

Valuation of Acta Holding ASA
- A financial service firm with negative earnings

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Executive Summary

This dissertation is an analysis and valuation of Acta Holding ASA. It will be based purely on publicly available information, hence be performed as an external analysis.

Acta Holding ASA is a financial service group providing both corporate and household investors with savings and investment solutions and advisory. Financial service firms offer some challenges in terms of the valuation process when key inputs to the traditional model fail to materialize. Also, the industry tends to be heavily regulated, and the legislations may impose restrictions and inhibit growth, and hence should be incorporated into the value if possible. Due to the financial state of Acta, this valuation encounters further challenges.

The subprime crisis caused a downturn in Acta resulting in negative earnings, which make the estimation of future cash flows difficult. These particular challenges will be the focus of this dissertation, as the knowledge obtained from the valuation process can be just as valuable as the numerical outcome.

To answer the problem statement and to extract the intrinsic value of Acta, a fundamental valuation approach will be performed. This entails an extensive analysis of both the business and its environment, starting with a general introduction, followed by a strategic analysis. This analysis revealed a threatening future for Acta, but also that a strong brand name and further product development can take the edge of the toughest competition. Next, a financial analysis of past performance and risk will be conducted, under the assumption that the past is relevant to the future. The financial analysis revealed a considerable spread in performance, and a company that is clearly suffering from the repercussions of the financial crisis.

With much uncertainty about the future and low correlation with past performance, the foundation for the value estimate and hence the value estimate may suffer from considerable uncertainty. The DCF approach delivered a value estimate of NOK 5,60 per share. But, as the analysis revealed, this estimate cannot be used indiscriminately and is very sensitive to changes in key drivers. The intrinsic value will probably be somewhat lower than NOK 5,60, but it should still exceed the market price of NOK 3,14.

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I would like to give a special thanks to my lovely family who has continued to keep my spirits up and provided me with invaluable support throughout this whole process. I would also like to thank my supervisor, Professor Bernt Arne Ødegaard, who has guided me and whose great knowledge has been an inspiration to me.

Thank you.

Stavanger, June.15th .2011.

Linn Koldal Amundsen

1. Introduction

This first chapter creates the foundation of the actual thesis, where I will give an explanation to why I chose to value Acta Holding, the objective of the thesis, and present a problem statement in order to formulate the goal of the thesis. In the last two parts of the first chapter I will present the limitations and justify the motive behind these choices, and finally present an overview of the structured approach made to answer the problem statement.

1.1. Background

The purpose of this dissertation is to finalize my two year master's degree in economics and business administration. It has been driven by the desire to learn more about the business arena and to be able to explore the practical aspect of the theories that we have been introduced to during my time here at the University of Stavanger.

The choice of both topic and case subject is a personal one, but can also be perceived as a current and relevant issue given the characteristics of the firm. Performing a valuation allows me to combine elements of several subjects I have found interesting and rewarding, and the comprehensive task of valuing a company will contribute to a better understanding of both the industry of choice and a variety of economic theories. The choice of industry was not based on prior knowledge or experience, but rather as an industry worth acquiring knowledge about before entering the competitive world of job searching. Because my specialization here at UiS was applied finance the financing industry was a natural choice.

I chose Acta because I find it to be an interesting case study considering its characteristics, its struggling financial state, and the fact that it's a local contributor located right here in Stavanger. Also, the fact that we find ourselves in a time where many companies are struggling after the financial crisis, makes Acta a good representative of a current and relevant issue.

The complexity regarding valuation of a financial service firm and a firm with negative earnings distinguishes this paper from a traditional valuation approach, and will be assigned a great deal of attention.

1.2. Objective

The main objective of this dissertation is to value the equity in Acta in order to compare the per share value to the per share price of the ACTA stock, on May 31st 2011. Due to certain characteristics of Acta, this dissertation will be awarded a secondary objective as well. The assumption is that the process itself will bring valuable insight into the intrinsic value of Acta, and that the specific issues regarding this case study could not only cause modifications to the traditional model, but also affect the outcome. These objectives should be captured by the following problem statement:

1.2.1 Problem statement

“Will the complex issues regarding valuation of firms in the financial service industry and firms with negative earnings provide further insight into the value of the ACTA stock, differentiating it from the market value provided by Oslo Børs?”

1.3. Delimitations

Valuation is not an exact science and there is a diversity of approaches to choose from, but I will be basing this valuation on a fundamental approach, namely DCF (Discounted free cash flow) valuation. The rationale for this choice will be given in chapter 3.1 *Valuation Techniques*.

This dissertation will only be based on information available to the public, and hence I will be performing the valuation as an external analyst. The data collected and used in this dissertation will be based on six fiscal years, ranging from the year 2005 to the year 2010, but also including 2004 in certain calculations. The rationale for this choice will be given in a subchapter under the *financial analysis*. The rationale for choice of comparable companies in the presentation and in the strategic analysis will be given in their respectable chapters. During the period of analysis Acta's primary source of capital has been common equity. When in need of large capital inputs to finance acquisitions, Acta has reached out to the investors and not the creditors. Because investment in subsidiaries is not a frequent event, this

implies that their current strategy of equity market financing is not an unreasonable approach, or an unreasonable assumption as a sustainable source of capital. The main source of debt financing has been the operational funding through short-term overdraft facilities. Therefore, this dissertation will be based on the assumption that Acta will continue to finance its operations with common equity as its main capital source, and carry no long-term debt.

Many of Acta's direct competitors are just a small part of a large and diversified group, and most of the competitors are not listed at Oslo Børs. Hence they are not required to publish annual reports etc., and information about their business can be hard to come across. Because this dissertation is only based on information that is public, comparative companies are limited. This means that the competitors mentioned in this dissertation is no guarantee that these are the biggest threats to Acta, or the most representative of the industry norm.

1.4. Structure

This dissertation aims to uncover the intrinsic value of Acta, and the assumption is that the true value of the firm is related to its fundamentals and its financial characteristics. Therefore, I will be performing a fundamental valuation, including a strategic analysis, a financial analysis and a prospective analysis. The dissertation will be presented in six parts, starting with an introduction of both the industry and the choice of method used.

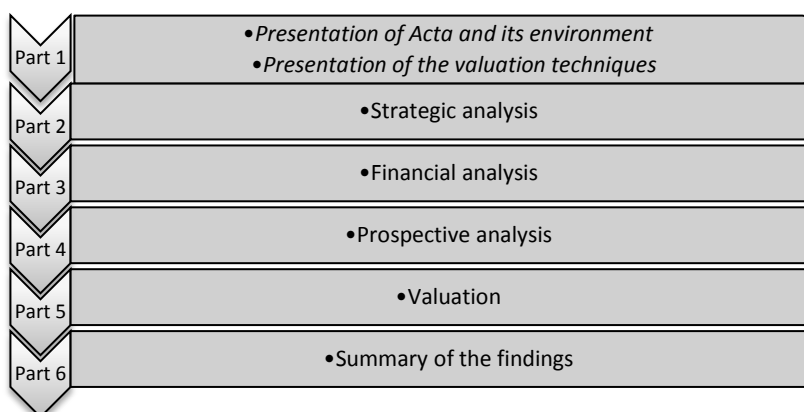


Figure.1: *The structure of the dissertation.*

Part 1

2. Presentation of Acta and its environment

This chapter will be an introduction to the finance sector, a few of Acta's competitors, and Acta itself.

