NWU POTCHEFSTROOM Business School

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NOORDWES-UNIVERSITEIT
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I hereby declare that the assignment which I herewith submit to the North-West University as partial completion of the requirements set for the MBA degree, is my own work.

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1. Executive summary

The Netcare (JSE:NTC) is one of the listed companies on the JSE and it is estimated that it has a market capitalization of R 49 billion. Netcare is ranked as South African's most empowered company in the healthcare sector, and 16th overall on the JSE, also in 2016 Top 100 most empowered JSE listed companies Report.

Netcare was incorporated on South Africa on 28 June 1996 under the name Ablab Designs (Proprietary) Limited. The name has since been changed to Network Healthcare Holdings (Proprietary) Limited on 8 November 1996 and subsequently changed to Netcare Limited (Netcare) in 2008.

In South Africa, Netcare operates the largest private hospital, primary healthcare, emergency medical services and the rental care networks. It is also differentiated by being a leading private trainer of emergency medical and nursing personnel in the country. Netcare's core value is care. From this value flow four others, namely dignity, participation, trust and passion.

2. Business risk and share price risk relationship on a stand-alone basis (Annexure A)

Risk is the likelihood or possibility that something is going to happen whether good or bad. It is therefore important to note that total risk consists of market risk (systematic) and firm specific (unsystematic) risk. Market risk is the risk that affects all players in the market, it is affected by economic fundamentals such as inflation, interest rate, and exchange rate. Market risk is measures by the beta coefficient.

NB

The business risk is defined as "the risk inherent in the operations of the firm, prior to the financing decisions. Therefore, it can be stated that business risk is the uncertainty inherent in the future operating income or earnings before interest and taxes. There are two factors which are the causes of business risk; they are sales variability and operating leverage

When risk was analysed in terms of investing either to Netcare or to the market, it was found that it is actually risky to invest in the market than in Netcare due to high Coefficient of Variance (CV) of the market compared to Netcare. Netcare's CV is 1.87 whereas the market CV is 5.89 **(Annexure A)**

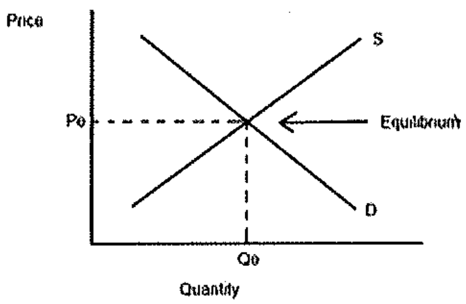
nope incorrect.

Stand-alone risk situation

Stand - alone risk is defined as a situation whereby an asset is considered in isolation. In the stand-alone risk situation (Annexure A) the netcare expected return was calculated to be 13.58% its CV was calculated to be 1.87 and the standard deviation was calculated to be 25.39. Whereas, in the market stand-alone situation the expected return was calculated to be 10.68% its CV was calculated to be 5.89 and standard deviation was calculated to be 7.93 7,93/10,68

Therefore, in terms of investing in a stand-alone situation, it is very risky to invest in the market because it has got a higher CV (5.89) than the Netcare 1.87 CV, one can invest in Netcare because of it is less risky

3. Share price equilibrium



economicsdecoded101.blogspot.com

Market price which is not necessarily equal to equilibrium price.

The share price of Netcare seems to move with the market and the average growth rate of the share price is close to the growth in the CRI (13.58% and 10.68%) Annexure H. However, the share price of Netcare is more preferred than the market capital return growth. Netcare's shares were compared to the movement within the market. Firstly, the Netcare's historical share price growth was compared to that of the market (CRI which was 13.58% and 10.68% respectively (Annexure H). By doing this, equilibrium share price was obtained **(Annexure A)**

The share price can therefore be managed to into equilibrium (ER=RR) through improving the return on assets. Assuming a market rate of return of 15% and comparing it to the expected rate of return of 14%, they are very close

In order to bring the share price into equilibrium relative to its rate of return of 16.13% and the market required rate of 14% the following was calculated: R 29.8= R23.54X(14/29.8) **Annexure A**

4. Five strategy related ratios

4.1 Current Asset Management

Current ratio

Current ratio reflects the relationship between the value of the current assets and extent of the current liabilities of a business. A value less than 1 means your company doesn't have sufficient liquid resources to do this. A ratio above 2 is best.

