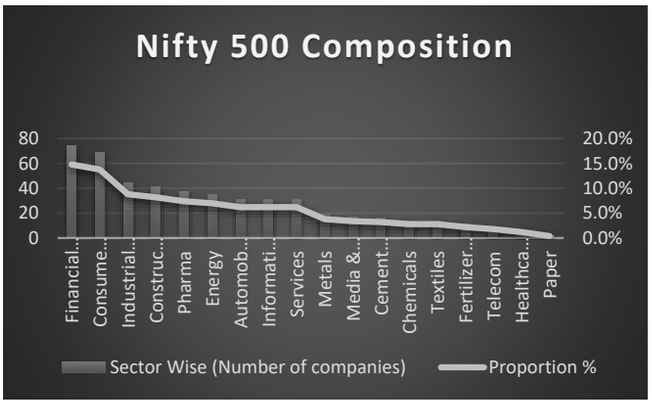

Fig. 1

Empirical data analysis has been carried out using Statistical Package for Social Sciences (SPSS). EPS, as a financial ratio, has been comprehensively used in this study. The financial statements of the selected Nifty 500 companies are used to calculate the relevant financial ratio. The EPS of the companies under Nifty 500 is expressed in terms of growth rate (R), where

R = CAGR, expressed to measure the EPS growth rate of each company under Nifty 500,

Rm = The average of all the EPS growth rates of the Nifty 500 companies, expressed as the benchmark of Nifty 500, and

R-Rm = Deviation between R and Rm.

The primary purpose is to identify the relationship between the sectoral constitution of the Nifty 500 population and the 50 top-performing companies under Nifty 500, considering R-Rm. However, taking a subset of Nifty 500, the study needs to confirm the relationship between the sectoral constitution of the 50 bottom-performing companies and the 50 top-performing companies under Nifty 500. Further, the relationships between the proportional distribution among the sectors within the 50 top-performing companies and that among the 50 bottom-performing companies under Nifty 500 are studied. The approach is to analyse the relationship of the discussed performance of the resembled parameters and to suggest improvements where required.

The following hypotheses were developed:

H1: There is a difference between the sectoral constitution of the 50 top-performing companies and the sectoral constitution of the 50 bottom-performing companies.

H2: There are differences in the internal sectoral proportions of the 50 top-performing companies.

H3: There are differences in the internal sectoral proportions of the 50 bottom-performing companies.

RESULTS

Table 2: Group Statistics

	GRP	N	Mean	Std. Deviation	t-Value	df	p-Value
Deviation(R-Rm)	Top	51	39.028208	27.0708240	41.436	100	.000**
Deviation (R-Rm) (%)	Bottom	51	-223.808796	36.3203975			

Table 3: Independent Samples Test

F		Levene's Test for Equality of Variances		t-test for Equality of Means					
		Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
								Lower	Upper
Deviation (R-Rm)	Equal variances assumed	7.084	.009	41.436	100	.000	262.8370043	6.3431309	250.2524132
Deviation (R-Rm) (%)	Equal variances not assumed			41.436	92.452	.000	262.8370043	6.3431309	250.2398185

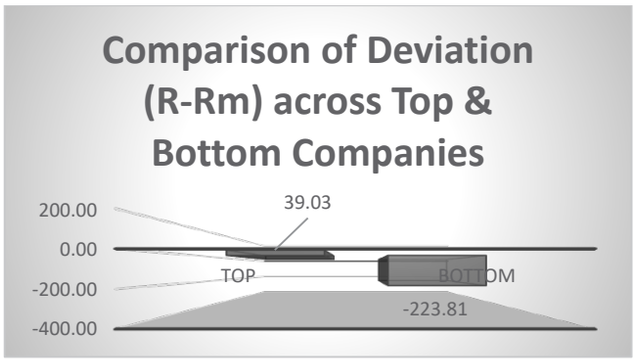

Fig. 2

The sectoral constitution of each of the groups, i.e., 50 top- and 50 bottom-performing companies is significantly different from each other, as the Sig. (2-tailed) value is less than 0.05.

Table 4

	N	Mean	Std. Deviation	df	Mean Square	F-Value	Sig.
Automobile	5	33.3335	12.71458	14	1115.505	1.910	.059*
Chemicals	1	22.2631	.				
Construction	3	77.1940	42.45588				
Consumer Goods	9	30.5486	16.56415				
Energy	4	65.1538	54.47596				
Fertilizers & Pesticides	1	29.1853	.				
Financial Services	4	21.8881	.97989				
Healthcare Services	1	31.5213	.				
Industrial Manufacturing	4	28.6128	6.48696				
Information Technology	5	61.5236	35.26032				
Media & Entertainment	2	41.9340	10.34723				
Metals	1	78.3458	.				
Pharma	3	26.9657	6.52810				
Services	4	31.0283	10.53282				
Textiles	4	24.2053	3.97892				
Total	51	39.0282	27.07082				

Table 5: ANOVA

Deviation(R-Rm) Deviation (R-Rm) (%)					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	15617.072	14	1115.505	1.910	.059
Within Groups	21024.403	36	584.011		
Total	36641.475	50			