2.1 The Finance industry

Acta Holding ASA belongs, according to the Brønnøysund Register Centre, in sector 490 *Finansielle hjelpeforetak* (Financial aid enterprises), and according to the stock exchange oslobors.no, in the *Finance sector*.

The *financial markets* is a collective designation for all markets for financial assets¹, where the participants range from households to financial institutions and the financial instruments include, among other, marketable securities and money market instruments². I will briefly comment on the financial markets in general before I address the securities market specifically.

Well-functioning financial markets are essential to a modern economy. They contribute to channel savings to investment projects which are assumed to be most profitable, and also allocate risk between parties. In practice, these trades almost always take place via an intermediary such as a bank, insurance company or securities entity such as Acta. The size of the financial sector in relation to the rest of the economy, and the relative importance of different parts of the financial system vary among countries. In regards to financing, a distinction is often made between countries with a bank-based financial system and countries with market-based financial systems, based on how much of their financing companies pick up in the market through the acquisition of equity or the issuance of bonds and certificates, and how much they collect from banks. Norway has a relatively well-developed financial market and range somewhere in between the two³.

¹ <http://www.norges-bank.no/no/finansiell-stabilitet/det-finansielle-systemet-i-norge/finansmarkedene/>

² <http://www.regjeringen.no/nb/dep/jd/dok/nouer/2004/nou-2004-16/13/6/5.html?id=386709>

³ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/2011/nou-2011-1/4.html?id=631165>

Because of the importance of the financial markets on the stability of the national economy, there are statutory regulations and supervision authorities to secure the stability and efficiency in these markets. The regulatory requirements and authorities affecting the business of Acta will be addressed on several occasions later in this paper.

The current market conditions' and the subprime crisis' effect on future development will be covered in the strategic analysis in chapter four.

The securities market in Norway can be divided into the markets for equity, debt and derivatives. The securities market includes transactions made both inside and outside of an organized market, which in Norway is Oslo Børs⁴. Oslo Børs ASA, which was founded in 1819, offers the only regulated market for securities trading in Norway today. To trade on the stock exchange the transaction must go through a securities entity etc. that are members of the exchange and have the necessary trading facilities, see the Exchange Act § 4-1⁵. Similar requirements about qualified intermediaries apply to the trades made outside the stock exchange, where the intermediaries need to be authorized to provide these services.

The terms *securities enterprises* and *investment firms*, referred to in this dissertation are those that provide the same services as Acta. These are mainly investment advice and distribution of investment and savings products. As mentioned, the securities enterprises must have a license to provide investment and savings advice in Norway, and the listings of all the corporations with this license could be found at the web-pages of the FSA (Financial Supervisory Authority).

The general market conditions will be addressed in the strategic analysis in chapter 4.

⁴ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/1999/nou-1999-3/8.html?id=116552>

⁵ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/1999/nou-1999-3/8.html?id=116552>

2.2. Competitors of Acta

Although the finance industry contains a variety of different enterprises, the only ones relevant to this study are those that deliver the same kind of service that Acta does, and are in direct competition with the company. This entails those enterprises offering investment advice and investment products, excluding safe placements like bank deposits, hence traditional banks.

Most of Acta's competitors are not listed at Oslo Børs and are not required to publish annual reports etc., and information about their business can be hard to come across. Because this dissertation is only based on information that is publicly available, comparative companies are limited. This means that the competitors analyzed in this dissertation are not necessarily Acta's greatest competition, or the most representative of the industry norm.

First Securities AS

The group consists of five companies: First Securities AS, First Eiendom AS, First Business Services AS, First Property Fund Management AS, and First Wealth Management AS. The parent company, First Securities AS, is one of the leading securities firms in Norway, with its head office in Oslo. The company also has branch-offices in Stavanger and Bergen. From November 2010, Swedbank AB owns 100 % of the shares in First Securities.

All the subsidiaries offer a full spectrum of services and solutions for institutional and private investors. The unifying aspect of all areas of the organization is that they utilize the firm's investment research expertise when developing products and consultancy services.

First securities investment services range from investment research services, brokerage services, private banking, advice on mergers and acquisitions, and so on. Also, First Securities offer a variety of investment products, ranging from funds, real estate, equities and currency.

Pareto Wealth management AS

The Pareto group is in the business of financial counseling, brokerage of securities, shipping, real estate, insurance, and project and asset management. Pareto is located in Oslo, Stavanger, Bergen, Trondheim, Kristiansand, Bryne, Tønsberg, Hamar, Singapore and New York.

Pareto wealth management, which in 2010 changed its name from the Pareto Universal Funds, sells investment products to wealthy residential customers, small and medium-sized businesses and associations. The core business is also investment advisory and asset management. In 2011, it is decided to merge the company with Pareto PPN, in hopes to become the leading provider of investment advisory and asset management in Norway.

SKAGEN Funds

SKAGEN Funds was established in Stavanger in 1993 and is one of Norway's leading fund managers. SKAGEN Funds invests in undervalued, under-searched and unpopular companies all over the world.

Although SKAGEN, which is primarily a fund manager, differ in some ways from Acta it is still a competitor in that clients can choose to place their funds with SKAGEN instead of Acta. SKAGEN has a leading reputation and is also located in many of the same places as Acta, like Stavanger, Trondheim, Bergen, Oslo, Tønsberg, and Ålesund in Norway. Also, SKAGEN has offices in Stockholm and København.

Investment banks in general and other financial institutions

The traditional banks offer standard banking services and safe placements, whilst investment advisory and risky placements represent only a small part of their business, if represented at all. This makes it hard to separate out the relevant detailed information of the division or subsidiary that is in direct competition with Acta, but it's still important to acknowledge that these institutions represent a direct threat to Acta.

An example is SR-Markets in Rogaland representing one of the largest threats to Acta Stavanger. SR-Markets, as a part of the Sparebank 1 SR-Bank group, represent only a small fraction of the group's business. The securities activities are organized in SR-Markets, and includes customer trading as well as trading at their own account, in interest rates, currency, and other investment management services. The management is mainly organized in a separate subsidiary, SR-Forvaltning.

Some might argue that these institutions represent only a small threat to a securities entity like Acta. Their clients would mostly consist of their bank-clients, and their investment services and products may be limited relative to a specialized institution. For example, face to face advisory and the customized expertise will be less prevalent in the bank offices. Also, an example of the limitations of the products offered, are SR-Markets' funds. They mainly offer stock market funds distributed by ODIN Forvaltning AS, which is a wholly owned subsidiary of the Sparebank 1 group.

Still, as one of the largest providers of banking services in Rogaland, SR-Bank have a large client base and have a well-known reputation in the industry. This might factor in when investors choose the manager of their funds.

Also important is the financial institution **Terra Group**, and the small but not insignificant investment firm **Grieg Investor AS**. Although not presented here, still is considered in the analysis of competitors and industry. For more information about these institutions, please visit their web-sites.

2.3 Acta Holding ASA

Acta was established in Stavanger in 1990 as a distributor of mortgage loans and life insurance products. Today Acta has grown into a large distributor of investment products and services both in Norway, Sweden and Denmark.

Acta is located all over Norway, with some locations being Bergen, Stavanger, Trondheim, Tromsø, Hamar and Oslo, but the company is also well established in Sweden, with their main office in Stockholm.