Netcare LTD (NTC) current ratio between 2016 (1.07) and 2017 (1.06) is satisfactory because it means the business had R 1. 07:1 and R 1.06:1 of current assets available for each R1 of its current liabilities in 2016 and 2017 respectively **(Annexure B).** The industry ratio (Investing.com) is 1.42, which further indicates that current ratio for Netcare LTD (NTC) is satisfactory. In 2014, 2011, 2010 and 2009 the current liabilities were rising faster than current assets hence the value was less than 1 **(Annexure B)**

Quick ratio

The quick ratio (Acid-test) ratio is similar to the current ratio except that it excludes inventory, which is usually the least liquid current asset

Netcare LTD (NTC) quick ratio shows some concerns as it is less than 1**(Annexure B)** and it is less than the industry norm which is 1.4 **(Investing.com).** Netcare LTD (NTC) must therefore, have a look at their inventory levels and debtor's days. As much as inventory has decreased by 3.5% between 2016 and 2017 (**See balance sheet**) it seems that inventory is still too high. The business must make sure that they pay off short-term obligations without relying on sale of inventory.

4.2 Profitability ratio (Annexure C)

Gross profit margin

The gross profit margin indicates how profitable sales have been, it measures the **percentage** of sales Rand remaining after the firm has paid for its good. The higher the gross profit margin, the better.

2012 was not a good year for Netcare LTD (NTC) because they recorded a negative gross profit margin which was -31.5%. **(Annexure C)** Comparing 2016 and 2017, gross profit margin has decreased from 20.3% to 15.2% between 2016 and 2017 respectively **(Annexure C)** this is a concern. This is as a result of decrease in sales between 2016 and 2017 and a subsequent increase in the cost of sales in same period. (See Income statement)

Netcare LTD (NTC) management must try to increase their sales and reduce the cost of sales

Operating profit margin NB variable = measure of operation effectivity

The operating profit margin measures the percentage of each sales Rand remaining after deducting all costs and expenses other than interest and taxes. Like gross profit margin, the higher the operating margin, the better.

Comparing 2016 and 2017, (**Annexure D**) it is clear that there was a sharp decrease on operating profit margin which was 5.56% in 2016 and -4.26% in 2017 respectively. This is a serious cause of concern. The contributing factor might be the decrease in sales between 2016 and 2017(**Income statement**) which was R 3,671,000 or 9.71% and the increase in cost of sales between 2016 and 2017 which was R 7,632,000 or 35.8%.

Netcare LTD (NTC) management must try to increase their sales and reduce the cost of sales

4.3 Debt Management ratios (Risk ratio)

Debt-to- asset ratio

The debt to total assets ratio is an indicator of financial leverage. It tells you the percentage of total assets that were financed by creditors, liabilities, debt.

Between 2016 and 2017, **(Annexures E)** Netcare LTD (NTC) debt-asset ratio was 57% and 52% respectively

In this example, the debt to total assets ratio tells us that on average 54% of Netcare LTD (NTC) assets are financed by the creditors or debt (and therefore 46% is financed by the owners). A higher percentage indicates more leverage and more risk; this is a concern because more than 50% of Netcare LTD (NTC) assets are financed by debt

4.4 Total asset turnover (Asset ratio)

The total asset turnover ratio is one of the many efficiency ratios that allow you to evaluate how well a company is using its assets to generate income. In order to do this, the ratio directly measures a company's net sales against its average assets, by doing this a company is actually determining exactly what percentage of those sales are being produced from each Rand of a company's resources. The higher the ratio is, the more efficiently a company is generating sales from its asset base.

Netcare LTD (NTC) total asset ratio is pretty stable; therefore, there is not concern (See Annexure F) Netcare LTD (NTC) total assets turnover is also more than the industry which is 0.82 **(Investing.com)**

5. Annexures

Annexure A

Current share Price: **R 23.54** (2354/100)

Stand-alone risk for past 10 years

	Company		Market	
Year	Share Price	Share Price Growth	Capital Return Index(CRI)	Capital return growth
2008	0			
2009	R 10.35		25164.04	
2010	R 13.57	31.10%	28433.2	12.90%
2011	R 13.24	-2.40%	30430.19	7.00%
2012	R 18.42	39.10%	35838.04	17.70%
2013	R 23.73	28.80%	43560.22	21.50%
2014	R 32.92	38.70%	50973.86	17.00%
2015	R 37.62	14.30%	49839.64	-2.20%
2016	R 32.81	-12.70%	52380.45	5.00%
2017	R 23.54	-28.20%	55828.58	6.50%
		13.58		**10.68**

