CHAPTER SIX

SUMMARY AND CONCLUSION

6.1 Summary

Investment in various sectors of the economy by different persons (corporate and individuals) is sine qua non for development and growth of any nation. The automobile sector is one such important sector to invest in. Investment decision is an important factor in creation of wealth. The investor decides whether to invest, or hold, or sell. His final decision will be guided largely by the amount and quality of information at his disposal, hence it is commonly said among financial analysts that information is power.

The present thesis titled 'Financial and Stock performance Analysis for Investment Decision-A study of Automobile Sector in India and Japan' is directed to providing information investors require on making investment decisions. Financial information mostly are sourced from data and correspondences made available by different companies, through publication of their business transactions and other activities that lead to generation of revenue and acquisition of assets. This is accomplished by studying the financial statements. Not mere studying, but to analyze the numbers and interpret them; this is the exact attitude of Warren Buffett (2). This involves comparing two sets of figures to determine how they relate or how one influences the other. This is the place of ratio analysis in financial statements analysis.

Different ratios give different information about a firm. Some reveal the financial health and soundness of a firm, some reveal liquidity status, and some reveal prudent and efficient utilization of assets, while others reveal profitability. The test of soundness is determined by Leverage ratios which includes debt-to-equity, debt-to-assets. Measure of liquidity ratios include current ratio, quick ratio; prudent and efficient utilization of assets is revealed by Activity ratios such as inventory turnover, assets turnover; and test of profitability ratios include gross profit ratio, net profit ratio, Return on equity, Return on assets. And other measures that will reveal performance include Earnings per share, dividend per share, dividend payout ratio, Earnings Retention ratio, etc. these ratios and others will surely guide the investor with enough credible information for investment purposes.

The other source of information to be able to assess the performance of firms is their performance at the stock market. It is considered that the value of firms that are doing pretty well in any industry will be revealed by how their stock prices are valued in the capital market, and volatility of the movement of stock prices and how it affects volume traded. If the performances of the firms you intend to invest in at the stock market are monitored over a period of time, trend of performance would be established and informed decision taken; and doing otherwise is tantamount to speculating D'Amalo, 2010(7). The influence of noise, fear and greed at the market and how they affect investors' perception of the companies' performance is crucial in this study.

Many studies Maheshwari, 2015; Popoola, Akinsanya, Babarinde, 2014; Tirkey, Khikhal, 2014; Piotroski, 2000(18, 20, 22, 28) have been undertaken to study the ratios and stock performance in a bid to determine the overall performance of a firm as to guide investors in making their investment decisions.

The present study is a double-barreled one in that it has combined financial statements analysis-using ratios and stock market performance to guide investors accurately in making investment decisions.

These performance indicators are studied in relation to the automobile sector in India and Japan. The automobile sector occupies a prominent place in the economies of the two countries; both of them in Asia. The automotive sector contributes to several important dimensions of nation's building: generating government revenue, creating economic development, encouraging capacity development, and fostering R/D and innovation SGE-JAMA, 2015(121).

In India, the automobile sector, has experienced a remarkable growth in the last two decades, impacting positively on employment generation, improvement in GDP, inflow of needed FDI for expansion of the economy, and other sphere of national economy. This growth of the automobile sector in India is because of massive investment by different entrepreneurs in the different segments of the sector, and as projected by industry watchers, it is expected to grow even more in the years ahead.

The turnover of the sector is more than 45% of the manufacturing GDP of India FY2014. The contribution of the sector to the different segment of national economy is appreciated by the following figures: it contributes 7.5% to GDP; 27% of India's industrial GDP; 4.3% of overall export(second to textiles & handicraft); incremental employment generation in excess of 19 million since FY2006; total investment in excess of US$35 billion – of which US$24 billion is contributed by automobile companies and US$11 billion by automobile components manufacturers; 13% of excise revenue; 8% of the country's R/D expenditures; improvement in fuel efficiency Kearney(122).

Japanese automobile sector as in the other countries has a vast and wide range of related activities that involve materials supply, vehicle production, sales and servicing, etc. The sector in Japan accounts for 8.34% of total employment. It contributes 17.5% to Japan total shipment in 2014 which is a major contributor to the nation's economy. There has been deliberate policy to reduce CO2 emission in the country to enhance the global campaign for climate change. It accounts for 8.2% of total tax revenue in Japan, JAMA, 2015(120). The automobile sector in Japan is projected to grow in size and volume but with fewer number of companies, that individually will turn out to be big conglomerates.