2.3.1 History

Acta was established in Stavanger in 1990 as a distributor of mortgage loans and life insurance products. During the 1990s the company developed a national distribution network consisting of 10 operative offices, went through a merger and a de-merger, and in the first quarter of 2000 the company started operations in Sweden, with Stockholm as its first office. In 2000 the Acta group was formed.

Acta Bank, Acta Link and Acta Online were launched in the spring of 2001. The company was listed on the Oslo Stock Exchange July 16th, 2001. Difficult market conditions in 2001 and 2002 led to Acta re-establishing a business model focusing entirely on distribution. Acta Real Estate, Acta Bank, Acta Link and Acta Online were sold during 2002 and 2003.

After this Acta offered investment advisory services with a broad range of savings and investment products in Norway and Sweden.

In 2007 Acta had its best year so far. The expansion continued, and Acta opened an office in Copenhagen, Denmark. (This office was liquidated in the first quarter of 2011, but Acta is still operative in the Danish market through a call center located in Stavanger).

New and stricter rules for financial consulting were introduced through the MiFID Directive the same year.

In 2008 Acta was hit hard by negative press coverage in connection with criticism of the distribution of so-called structured products. In addition, the global economy was shaken by a financial crisis not seen since the 1930s. Acta had to adapt to the new regulatory frameworks and undertake a major consolidation of its operations.

In 2009 a new Acta with new management was formed. Acta had used the turbulent period to mark a new course.

2010 was an eventful year, with the main activities being the acquisition of Axir in March, along with an increase of Acta’s share capital the same month.

2.3.2. Corporate structure

The Acta Group consists of the parent company Acta Holding ASA and the fully owned subsidiaries Acta Asset Management AS, Acta Finans AB, Acta Markets AS, Acta Corporate Services AS and Acta Kapitalforvaltning AS, including Acta Kapitalforvaltning AS’s Swedish branch Acta Kapitalförvaltning⁶.

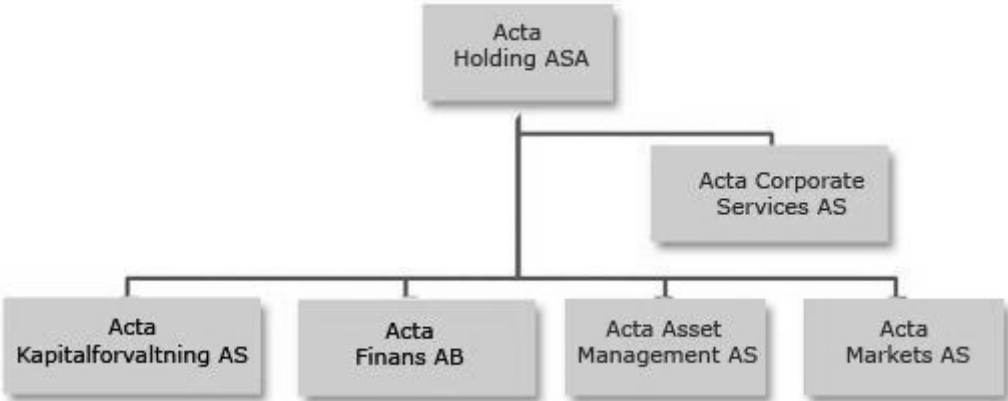


Figure.2: Acta’s organizational chart, where subsidiaries are 100% owned by the parent company Acta Holding ASA.

Source: www.Acta.no

⁶ Acta’s Annual report for 2010.

As this is a valuation of the entire group and the core business of the entity as a whole is the same, a listing of each subsidiary and its activities would be redundant. For a detailed description, see www.acta.no.

2.3.3. Acta's strategy, product and services

Acta's business concept and vision are:

“We will create a leading Nordic financial institution”

“We will give our customers a good return on their investments”

With this as their foundation, Acta will provide neutral advisory and sales, develop good investment products, and create a gathering point for all the trades and reports of their clients and partners. Acta's clients consist of both corporate and household investors and savers.

Services

The core business of Acta is investment advisory and sales. Operations which require licenses from the authorities are carried out by the companies Acta Asset Management AS, Acta Markets AS, Acta Kapitalforvaltning AS and Acta Finance AB.

There has been a major change in the income-structure of Acta's advisory service that is most relevant and important to review.

In 2010 Finanshuset Acta launched what they call a *Portfolio account*. Finanshuset Acta's clients were then given the opportunity to choose a neutral alternative to the traditional transaction based fee structure. By choosing the Portfolio account, clients will pay an annual management fee based on the equity they have under management with Acta. At the same time they will pay lower or no transaction fees. This fee structure is in line with what clients demand and what the regulatory authorities would like the industry to implement. By

launching a Portfolio account, Finanshuset Acta is a neutral and independent supplier of financial advisory services.

The well-known transaction-based services are expected to become a secondary choice for clients as the portfolio account could portray a more investment-neutral and activity-neutral service. For instance, when the investment advisor calls a client with a recommendation for trade, the advisor will no longer be met with the question of whether the motivation behind the call is related to the possibility of charging the client with a transaction fee.

Products

Some of Acta's savings and investment products are mutual funds, private equity, and real estate. The risk-profile of the investments range from one scale to the other, and the horizons are mostly long-term. These and other characteristics will be reviewed in the external analysis addressing the threat of substitutes. Also, an insight into the range of products offered by Acta will be assessed when comparing these to the competitor's products.

A full listing of the products and characteristics would be too extensive and also considered to be unnecessary to include. For a full listing it is therefore referred to Acta's homepage.

2.3.4. Regulatory environment

Acta is an investment advisory company that has a license from the Financial Supervisory Authority to provide investment advice and management.

Acta's business is primarily regulated by *Verdipapirhandelloven* in Norway (the Securities Trading Act). The Securities Trading Act is designed in accordance with the EU directive *Markets in Financial Instruments Directive*, known as MiFID. For a complete listing of the

laws and regulations, I refer to Acta's web page⁷, Finanstilsynet's listings relevant to investment firms⁸, and the complete collection of Norwegian laws⁹.

Acta is also under the supervision of Finanstilsynet, which is “*an independent government agency that builds on laws and decisions emanating from the Parliament (Stortinget), the Government and the Ministry of Finance and on international standards for financial supervision and regulation*”¹⁰, and the corresponding authority in Sweden for its Swedish operations.

In particular, to protect depositors and creditors, financial service firms are subject to capital adequacy requirements, cf. Section § 8-12 of the Securities Trading Act.

To what extent these laws and regulations have an impact on the valuation of Acta, will be reviewed in the section on the *Regulatory Overlay*.

2.3.5. The ACTA stock

The company was listed on the Oslo Stock Exchange on July 16th, 2001, with the ticker ACTA. The shares of Acta Holding ASA are listed on the Main List of the Oslo Stock Exchange (OSE). Since 1 January 2004 the company has been on the Oslo Stock Exchange's OSEBX index. There is only one share class, and each share carries one vote at the company's general meeting.