Standard deviation of returns over the past 10 years

Year	Share price growth	Average Return			Capital Return Index Growth	Average Return		
	A	B	(A-B)	$(A-B)^2$	D	E	D-E	$(D-E)^2$
2010	31.10%	13.58	17.5200%	306.95	12.90%	10.68	2.2200%	4.93
2011	-2.40%	13.58	-15.9800%	255.36	7.00%	10.68	-3.6800%	13.54
2012	39.10%	13.58	25.5200%	651.27	17.70%	10.68	7.0200%	49.28
2013	28.80%	13.58	15.2200%	231.65	21.50%	10.68	10.8200%	117.07
2014	38.70%	13.58	25.1200%	631.01	17.00%	10.68	6.3200%	39.94
2015	14.30%	13.58	0.7200%	0.52	-2.20%	10.68	-12.8800%	165.89
2016	-12.70%	13.58	-26.2800%	690.64	5.00%	10.68	-5.6800%	32.26
2017	-28.20%	13.58	-41.7800%	1745.57	6.50%	10.68	-4.1800%	17.47
				4512.97				**440.38**
Variance			4512.97/7	**644.71**			440.38/7	**62.91**
Standard Deviation				25.39				7.93
Coefficient of Variation			25.39/13.58	**1.87**			62.91/10.68	**5.89**

Beta Calculation

Year	Share Average return (Y)	CRI Average return (X)
2010	31	12
2011	-2	7
2012	40	17
2013	28	21
2014	38	17
2015	14	-2
2016	-12	5
2017	-28	6

Calculating beta using a calculator:

Enter X values and then Press Input

Enter Y values and then Press ∑+

Press 2nd function then ŶM = -8.46

Press 2nd function then Swap = **2.13** which is beta

Therefore, the regression line equation is -8.46+2.13

P = 0.65

Testing for equilibrium using the SML approach

According to CAPM required return = Risk free +Beta(Market Return-Risk free Return)

Assumptions:

1. Bond SA (Risk Free) = 8%
2. Normal market risk in SA = 6%
3. Beta = 2.13
4. Normal market required return in SA = 15%

Risk free return =YTM	Historical company Beta	Historic Market return	Market Risk Premium
8%	2.13	10.68%	6%

Required rate of return	15%

Expected return on the market = Risk free rate + Market risk premium

= 8% + 6%

= **14%**

From where?

Required rate of return = Risk free rate + Market risk premium x Beta

= 8%+6% x 2.13

= 29.8

Share price where in equilibrium		
Expected return	14%	
Required return	29.8	
Current share price	R 23.54	
Equilibrium share price	R 11.05	14%/29.8x R 23.54

that is for market not for share.

Equilibrium: ER = RR

4. Five strategy related ratios

4.1 Current Asset Management (Annexure B)

Current ratio

The current ratio = Current Assets/Current Liabilities

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
1.06	1.07	1.02	0.97	1.01	1.05	0.88	0.73	0.9	1.0

Quick ratio = Current Asset – Inventory/Current Liabilities

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
0.93	0.94	0.89	0.84	0.87	0.93	0.77	0.64	0.84	0.84

4.2 Profitability ratio (Annexure C)

Gross profit margin = Sales - Cost of goods sold/Sales

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
15.2%	20.3%	25.3%	23.4%	34.37%	-31.5%	23.3%	23.3%	22.9%	22.4%

Operating profit margin = EBIT/sales (Annexure D)

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
-4.26	5.56%	10.66%	9.98%	22.03%	-38.84%	15.84%	16.09%	15.8%	15.1%

4.3 Debt management ratio (Annexure E)

Debt –to-assets ratio = Total debt/Total assets

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
0.57%	0.52%	0.55%	0.56%	0.6%	1.07%	1.06%	1.07%	1.07%	1.06%

4.4 Asset management ratios (Annexure F)

Total asset turnover (Asset ratio)

2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
1.31	1.43	1.26	1.42	1.39	0.66	0.66	0.73	0.75	0.65