Long term solvency of a firm is very important in the automobile sector to determine the health condition of firms. This has been explained using debt-to-equity and debt-to-assets. It is observed that the Indian automobile companies are more conservative in the use of debt in its capital structure than Japanese automobile companies, and also in financing assets. However, we noted that in the automobile sector, there is need to invest more in their operations- especially in innovations, R/D which prompts the use of more debt as to stay competitive. The Japanese companies are expected to be competitively stronger. Their high use of debt is shown in their cash flow statement as the net cash flow from investment show negative throughout the period. As long as the firms are earning enough income to sustain the debts, they should go for it to stay relevant in the industry. High debt financing of Japanese companies affected their returns (ROE), which is lower than the Indian companies; and also Mazda that employed less debt among Japanese companies has the highest ROE. This is due to interest charges that has to be paid because of debt financing. However, production and sales will be higher for the companies with more debt financing for R/D that will make them stay competitive. Moreover, continue use of equity financing dilutes control thereby affecting EPS and DPS negatively; however level of risk is minimized. But with additional financing of debt sources, control is intact while investors and the company are exposed to higher risk. Both debt and equity financing have their pros and cons and should be used in moderation and depending on the industry.

Liquidity is crucial for survival of companies in most industries, and the automobile sector is one of such industries. The firms in both nations do not possess adequate liquidity to meet the minimum standard, as required of CR and QR. Current ratio minimum is 2:1, and Quick ratio is 1:1. The individual averages CR of Indian firms are Ashok Leyland 1.345; Eicher 1.3191; M&M 1.1445; Maruti-Suzuki 1.5591; Tata 0.704, giving us overall average of Indian firms as 1.17434. And Japanese individual averages of Japanese firms are: Honda 1.213; Mazda 1.22; Nissan 1.41; Suzuki 1.276; and Toyota 1.083, giving us an overall average of 1.2404. This result shows that Japanese firms are marginally above the Indian firms in terms of liquidity, but both countries fall below the acceptable minimum of 2:1. In respect to QR, Indian firms stand as follows: Ashok Leyland 0.6727, Eicher 1.0673, M&M 0.8440, Maruti-Suzuki 1.2636, and Tata 0.499; this gives an overage average of 0.86932. While Japanese firms have the following individual averages Honda 0.0949, Mazda 0.706, Nissan 1.20, Suzuki 1.107, and Toyota 0.9418, leaving us with an overall average of 0.82874. The two countries QR are about the same and still below acceptable limit of 1:1, though two firms in each country had the minimum acceptable. Liquidity therefore, is low in the automobile industry as depicted in this study. . If the inflow of cash is consistent, then a low liquidity will not be a hindrance for meeting short term obligations, but should be high enough to assure investors that there will not be serious default in servicing short-term debts. A company with an impressive and robust earning may not find it difficult to access cheap commercial papers market. The rule in the industry is not high liquidity and not too low liquidity index, what is paramount is a strong earning power. The companies should think towards increasing current assets and reducing current liabilities by prudent assets management.

Efficiency in utilization of firm’s assets is key in the automobile sector. The ratio that is prominent here is the inventory turnover ratio. Revenue of the industry largely depend on sales of the output (vehicles). So, how many times does a company sell and replenish in a year, is a good indication that its products have good share of the market. As far as this barometer is concerned, we need to look for inventory and earnings that are consistently on the rise, it indicates profitability as a result of increase in sales. The ITR of the Indian companies are higher than their Japanese counterparts, but remain unsteady throughout the period of study. It nets in more sale revenue and consequently more profits. However, towards the end, Japanese companies recorded steady increase in their ITR which is as a result of increase in sales figure during the period. Efficient inventory management would improve on the performance of ITR. Rapidity in sales and stock replenishment (purchases) will guarantee steady rise in ITR and marketing functions are tied to this goal.

Profitability of a company is determined by what is left for the owners after settling the outsiders which is represented by the net income. Several variables have been considered in this thesis to determine a firm's profitability, which includes gross profit ratio, net profit ratio, ROE, ROA, EPS, DPR, etc. In the present study, the GPR of Japanese automobile companies are higher than the ones from India, and how this will translate to net earnings will depend on what happens to operating expenditures. The NPR of Indian auto companies proves to be better than the Japanese companies because of higher employment of debts by the Japanese companies in financing their operations. This is revealed in the investment segment of cash flow statement where it showed negative numbers almost the entire period.