⁷ <https://www.acta.no/no/Bli-kunde/Trygghet-som-kunde-i-Acta/Kvalitetssikring/Lovverk-og-regler/>

⁸ <http://finansstilsynet.no/no/Verdipapirromradet/Verdipapirforetak/Regelverk/Lover/>

⁹ <http://www.lovdatab.no>

¹⁰ <http://finansstilsynet.no/en/Secondary-menu/About-Finanstilsynet/>

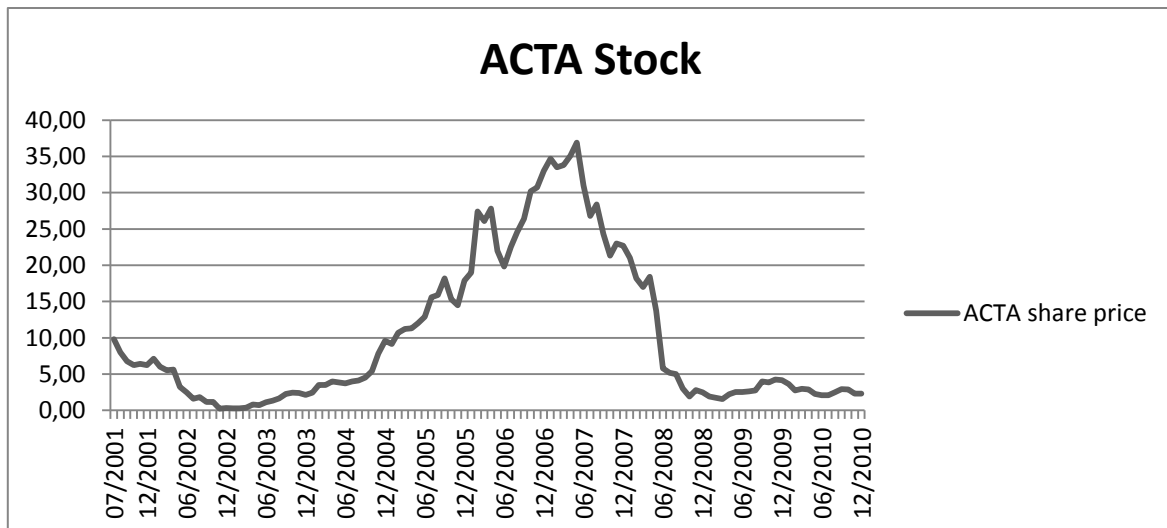


Figure 3: Historical share prices, ACTA stock.

Source: www.oslobors.no, provided by Professor Bernt Arne Ødegaard.

The decline that followed after the IPO may be attributed to the difficult market conditions and the subsequent re-establishing of the Acta business model focusing entirely on distribution. This may appear to have been successful in that the ACTA share peaked in 2006 after a steady rise as of the year 2003. The share has been priced closed to NOK 40, but has since then had a rapid decline due to many isolated incidences which will be discussed later in the section on the financial crisis.

Per May 31st 2011, the share is priced at NOK 3,14. With 257 million shares outstanding the market cap is calculated to be approximately NOK 773 million.

The dividend policy of Acta

“The company aims at the highest possible distribution ratio, where legal requirements and the requirement for financial solidity and liquidity are taken into consideration”¹¹.

¹¹ <https://www.acta.no/en/Investor-Relations/Investor-Relations/Shareholder-Services/Dividend/>

3. The theoretical framework

Because this is a master's thesis and not a business analysis performed by a hired analyst, I choose to include relevant theory on the subject of valuation and the special circumstances regarding this case study. This is not only to illustrate the correct choice of method, but also to shed some light on Acta's situation and the complexity regarding valuation of this particular business. The theoretical framework will primarily be based on insight from Damodaran (2002) and Penman (2010).

There are four general approaches to valuing an asset or a firm¹². Asset-based valuation, discounted cash flow (DCF) valuation, relative valuation and contingent claim valuation. The outcome obtained from these methods may vary, and so the choice is critical. I will here present these methods, along with the theory on valuing financial service firms and firms with negative earnings, and use this insight along with the business characteristics of Acta to make a choice of a valuation technique at the end of this chapter.

3.1 Valuation techniques

In general terms, there are four approaches to valuation: Asset-based valuation, DCF valuation, relative valuation and contingent claim valuation.

3.1.1 Asset-based valuation

Asset-based valuation, including both the liquidation value and the replacement cost approach, is a method based on estimating the current value of the assets owned by a firm. Asset-based valuation is best suited for firms whose assets are separable and marketable, and work best under the assumption that the firm will cease its operations today or in the near future.

¹² Damodaran (2002). p.946.

These characteristics do not apply to Acta, and hence this valuation technique is not suited for the valuation of Acta, cf. the subchapter on the issue of *going concern*.

3.1.2 Discounted cash-flow models

Discounted cash-flow (DCF) valuation is based on discounting future cash flows to arrive at a value of equity or the entire firm.

There are three paths to DCF valuation. One, you can value the equity stake in the business directly. Two, you can value the entire firm, or three; you can value the entire firm in pieces with adjusted present value (APV) valuation. Because Acta is a financial service firm, the best approach is the equity approach, which will be justified and discussed further in chapter 3.2 *issues in valuing financial service firms*.

The value of equity is obtained by discounting expected cash flows to equity at the cost of equity.

$$\text{Value of equity} = \sum_{t=1}^{t=n} \frac{\text{CF to equity}_t}{(1 + k_e)^t}$$

Where,

n = Life of the asset. (cf. subchapter on *Horizon*.)

CF to equity_t = Expected cash flow to equity in period t. (cf. below)

k_e = Cost of equity, i.e., the rate of return required by equity investors in the firm. (cf. subchapter on *Cost of capital*).

The cash flow to equity is the residual claim (i.e., the cash flows after meeting all expenses, reinvestment needs, tax obligations, and interest and principal payments) left over for the shareholders of the firm. This equity cash flow can be either dividends or free cash flows to equity (FCFE).

Dividend discount model

The dividend discount model values the equity by forecasting future dividends, and discounting these dividends at the cost of equity. At first sight this model is very appealing because of the easy concept – we value the stocks by discounting the cash flow from stocks - and the predictability – dividends are usually fairly stable and easy to forecast. But there are disadvantages related to this approach. First, the dividend payout is not directly related to value¹³, and second, the model requires a very long forecasting horizon. The model works best when the payout is permanently tied to the value generation in the firm¹⁴, which in Acta's case could be said to be fulfilled, because of the fixed payout ratio of maximum proceeds¹⁵. Given the infinite forecasting horizon and the overall dividend policy of Acta, the disadvantages of the dividend discount model should be negligible and the model itself should converge on to the free cash flow model.

Still, a closer look at the payout ratio of Acta reveals that it varies and it is not consistent with the EPS: The maximum proceeds policy does not imply a hundred percent payout-ratio.

Payout-ratios	2004	2005	2006	2007	2008	2009	2010
EPS	0,95	1,86	2,67	3,15	0,44	-0,14	-0,07
Dividends	1,25	2,0	2,65	2,55	0,0	0,0	n/a
Payout ratio	131 %	107 %	99 %	81 %	0 %	0 %	n/a

Table 1: Acta's payout-ratio.

Also, given the fact that Acta is subject to laws and regulations that has an impact on the payout-ratio and that these restrictions are not set for the future, the payout-ratio cannot be expected to be consistent over time, hence the dividend discount model will not be optimal for Acta.

¹³ The firm can borrow to pay dividends, which is not related to their investment or operating activities where value is created. Dividends are distribution of value, not creation.

¹⁴ Penman, 2010

¹⁵ Acta's annual reports state that: *"the company's dividend policy: distributing the highest possible share of net income as a dividend, where legal requirements and the requirements for satisfactory financial solidity and liquidity are taken into consideration"*

The discounted free cash flow to equity model (FCFE)

By discounting the free cash flow to equity at the cost of equity, you get the value of the equity in a firm. This should be a more accurate measure of the returns to stockholders as *the company aims to pay out everything that is left over after meeting all obligations, regulations and reinvestment needs*, i.e., the free cash flow of the firm.