Annexure G

Statement of financial position (Balance Sheet) of Class Case										
September	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
	Sept	Sept	Sept	Sept	Sept	Sept	Sept	Sept	Sept	Sept
Equity & Liabilities	R	R	R	R	R	R	R	R	R	R
Equity										
Ordinary Shareholders Interest	R 8 282 000	R 10 177 000	R 10 312 000	R 8 646 000	R 7 160 000	R 1 002 000	R 5 155 000	R 4 157 000	R 4 144 000	R 4 493 000
Outside Shareholders Interest	-R 64 000	R 2 188 000	R 3 325 000	R 2 882 000	R 2 628 000	-R 2 666 000	R 1 886 000	R 1 728 000	R 2 345 000	R 3 714 000
Preference Share Capital	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000	R 644 000
Total Equity	**R 8 862 000**	**R 13 009 000**	**R 14 281 000**	**R 12 172 000**	**R 10 432 000**	**-R 1 020 000**	**R 7 685 000**	**R 6 529 000**	**R 7 133 000**	**R 8 851 000**
Liabilities										
Deferred Tax	R 1 049 000	R 1 207 000	R 1 633 000	R 1 360 000	R 1 129 000	R 3 530 000	R 5 178 000	R 4 430 000	R 5 041 000	R 6 681 000
Long Term Interest Bearing	R 7 232 000	R 6 132 000	R 6 104 000	R 4 939 000	R 5 293 000	R 34 448 000	R 30 425 000	R 25 743 000	R 28 220 000	R 33 184 000
Other Non-current liabilities	R 3 308 000	R 2 822 000	R 892 000	R 569 000	R 405 000	R 337 000	R 332 000	R 331 000	R 459 000	R 217 000
Non-Current Liabilities	**R 11 589 000**	**R 10 161 000**	**R 8 629 000**	**R 6 868 000**	**R 6 827 000**	**R 38 315 000**	**R 35 935 000**	**R 30 504 000**	**R 33 720 000**	**R 40 082 000**
Assets / Utilisation of funds										
Non-Current Assets										
Intangible Assets	R 2 037 000	R 4 256 000	R 4 879 000	R 4 316 000	R 3 873 000	R 5 426 000	R 15 400 000	R 13 484 000	R 14 669 000	R 17 910 000
Investment at market Value	R 596 000	R 547 000	R 536 000	R 363 000	R 271 000	R 129 000	R 122 000	R 117 000	R 111 000	R 68 000
Long Term Loans	R 2 280 000	R 2 017 000	R 2 028 000	R 1 672 000	R 1 281 000	R 1 003 000	R 372 000	R 63 000	R 19 000	R 36 000
Fixed Assets	R 13 908 000	R 14 421 000	R 13 622 000	R 11 504 000	R 10 487 000	R 27 678 000	R 26 416 000	R 23 852 000	R 25 097 000	R 29 732 000
Other Non-Current Assets	R 1 175 000	R 1 373 000	R 1 659 000	R 1 444 000	R 1 274 000	R 2 730 000	R 2 176 000	R 1 472 000	R 1 151 000	R 1 465 000
Total Non-Current Assets	**R 19 996 000**	**R 22 614 000**	**R 22 724 000**	**R 19 299 000**	**R 17 186 000**	**R 36 966 000**	**R 44 486 000**	**R 38 988 000**	**R 41 047 000**	**R 49 211 000**
Current Liabilities										
Trade Payables	R 5 921 000	R 6 017 000	R 6 407 000	R 5 726 000	R 5 145 000	R 4 342 000	R 3 901 000	R 3 118 000	R 2 924 000	R 3 468 000
Dividends Payable	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0
Tax Payable	R 56 000	R 81 000	R 110 000	R 203 000	R 251 000	R 210 000	R 205 000	R 276 000	R 330 000	R 268 000
Short-Term Interest Bearing	R 1 684 000	R 1 391 000	R 2 237 000	R 1 748 000	R 1 264 000	R 2 375 000	R 2 938 000	R 3 945 000	R 1 834 000	R 2 261 000
Bank overdraft	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 1	R 2	R 3
Total Current Liabilities	**R 7 661 000**	**R 7 489 000**	**R 8 754 000**	**R 7 677 000**	**R 6 660 000**	**R 6 927 000**	**R 7 044 000**	**R 7 339 001**	**R 5 088 002**	**R 5 997 003**
Current Assets										
Inventory	R 984 000	R 1 019 000	R 1 107 000	R 987 000	R 920 000	R 817 000	R 721 000	R 652 000	R 621 000	R 638 000
Trade Receivables	R 4 595 000	R 5 030 000	R 5 263 000	R 4 714 000	R 4 107 000	R 3 508 000	R 3 102 000	R 3 354 000	R 3 470 000	R 3 879 000
Cash & Near Cash	R 2 531 000	R 1 980 000	R 2 551 000	R 1 712 000	R 1 686 000	R 2 906 000	R 2 355 000	R 1 378 000	R 803 000	R 1 202 000
Dividends Receivable	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0	R 0
Tax Receivable	R 6 000	R 16 000	R 19 000	R 5 000	R 20 000	R 25 000	R 0	R 0	R 0	R 0
Total Current Assets	**R 8 116 000**	**R 8 045 000**	**R 8 940 000**	**R 7 418 000**	**R 6 733 000**	**R 7 256 000**	**R 6 178 000**	**R 5 384 000**	**R 4 894 000**	**R 5 719 000**
Total Assets	**R 28 112 000**	**R 30 659 000**	**R 31 664 000**	**R 26 717 000**	**R 23 919 000**	**R 44 222 000**	**R 50 664 000**	**R 44 372 000**	**R 45 941 000**	**R 54 930 000**
Total Liabilities	**R 19 250 000**	**R 17 650 000**	**R 17 383 000**	**R 14 545 000**	**R 13 487 000**	**R 45 242 000**	**R 42 979 000**	**R 37 843 001**	**R 38 808 002**	**R 46 079 003**
Total Equity plus Liabilities	**R 28 112 000**	**R 30 659 000**	**R 31 664 000**	**R 26 717 000**	**R 23 919 000**	**R 44 222 000**	**R 50 664 000**	**R 44 372 001**	**R 45 941 002**	**R 54 930 003**
		R 0	R 0	R 0	R 0	R 0	R 0	R 1	R 2	R 3
Net Current Assets	**R 455 000**	**R 556 000**	**R 186 000**	**-R 259 000**	**R 73 000**	**R 329 000**	**-R 866 000**	**-R 1 955 001**	**-R 194 002**	**-R 278 003**