As we indicated earlier, ROE is an important indicator to guide investors in their investment decisions; and is noted in this study as such that Indian firms in the study did better than the Japanese firms. The high debt financing by the Japanese firms which resulted in high interest charges might be responsible for this low ROE. This assertion is confirmed in that the only company among the Japanese companies that used less debt financing, also has the highest ROE. Stockholders being the real owners look forward to a better, increased and steady earnings. Earnings per share (EPS), which is also vital to the investors is shown here as revealing positive contribution of debt financing as it is higher for Japanese companies when compared with their Indian counterparts. The logic is that with additional debt financing, the number of equity shares remain unaltered and since more investments attract more income, earnings per unit of share will increase, all other things remaining the same. On other, more issuance of equity increases total number of shares, thereby diluting a compact control of shareholding that will all participate equally on sharing of its income.

The study notes that Indian firms have higher dividend payout ratio than the Japanese firms. The Japanese firms adopt a policy of more retention than dividend payout. Indian firms pay higher and retain less. When more is retained, shareholders wealth is improved than payment of cash dividends, and this is the reason behind the high retention ratio of Japanese firms.

Misstatements occur in financial statements that have far reaching consequences on calculated ratios. Both assets and liabilities are sometimes fraudulently stated in the accounts which will eventually affect results of calculated ratios and may mislead unsuspecting investors when making investment decisions. There are sometimes hidden items in the statements that if revealed many investors will be indifferent as regards such companies' stocks, hence it is important to seek expert advice in this direction, such things as stock valuation, depreciation, etc.

Stock performance of the Japanese firms is more stable when compared with Indian companies. In the case of the Indian firms, the distance between the reversal points is very wide, an indication of long time period of low price before a sudden rise in price. It is easier to predict the future close stock price of Japanese firms than Indian firms. When close prices are high above the roof, should not be the best period to buy, but at the support level which eventually lead to an upswing in price.

There are other variables that are considered by investors before any investment decision is made. This includes the effect of expenditure on R/D, stock buybacks, cash flow, etc. Investors should consider firms with high expenditures on R/D in the automobile sector because they tend to do better as they will have modern technology embedded in their products. Such innovations are sine qua non in the automobile sector. Japanese companies have massive investment in R/D resulting to more innovations of their outputs. R/D is taken very seriously in Japan that most of the companies operate the R/D segment as a full fledge subsidiary of the OEM. Most of them have a combination of development of new technologies and acquisition from other companies having patents to modern technology.

Other aspects of the additional variables being stock buyback is a good indication of a firm having competitive advantage for investment. Firms that are able to 'buy-back' their stock is a good sign that it is doing well and having excess idle cash that should be utilized in profitable projects. In addition, a stable and robust cash flow can take care of so many limitations in an organization, such as reduction of risk of inadequate liquidity.

The happenings in the national economies of the countries are important inputs in deciding whether to invest in companies domicile in them in terms of political stability, fiscal and monetary policies, economic growth, strength of legal institutions, etc. The general view is that unless these factors are considered favourable, investing in such countries would be of high risk.

India stands out as having a stable political system in a democracy that can be trusted and relied upon to boost business; a progressively standard fiscal policies designed over the years to primarily be of benefit to the country, institutions are strong and can be trusted; and economic growth is high at 6% to 7.4%; population of India and the growth of the middle class is a good attraction for investors with assurance of high demands of goods and services.

Japan's economy is the third largest in the world by GDP, fourth largest by purchasing power parity (PPP), and the second largest developed economy. The economy is facing some challenges in terms of growth, now at about 1%, aging population, a huge public debt Govt. of India, 2016(123). The government is pursuing a fiscal policy that will expand the economy on the part of growth and encouraging investors on domestic investments. Another challenge is hostile immigration policy, which if relaxed, should help its aging work-force. The automobile industry is hard hit by this aging population.

India presents a better environment for investment for now when the national economies of the two countries are compared. This accounts for the increase in demand of the Indian auto companies' stocks. This however should not be considered in isolation of the other variables or factors.

6.2 Conclusion and Recommendations

6.2(a) Conclusion

The following conclusions are drawn from the study:

Investment decisions are made after careful considerations of facts and figures that will impact on the outcome of such decisions.
Having adequate information regarding national economies, industries, firms, and stock price movements are sine qua non in making investment decisions, or else we end up speculating.
Financial statements of firms are where most important information of firms are disclosed as depicted in the profit and loss accounts, balance sheet, and cash flow statements.
These financial statements need to be analyzed and interpreted to guide the investors on whether to invest or not.

Ratio analysis, comparative financial statements, establishing trends are necessary tools to analyze and interpret the financial statements.

Ratio interpretation is not done in isolation. A combination of ratios are analyzed and interpreted to be able to properly guide the investor.