Normally, we would start with net income and convert it to free cash flow by adding back any noncash items like depreciation and amortization, subtracting out a firm's reinvestments needs, adding any increase in non-cash working capital (WC) and also adding the net debt issue. In Acta's case this procedure needs to be modified due to certain aspects of their business.

The modified calculation of Free Cash flow to equity:

$\text{Free cash flow} = \text{Operating Income (OI)} - \text{Change in net operating assets } (\Delta\text{NOA})$
--

The rationale for this will be clear as this chapter comes to an end. The issue of debt in Acta, reinvestment needs and changes in working capital will be addressed in chapter 3.2 *Issues in valuing financial service firms*. The issue of negative earnings will be addressed in chapter 3.3 *issues in valuing firms with negative earnings*.

3.1.3 Relative valuation

In relative valuation, the value of an asset is extracted from the pricing of similar assets in the market. This valuation technique is based on finding comparable assets and standardizing common measures such as earnings or cash flows to be able to say something about one relative to the other, under the assumption that the market is pricing these assets right, on average.

The relative valuation would be a great supplement to the fundamental valuation as it is less time consuming, it does not require much information, and the outcome may provide a different perspective useful to the final conclusion. After a review of the currently listed

financial companies on the stock exchange, I find the special circumstances of Acta and its financial state to be too distinct to be able to extract any reliable information from a relative valuation. The GICS (Global Industry Classification Standard) codes, assigned all companies on the stock exchange based on their line of business, support this assessment. I will therefore not include a relative valuation of Acta in this dissertation on the basis that no comparable value is better than a skewed one.

3.1.4 Contingent claim valuation

The contingent claim valuation approach uses option pricing theory and models to value assets that share option characteristics. This can be options that do not currently produce cash flows but are expected to be profitable contingent on the occurrence or nonoccurrence of an event. The value of such options will not be captured with a traditional discounted cash flow valuation.

This can be a fairly good model when the asset being valued has option-like features and these options can be separated and valued easily. But there is a danger of double-counting these options when this is not the case, and hence is not the optimal model for valuing Acta. However, the relatively new incentive scheme that has been established in Acta where employees are awarded with stock options, are valued using the option pricing model developed by Fischer Black and Myron Scholes. Employee stock options are measured at fair value at the time of distribution, and the calculated value is recognized as a personnel expense, and divided over the period until the employees become unconditionally entitled to the stock options. Hence, the value of the options has been incorporated into the calculation of FCFE by Acta, and will not be valued in this dissertation, under the assumption that these are valued right, on average.

3.2. Issues in valuing financial service firms

Acta provide financial services and distribute investment products to individuals and other firms, and can therefore be categorized as a financial service firm. Further, different categories of financial service firms are based on how they make their money. Acta, as a provider of investment advice and a manager of portfolios for clients, make their money on advisory fees for the advice and management and sales fees for investment portfolios, and can therefore be categorized as a *securities entity* or an *investment firm*¹⁶.

Valuing financial service firms can be a challenge for two reasons. First, defining both debt and reinvestment, two critical inputs to traditional valuation, can be difficult given the nature of the firm's business. Second, financial service firms tend to be heavily regulated, which can affect value through both the measurement of growth and risk, and therefore has to be considered as an addition to the traditional valuation process. I will here address these issues one by one, and base the theory on Damodaran's (2002) chapter on how to value financial service firms.

3.2.1 Debt in Acta

Debt, originally viewed as a source of capital, can take on a different connotation with financial service firms. The funds from an increase in debt are normally used to increase the firm's investments, but for a financial service firm debt can be a source of raw material molded into a new financial product and sold at a higher price to yield a profit. The debt then becomes part of operations and value creation, and not the firm's financing activities.

When debt and debt payments are difficult to identify, estimating cash flows to the firm can be problematic. This suggests the use of equity cash flows instead, valuing the equity directly by discounting free cash flows to equity at the cost of equity.

Acta only provide investment advice and act as an intermediary in regards to financial products, and do not offer financial aid or products itself. The debt in Acta could therefore be categorized as financial – used for financing investment-activities, and not as raw material

¹⁶ (Damodaran, 2002)

used in operating activities. Still, the short-term financing in Acta, which during the years has consisted of overdraft-facilities, will be categorized as operating liabilities. A rationale for this and a further discussion on the categorization of operating and financial activities will be made in the chapter *financial analysis*.

Per day, Acta has no interest-bearing liabilities or long-term debt¹⁷, and the only liabilities found in Acta's balance sheet are related to its operating activities, cf. Appendix "*Balance sheet*". The equity method will therefore be applied, under the assumption that it will yield the same result as the total capital approach, but at a much smaller cost.

$$\text{FCFF} = \text{FCFE} + \text{Interest expense} (1 - \text{tax rate}) + \text{Principal payments} - \text{New debt issues} + \text{Preferred dividends}$$

3.2.2 Reinvestment in Acta

Reinvestments, which consist of net capital expenditures and working capital requirements, may also be defined differently in financial service firms. While a manufacturing firm invests in fixed assets such as goods, plant and equipment and is dependent on continuous investments to be able to grow, a financial service firm invests in intangible assets such as brand name and human capital, and does not have the same reinvestment needs, working capital needs or either needs to the same extent.

Acta has operational rental agreements regarding office premises, IT equipment and office machines, and the capital expenditures consist mostly of upgrades and maintenance towards these assets as well as the occasional investment in subsidiaries and other acquisitions. It is questionable whether the growth in Acta is directly related to these investments, and whether a reinvestment measure based on these capital expenditures will serve its intended purpose and cover the reinvestment needs of Acta. Because growth in Acta, as with other financial service firms, is related to investments in brand name, product research and other intangible assets most likely to be classified as operating expenses, and which could be hard or even impossible to quantify, a reinvestment measure based on the investments from the cash-flow statement and working capital needs from the balance-sheet can skew the estimate.

¹⁷ Acta's Annual report for 2010, and Quarterly report, 1st quarter of 2011.

In regards to growth in earnings, we would usually estimate growth based on reinvestment and the return on these investments. But, a more reliable estimate in Acta's case should exclude the measure of reinvestment and base the growth on historical growth in revenues and operating margins instead. The reason the historical growth will be based on revenues and not earnings, is because revenues proved to be a better and more reliable estimate for historical growth estimates¹⁸. Still, there are some complications to using the historical financial statements as a basis for future estimates, and that will be addressed in chapter 3.3.

Normally we would extract FCFE from earnings by removing the reinvestment needs. But, due to the complications of this measure, the calculation will be based on the historical measure of Net Operating Assets, NOA, instead, along with market and growth estimates regarding this measure. Change in NOA will provide a better estimate of the cash that needs to be set aside for continued operations and investments, instead of the possible skewed estimate obtained from trying to identify and quantify the separate items of capex and working capital needs.

The solution is: Free cash flow = Net Operating Income – Change in net operating assets

In short: $FCFE = OI - \Delta NOA$

And growth in FCFE is calculated from estimating growth in revenues, net operating margins (ROS), and NOA turnover.

3.2.3 The Regulatory overlay

Financial service firms tend to be heavily regulated, which put restrictions on several aspects of their business. In regards to valuation, regulatory requirements affect both risk and growth potential.