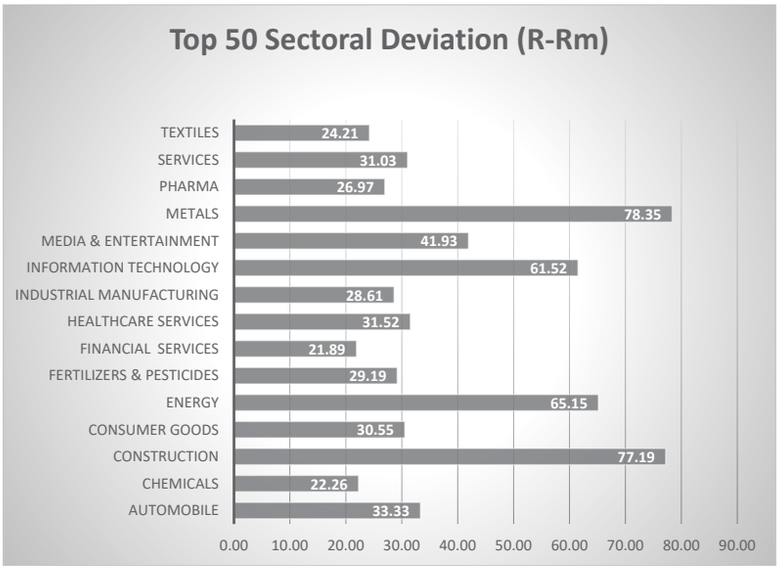

Fig. 3

There is no significant difference among the sectoral proportions of the 50 top-performing companies, as the Sig. (2-tailed) value is more than 0.05.

Table 6

	N	Mean	Std. Deviation	df	Mean Square	F-Value	Sig.
Automobile	3	-248.8080	12.98229	15	2085.241	2.104	.035*
Cement & Cement Products	3	-202.2474	46.23351				
Chemicals	1	-171.3069	.				
Construction	4	-278.5635	51.38315				
Consumer Goods	5	-217.3766	27.50507				
Energy	3	-234.1478	28.32069				
Financial Services	10	-194.6591	16.97588				
Healthcare Services	1	-234.8710	.				
Industrial Manufacturing	5	-230.3084	40.60328				
Information Technology	2	-217.5635	31.89038				
Media & Entertainment	3	-239.5253	18.28514				
Metals	2	-223.0596	17.33520				
Paper	1	-275.0178	.				
Pharma	1	-241.7454	.				
Services	2	-217.7444	61.55095				
Telecom	5	-220.2233	25.26868				
Total	51	-223.8088	36.32040				

Table 7: ANOVA

Deviation(R-Rm) Deviation (R-Rm) (%)					
	Sum of Squares	df	Mean Square	F	Sig.
Between Groups	31278.611	15	2085.241	2.104	.035
Within Groups	34679.953	35	990.856		
Total	65958.564	50			

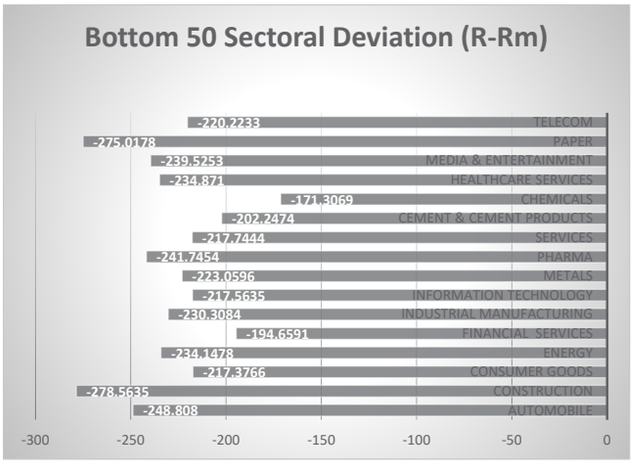

Fig. 4

There is a significant difference among the sectoral proportions of the 50 bottom-performing companies, as the Sig. (2-tailed) value is less than 0.05.

FINDINGS

The results indicate that the sectoral constitution of the 50 top-performing companies under Nifty 500 is significantly different compared to the 50 bottom-performing companies. When we compare the internal sectoral proportions among the various sectors of the 50 top-performing companies, there is no substantial difference among them. However, the internal sectoral proportions among the various sectors of the 50 bottom-performing companies have a significant difference among them.

It has been observed that the sectors among the 50 top-performing companies, which have the least deviation compared to the benchmark of Nifty 500 (Fig. 3), are the sectors with a majority proportion in the Nifty 500 population (Fig. 1). The sectors are textiles, services, pharma, industrial manufacturing, healthcare services, financial services, fertilizers and pesticides, consumer goods, chemicals, and automobiles. The result indicates that Nifty 500 comprises a majority of companies in sectoral investment where volatility is taken care of. Performances closer to the benchmark indicate promising behaviour for investors, where the average returns promised by the Nifty 500 portfolio has always been a priority.

CONCLUSION

A reliable investment portfolio is a requirement for any investor. Though a speculator always aims for high returns, it comes with a lot of risk. Moderate investment behaviour, where the returns are definite, and the volatility of risk and returns is balanced, always reaps gains. The present study identifies the relationship between the sectoral constitution of the Nifty 500 population and the 50 top-performing companies under Nifty 500. The selected data includes the Nifty 500 population, comprising 500 companies, during the financial year 2012 to 2017. The study revealed that the sectors among the 50 top-performing companies under Nifty 500, which have the least deviation compared to the benchmark of Nifty 500, are the sectors with a majority proportion in the Nifty 500 population. The sectors are textiles, services, pharma, industrial manufacturing, healthcare services, financial services, fertilizers and pesticides, consumer goods, chemicals, and automobiles. This behaviour of Nifty 500 supports their target in achieving their benchmark. However, the subsets of Nifty 500, that is, the top 50 and bottom 50 performers, are also confirmed. The statistical results confirmed that the sectoral constitution of the 50 top-performing companies are significantly different compared to the 50 bottom-performing companies. When we compare the internal sectoral proportions among the various sectors of the 50 top-performing companies, there is no substantial difference among them. However, the internal sectoral proportions among the various sectors of the 50 bottom-performing companies have a significant difference among them. This may prompt future researchers to investigate the influence of sectoral performance on Nifty 500.

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