Impacts of misstatements in the financial statements and how they affect ratios should not be underestimated. Such misstatements, whether fraudulently or otherwise, will distort results of ratios, their analysis and interpretation

Stock price movement over some period in the past should be able to guide the investor in predicting future prices. It is the opinion of the researcher that volume traded of company's stock reveal so much about the company. A company not doing well will be avoided while deciding to invest. So while considering stock price movements, investors should also consider volume of stock traded over a period of time.

Noise in the capital market plays an important role in price fluctuations and should not be overlooked. Noise traders can dislodge market stability with their activities that may not be backed with adequate and verifiable information. One of such transactions in the morning may push up price temporary until the reason for the rise in price is decoded later in the day. The 'look before you leap' syndrome may be important here.

A combination of fundamental and technical analysis is what an investor needs for investment decision making. These two sources of information should be employed to make effective investment decision, i.e. Ratio analysis and stock performance analysis. They should be used as complementary methods rather than competitive methods.

Automobile sector grows a nation in different aspects in any country, for example in attracting FDI, reduction in unemployment, expansion in foreign trade, growth of GDP, etc.

A firm with low liquidity but having a robust cash flow is likely to be viable for investment, its low liquidity notwithstanding. Therefore, while considering liquidity, it is important to look into other variables that boost cash flow or impede it.

Countries that do not have automobile sector should be spurred by the contributions of the sector and establish same, especially, African countries because of its contributions to national economy.

There is need for high debt financing in the automobile sector because of the high demand in respect of R/D and innovation as to produce up-to-date vehicles with high tech fittings.

The growth indicators in the Indian economy outweighs those of the Japanese economy, which are capable of sustaining investments in other sectors of the economy.

Japanese firms are leading in production outputs over the Indian firms, while the Indian companies have sustained volume of stocks traded over the years; this should be of interest to investors since sustained volume traded is an indication of confidence in a company.

Indian firms pay out more dividends rather than retention as is the case with the Japanese companies.

Closing stock prices affect stock traded at the stock market. Stocks that have stable prices are likely to attract investor's interest, hence volume traded would rise. Investors therefore, should take seriously the volatility of stock prices before investing in the companies.

Stock buybacks is a sign of liquidity and solvency. It is only companies doing well that would accumulate enough undistributed profits that would enable them to have a plan of buying back their stocks. This is good for the shareholders, because it will increase their EPS as a result of reduction in the number of outstanding equity shares.

6.2(b) Recommendations

The following recommendations are made as a result of this study:

Financial statements of a company for some years should be studied and proper analysis made to determine a company's viability in terms of solvency, liquidity, effective management of assets, profitability and returns to shareholders before investing, because vital information concerning a company are disclosed in them;

Adequate information about national economic outlook of a country should be considered in relation to growth potentials, political stability, friendly business environment, sound institutions, etc.;

Adequate information about the industry, the company and price movements should be obtained from all available sources, e.g. Stock Exchanges, credible websites, etc.;

Ratios analysis, comparative financial statements and technical analysis should be employed as important tools in making analysis of a company's status before investment decision. Combination of fundamental and technical analysis should be used as complementary techniques;

A combination of ratios should be analysed to have a comprehensive outlook of a company's status, because a few ratios may be deceitful;

Misstatements in the financial statements could be devastating and distort results of analysis hence should not be underestimated. An expert advice will reduce the danger as a variety of items are involved;

A study and analysis of stock price movement over some period will be necessary, so that a trend could be established and future price predicted with some level of accuracy. So while considering stock price movements, investors should also consider volume of stock traded over a period of time. Rising volume traded could be a sign that the company is doing well and attractive to investors and vice versa;

The effect of Noise trading should be considered while looking at stock price performance so that the investor is not misled by its impact;

Considering the contributions of the automobile sector to an economy as highlighted in this study, other countries should think of establishing automobile industry, especially African countries;

Firms in the automobile sector should employ more debts in financing as to stay competitive in terms of R/D and innovations that are necessary in the industry which will eventually increase output, market share, returns to shareholders in terms of EPS, while still holding to control;

Investors should invest in a company even with low liquidity, if the cash flow is robust; this will guarantee availability of cash at short notice from short term creditors;

The Indian economy looks more favourable for investment at the meantime, hence investors are advised to invest in the Indian companies;

In most cases, companies with policy of stock buybacks are looked at as having a strong financial base, hence such companies should be given priority where they exist in the industry;

A stable dividend policy that guarantees steady dividends but having higher percentage of available profits as retention should be adopted by management to grow shareholders' wealth.

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6.3. Prospects for further studies

Misstatements in financial statements and how they affect financial performance analy,sis for investment decisions.

Financial performance analysis in the automobile industry compared with financial performance analysis of oil and gas industry.

The rising profile of 'Noise' as a determinant of investment decision making.