¹⁸ Damodaran (2002) p. 277

Acta Holding ASA is subject to capital adequacy requirements on a consolidated basis, cf. Section § 8-12 of the Securities Trading Act¹⁹. On the basis of the capital adequacy requirements, restrictions exist regarding for example the opportunity to transfer funds between companies in the Group. Also, the supervisory authorities put restrictions on Acta's product range and services. For example, in 2008 one of Acta's products, leveraged index products, was prohibited, and as a result, Acta lost a fair amount of income and also received bad publicity in the process. As will be pointed out later in this paper, is the importance of a quality brand name in this industry.

In regards to risk, the regulatory restrictions may change - adding a layer of uncertainty about the future, and this risk can affect the value of Acta. Evaluating the risk factor is not only a question of a possible numerical impact, but also an evaluation of the fundamentals in Acta. Acta has no debt, is not capital-intensive, has a dividend policy that considers the capital adequacy requirements, and exercise active risk management. These factors indicate that they have a solid foundation to cope with changes in both capital requirements and other regulations, hence making the uncertainty of a numerical estimate more invasive than omission of such an estimate. The conclusion is that such changes are sporadic and cannot easily be calculated, and under the assumption that they will not be too severe the structure and risk management in Acta indicate that they should be able to survive any legislative change.

In regards to the second issue, the question is if the regulatory overlay put restrictions on Acta's ability to grow. If so, this will have an impact on the value, and should be embedded in the valuation. Because the subordinated capital in Acta has to fulfill certain requirements, according to the *capital adequacy regulations*, this could in some cases inhibit growth. Assuming that growth in Acta entails continuous development of their brand name and expertise, these investments should be captured by the modified FCFE calculation and the NOA estimates. Assuming that these investments are regular and of no monetary significance, relatively speaking, the regulations should not impair this growth. Including mergers and acquisitions in the growth assumption these have until now been financed entirely through equity issues, and the assumption already made is that Acta will continue to be able to do so in the future. Of course, Acta can still and probably will, encounter specific situations where

¹⁹ Acta's Annual reports, under capital adequacy requirements

these restrictions may hinder an acquisition or slow down investments, but it should then be regarded as an exception and it will not be incorporated as a value-reducing quality in this analysis. This is also due to the uncertainties regarding such an estimate.

3.3 Issues in valuing firms with negative earnings

The value of Acta, if based on current earnings, will yield a negative value. This does not necessarily imply that future earnings will be negative and that the value of Acta will be zero to its investors. To address this issue, the first thing to be evaluated and clarified is whether Acta can be valued on a going-concern basis. This will be discussed in section 3.3.1. Then the issue of how to deal with the current financial state in the valuation process will be discussed in the subsequent section.

3.3.1 Going concern

The question of continued operations is a question of the cause of the current problems. Can the negative earnings of Acta be identified as temporary problems, or as long-term strategic problems? If the current level of earnings will continue to persist as a result of long-term strategic problems it is only a matter of time before the company will go bankrupt. A small comment on the cause of the current financial state will be presented here due to its relevance, but a more comprehensive assessment will be performed in the sub-chapter on the financial crisis.

The subprime crisis in 2008 and the recession that followed seem to be the major cause of the negative development in Acta. This statement is backed up by the positive development and growth in income in the preceding years, and the fact that 2007 was the best year in Acta's history. The sudden turnover in the financial statements of 2008 is coherent with the impact of the financial crisis and the firm-specific events of negative press coverage and product restrictions and therefore concluded to be the main events causing the current problems in Acta. This indicates temporary problems, and not long-term problems caused by any strategic or operative mismanagement.

The conclusion of continued operations is reinforced by the documentation of the going concern assumption from both Acta and its auditor, Ernst & Young in the auditor's report of 2010. cf. Acta's Annual report of 2010.

With this said, there may be a possibility that the interim conditions can cause the downfall of Acta. A risk assessment of Acta will be performed in the financial analysis, where the short-term liquidity risk and the long-term solvency risk will be reviewed.

3.3.2 Dealing with the current financial state

The financial statements cannot be used indiscriminately as many of the figures suffer from an abnormal trend. It has already been established that the situation after the year 2007 has been greatly impacted by several temporary and one-time events, causing a downturn in Acta. These events, and the consequences that followed, cannot be expected to be a good foundation for future estimates of normal and recurring value creation.

For example, even though the revenues are not negative, the historical development has been, so a historical growth estimate would yield a negative result. Also, because the revenues have been affected by the recession in the industry, which does not categorize as a normal and recurrent event, these estimates cannot be assumed to be a proper reflection of the future.

As a solution, estimates will partly be based on historical estimates from the normalized financial statements from the year 2005 to 2007, and partly on the figures from the 2010 income statement combined with insight from the strategic analysis performed in chapter 4. This will ensure insight into a normal growth period, which is represented by the 2005-2007 fiscal years, and also provide a current and appropriate base for the future estimates, represented by the normalized fiscal year of 2010. The financial analysis will provide information about historical performance, while the strategic analysis will provide necessary information about the expectations about the future, so that these can be combined and create a solid foundation for the prospective analysis. Normalized figures are those figures that stem

from recurring and normal value creation, which will be discussed in detail in the financial analysis.

The estimated cash flows will, also due to the current financial state, need to be assigned different stages based on growth assumptions. The various stages will be discussed and assigned in one of the subchapters of the prospective analysis, namely *horizon*.

3.4 Rationale for the choice of valuation technique

Acta, despite the current financial situation, will be able to continue its operations, and the analysis should therefore be based on an infinite horizon. Also, the purpose is to find the intrinsic value of Acta and the main approach should therefore be a fundamental one.

The insight sustained in the process of valuation and the outcome of each approach may vary, and because they are not mutually exclusive, this suggest the use of more than one approach to ensure better quality of the valuation. Still, relative valuation, as the only other option, will not be applied due to the lack of qualified comparable companies.

With consistent assumptions about growth and leverage, the firm approach and the equity approach will yield the same result. Because Acta is assumed to sustain its current capital structure, valuating the equity directly will yield the same result as the firm approach, but in a more efficient manner. Because the capital expenditures and working capital needs are not easily extracted from Acta's financial statements, the calculation of FCFE will be extracted from the Operating Income, after subtracting out any change in Net Operating Assets.

The valuation will be based on a DCF approach, discounting free cash flows to equity at the cost of equity.

Part 2

4. Strategic Analysis

A strategic analysis is a part of the fundamental valuation process. This analysis will bring critical insight into the future of the business and make the assessment and estimation of future cash flows possible and more accurate. The strategic analysis is a qualitative analysis of the company's key profit drivers, profit potential and business risk. It will mainly be based on theory from Barney (2007) and Løwendahl & Wenstøp (2003).

4.1 Framework

The strategic analysis will be divided into four sections. First, the internal environment in Acta will be assessed by identifying key resources and drivers, and applying the VRIO framework to assess whether these resources can lead to a competitive advantage. The second section will be an external analysis first reviewing the microenvironment and then the macro environment. Section three will be devoted to the financial crisis. Even though this is a past event, it is an essential part of Acta's current situation and insight into this event may provide crucial information regarding their financial situation and a clue to the where they are headed. Also, it will form a basis for the fourth section which will be an assessment of the overall economy. A summary of the strategic analysis will be performed in sub-chapter 4.6.