Statement of Comprehensive Income (Income Statement) Class Case										
September	2017	2016	2015	2014	2013	2012	2011	2010	2009	2008
	R	R	R	R	R	R	R	R	R	R
Turnover	R 34 125 000	R 37 796 000	R 33 711 000	R 31 783 000	R 27 801 000	R 25 731 000	R 23 221 000	R 22 474 000	R 23 499 000	R 22 298 000
Cost Of Sales	R 28 944 000	R 21 312 000	R 18 948 000	R 18 227 000	R 15 746 000	R 14 587 000	R 13 513 000	R 12 893 000	R 13 701 000	R 12 842 000
Gross profit	**R 5 181 000**	**R 7 686 000**	**R 8 530 000**	**R 7 443 000**	**R 9 554 000**	**-R 8 095 000**	**R 5 409 000**	**R 5 246 000**	**R 5 387 000**	**R 4 990 738**
Operating / Fixed cost	R 5 419 000	R 4 296 000	R 3 801 000	R 3 224 000	R 2 410 000	R 677 000	R 592 000	R 547 000	R 517 000	R 439 738
Depreciation	R 1 216 000	R 1 290 000	R 1 135 000	R 1 046 000	R 1 020 000	R 1 222 000	R 1 139 000	R 1 083 000	R 1 156 000	R 1 193 000
Operating Profit (EBIT)	**-R 1 454 000**	**R 2 100 000**	**R 3 594 000**	**R 3 173 000**	**R 6 124 000**	**-R 9 994 000**	**R 3 678 000**	**R 3 616 000**	**R 3 714 000**	**R 3 358 000**
Interest & Finance Charges	R 294 000	R 620 000	R 586 000	R 489 000	R 698 000	R 1 966 000	R 1 824 000	R 1 957 000	R 2 398 000	R 2 548 000
Profit before taxation	-R 1 748 000	R 1 480 000	R 3 008 000	R 2 684 000	R 5 426 000	-R 11 960 000	R 1 854 000	R 1 659 000	R 1 316 000	R 810 000
Taxes paid	R 935 000	R 836 000	R 936 000	R 801 000	R 673 000	-R 2 016 000	R 114 000	R 294 000	R 350 000	R 68 000
Profit after taxation / Net Income	**-R 2 683 000**	**R 644 000**	**R 2 072 000**	**R 1 883 000**	**R 4 753 000**	**-R 9 944 000**	**R 1 740 000**	**R 1 365 000**	**R 966 000**	**R 742 000**
Share Price in Cents	2354	3281	3762	3292	2373	1842	1324	1357	1035	
Ordinary Dividends Paid per Share (Cents)	95	95	92	80	67.5	56	53	21	0	0
Preference dividends paid	0	0	0	0	0	0	0	0	0	0
Retained Profits										
Number of Shares issued	1360000	1356000	1349000	1337000	1329000	1317000	1295000	1277000	1266000	1262000