4.2 Internal analysis

The purpose of the internal analysis is to assess the strengths and weaknesses of Acta, relevant to the valuation.

First, the key drivers of value that can lead to a competitive advantage needs to be identified. As Acta's vision and mission statement suggests, the goal is to create good investments and attract enough clients and funds to make Acta the leading investment firm in the industry.

The key drivers then are identified as:

Employees: Expertise, in attracting the right suppliers and choosing the right products

Investments: The quality, i.e., the return on the investments.

Products: A good foundation of investment opportunities to ensure that the needs of a diversified investor-market are met.

Service: Good and available service to those that need investment advice.

Brand name: A well-known and good reputation to attract investors

Two of these resources regarding products will be joined under the designation *products* in the analysis.

To assess whether Acta possess these resources and whether the same resources can give Acta a competitive advantage, the VRIO framework will be applied. For a resource to give a sustainable competitive advantage it needs to be **V**aluable, **R**are, **I**mitable and **O**rganized.

Employees

The expertise of the employees is a critical factor in choosing the suppliers and products for the portfolio, and in sales. This expertise is often measured by the educational level of the employees or years of experience from the industry. Acta's group management is listed with their educational level and years of work-related experience in the annual reports and all of their employees are licensed through the qualification test organized by the FSA. To what extent their expertise are superior to others is not possible to quantify or even comment on. But, in regards to the VRIO framework, the employees are valuable in that Acta, with a high level of expertise, will be able to better face threats and explore opportunities in its environment. However, the resource is not rare and it is imitable – higher education is relatively common and the expertise can also be acquired through experience working in the industry. Also, anyone can take the qualification test at the FSA authorizing them to provide investment advice.

Still, it should be mentioned that a competitive advantage due to expertise may be achieved in certain areas. For example, it is a common assumption that a specialized institution like Acta is in possession of greater tailored knowledge and expertise than those institutions, like for example investment-banks, that have a wider focus and are not specifically aimed at the investment market.

Products

The savings and investment products offered by Acta are designed to meet a variety of needs from different investors. The products include investments in real estate, shipping, infrastructure, renewable energy, equity and money-market funds, and insurance funds. The investment horizon along with risk exposure and expected returns vary with each product. Also, Acta pride themselves in staying neutral in regards to products and suppliers, and state that they can choose from a range of suppliers after years in the business.

Some of the competitors only offer products that the company itself or its subsidiaries owns. For example, SKAGEN offers SKAGEN funds and SR-Markets offer its clients ODIN which is owned by the Sparebank 1 group. Also, the variety of risk and return that Acta offer through a variety of products, some competitors cannot deliver. Whether the products of Acta are superior to its competitor's products depends on the risk and returns on these products. Acta use considerable time and expertise in continuous development of their product portfolio; hence there is at least no reason to believe that Acta will be in possession of inferior products, on average.

The products that Acta distribute are valuable, organized and also rare. But the products are not inimitable.

Services

Financial institutions have, in the last couple of years, started to close down offices as they are no longer needed. Banks rely more on their internet services and phone banking. Investors buy stocks and bonds over the internet with the help of automated services and Bank ID. Still,

the service of investor advisory seems to continue to rely a great deal on face-to-face interaction. Many may need to have a picture drawn or just someone real in order to create relations. Acta has offices in many of the biggest cities in Norway, and also a couple of offices Sweden. But so does some of Acta's competitors.

Finanshuset Acta's range of services offered to private investors and corporations comprises investment advice, wealth management, brokerage and online services. Because different investors require different treatment and advice, also imposed by the MiFID directive, Acta has separated services in order to meet the needs of each investor. For example, Acta offer online-services where clients can buy and sell mutual funds online. On the other scale wealth management services are suited for companies and clients with large portfolios, where Acta offer a team of experienced advisors following up investments and help clients reach their investment goals. In addition, they will have access to tax advice, advice from legal experts and insurance advice.

The services of Acta are valuable and organized, bur rare or inimitable they are not.

Brand name

Both products and brands are designed to lure customers from the competition and built to maintain enduring customer loyalty. In order to attract investors the brand name should be well-known, but also based on a good reputation. In Acta's case, the brand name might be well-known in the Norwegian market, but Acta has had its share of bad publicity. This might affect how investors perceive Acta, and it is therefore important that the company develop marketing strategies and other initiatives to come across as a professional institution where the clients' interests are taken care of. Acta's new Portfolio Account, where the company will give their clients the opportunity to choose to deviate from the traditional transaction-based services, is one way of doing so.

The brand name is valuable and *organized*. This is because the brand name creates opportunities in cooperation with renowned suppliers and provides more assets under management through investors, and also as the organization of Acta is tailored to take advantage of these opportunities, it can and will create value. Because it takes a long time to

acquire a good reputation it can be considered as rare, but Acta's brand name is not superior to many of the other investment companies in the market. Names like SKAGEN, Pareto and First Securities are well-known brand names. In the smaller markets, like for example Bergen, a local contributor like Grieg Investor AS has a well-known and good reputation.

Summary of the findings, using the VRIO framework

	Valuable?	Rare?	Inimitable?	Organized?	Competitive Implications
Employees	Yes	No	No	Yes	Parity
Products	Yes	Yes	No	Yes	Parity/ Temporary adv.
Services	Yes	No	No	Yes	Parity
Brand Name	Yes	No	No	Yes	Parity

Table 2: VRIO Framework

Acta is in a state of competitive parity.

4.3 External analysis

The purpose of the external analysis is to uncover the opportunities and threats in Acta's environment. The analysis has been divided into two parts. Acta's microenvironment will be explored using Porter's 5 Forces while the macro environment will be explored using a PESTEL framework.

4.3.1 Acta's microenvironment

The analysis of Acta's microenvironment will be conducted using Porter's 5 Forces. It will provide insight into the industry in which Acta operates and give a perspective on the competitive situation at hand. According to Professor Michael Porter, there are five central forces affecting the growth and earning-potential in any company. These are:

- ✓ Threat of new entrants
- ✓ Rivalry among existing competitors
- ✓ Threat of substitute products or services
- ✓ Bargaining power of suppliers
- ✓ Bargaining power of buyers

These will be examined one by one.

The threat of entry

One threat to the firm's ability to maintain or improve their level of performance may be the threat of new entrants. These are firms that have either recently begun operating in the industry or that threaten to begin operations in an industry soon²⁰.

The financial crisis made this threat smaller when several financial institutions collapsed, and stricter legislation was imposed. It is safe to assume that new entrants would seek high profits and would not enter an industry if there is no potential for superior performance. Under the

²⁰ Barney (2007)

assumption that potentially new entrants are, in the finance industry included, motivated by profits, we should examine the current situation in this market. The macro analysis and the prospective analysis will show that the financial market today is still affected by a high level of uncertainty and the near future does not portray an attractive market for new entrants.

The cost of entry can also be a barrier and will depend on the attributes of the industry's structure. If the cost of entry surpasses the profit from entry, the threat is eliminated. In regards to the finance industry which is not capital-intensive it is more the legislative aspect and supplier access that creates an obstacle, and not so much the initial capital investment. To operate as a securities entity and to be able to legally provide advice to investors the firm needs to be authorized and be registered with the FSA.

One more entry barrier that should be mentioned is reputation, which is one of the key drivers of a securities entity. When handing over their life savings, investors trust that the manager of these funds have both the expertise and determination to manage these properly. A good reputation, or even familiarity and previous relationships can be crucial when picking a fund manager, and entering an industry with this much reliance on a built up goodwill can be a huge barrier.

The threat of new entrants is considered to be moderate, for now. But as Acta begin to show profit and the markets stabilize, the threat of new entrants should increase.

The threat of Rivalry

The intensity of the competition can also affect Acta's future performance. On the cost side, this competition will require efforts like marketing campaigns and continuous product development, rapid competitive actions and reactions, affecting the operating margins. And on the revenues side of it, price war and other customer-friendly measures can put a damper on the income growth.

Factors that determine the level of this rivalry are the number of competitors in the industry, the level of competing firms that are the same size and have the same influence, level of industry growth, and level of product differentiation (Barney, 2007).

The competitive arena of Acta is the securities entities and other providers of savings solutions and investment advice, and there are over a hundred entities with the required license registered with the FSA, in Norway alone. This does not include those entities that are registered as a fund manager, like SKAGEN. The market for financial services has been increasingly internationalized through technological development, the institutionalizing of savings, increased international trade, increased allocation of portfolio allocation and the establishments across national borders. All of these factors have an impact on the competitive situation of the securities markets, but, to operate in the Norwegian market as a securities entity there is still the required license already mentioned, and the number of competitors mentioned should therefore consider most of the threat.

Considering the brand name of competitors, as discussed in the internal analysis, these indicate that Acta is in direct competition with many well-known companies. Still Acta consider themselves to be one of the incumbent providers of investment advisory and products:

“Finanshuset Acta is a leading investment advisory group in the Nordic market, which offers a wide range of savings and investment solutions to private investors and companies”.

Product-differentiation is one of the key drivers that separates and ease the level of rivalry. Still, the threat of rivalry is considered to be high.

The threat of substitutes

The notion of substitutes refers to products or services that meet approximately the same customer needs. First, it is important to identify what products and services Acta offers. Even though the core business of Acta is investment advisory, the investors seeking a securities entity like Acta is basically looking to place their funds. Therefore, a substitute will in this case refer to a substitute investment product.

An alternative placement could either include a different risk profile, a different payoff profile, a different product class or a different product supplier. For example, if an investor

wishes to invest in something outside Acta's portfolio, a substitute product could be a bank-deposit, or perhaps a single share or simply a different real estate market than the one currently being offered by Acta.

A different risk profile may also make the investor choose products outside Acta's portfolio. A risk-averse investor may stick to the safe bank-deposit savings, whilst a more risk seeking and experienced investor may invest in a single stock.

Investors may also choose between different payouts and horizons. Some wish to have regular payouts or at least some level of access to their funds, whilst others may have a longer investment-horizon and may not be too concerned with the regularity of payouts.

Even though the products of Acta's competitors may be of the same nature, they can also vary by supplier. For example, the Norwegian company US Opportunities AS is one of Acta's suppliers offering real estate investments in the U.S. Another real estate product is offered through Boligutleie Holding I AS which provides investment opportunities in the Swedish rental market.

Investors may also make their choice based on the market. For instance, when the market is in a state of uncertainty many investors may prefer to place their money in a safe institutions that guarantees a return. But if risk premiums are high, or the real return is negative due to low interest rates, many investors may turn to the stock market to place their funds.

The level of threat therefore depends on the selection of products that Acta offers and the return on these products. The products should capture the needs of a variety of different investors.

In regards to risk, Acta offer products of high risk like warrants and equity funds, but also products of a less risky nature like money-market funds. In regards to payments, there are products which ensure regular payments, like insurance funds, but also those that vary, like private equity. Most of the products offered by Acta have a long investment horizon, usually five-year or longer.

In broad terms, the only needs that Acta doesn't cover is the needs of a risk-averse investor, namely safe placements. But considering the core business of Acta, which is investment advisory, Acta is not competing for the most risk-averse clients that won't need this kind of advisory. The threat of substitutes therefore, in most part, overlaps with the threat of rivalry, where investors will choose other placements due to credibility and reputation, and not lack of investment opportunities.

This said, without continuous product development product-substitution will become a substantial threat.

The threat of substitute products is considered to be a small.

The threat of suppliers

Acta's suppliers consist of investment product suppliers, external suppliers of supplementary services (legal advice etc.) and suppliers of short-term financing.

The threat of suppliers was one of the most critical factors for many companies during the financial crisis as there was a drought in terms of access to financing. Though the bargaining power of such suppliers normally is considered to be low, the drought and the spread between the key policy rate and the money-market rates at that time proved that under special circumstances this threat is significant. The threat has now been reduced, and in Acta's case who's currently only in the market for short-term financing, this specific threat is considered to be minimal.

As for the other suppliers, the only one worth mentioning is the suppliers of investment products. These suppliers are important to the product portfolio, as mentioned above. Acta claims to have a large network built strong over the past decade. As this market is global a potential threat is considered negligible.

Overall, the threat of suppliers is considered to be small.

The threat of buyers

Acta's buyers are both corporate and household savers and investors. The bargaining power of these investors will depend on several aspects, and the extent to which Acta has to reduce costs or comply with their every demand depend on the level of this power.

The buyers will look for high profit at a low cost, and they will use their bargaining power to achieve this. Such power may depend on the size of the market of potential investors, the cost in switching among suppliers, the level of product customization and differentiation, or even on the size of their engagement.

When it comes to the size of the market of potential savers and investors it may vary with the market conditions, but it cannot be considered as limited and hence be used as a strong bargaining position for the average investor.

To counteract the threat of buyers switching to another supplier Acta can build goodwill in the market and a relationship with their investors. Customer loyalty programs, long-term contracts and long-term investment horizons are helpful tools, but they also need to address the negative media coverage leaving a scratch in their reputation.

The MiFID directive requires the corporation to classify the investors in categories depending on their knowledge, expertise, in which degree the investor is able to handle risk along with other criteria, making sure the investment advice and product recommendations are tailored and suited for this particular client. This, along with the differences in the product origin and supplier in each company, makes the investment advice and products relatively customized and differentiated.

The threat of buyers is considered to be moderate.

4.3.2 Acta's macro environment

The external environment is out of Acta's control, but it is still important to assess this environment to get an idea of how they should relate to their surroundings and also identify possible opportunities and threats. The PESTEL framework has been designed to capture the most important macroeconomic factors. These are: Political, Economic, Sociocultural, Technological, Environmental and Legal.

This analysis will only consider those factors of most relevance to this study, and only factors that are currently changing and are expected to change and therefore may influence the business of Acta in the future. Historical trends are already incorporated and thus not relevant.

The environmental factors will be excluded due to irrelevance in regards to this case study.

Political factors and Legal factors

The political and legal conditions are closely linked and will therefore both be considered in the same section.

The business of Acta is fairly internationalized with offices in Sweden and Denmark, and products like global infrastructure and real estate. Therefore, both the national and international political and legal environment should be monitored closely.

Supply, demand and return on investments are linked to the political stability and legal restrictions abroad. There is nothing to indicate any threats in the political or legal department in the respective areas per day, but there is always that risk. There is however the current global uncertainty regarding the economic development which will be addressed in a subsection about the financial outlook.

In Norway, the general framework and basic regulation of the securities market and its participants must, at all time, comply with the current legislation, cf. www.lovdata.no. The overall responsibility of supervision of the Securities Industry lies with the Ministry of Finance, see the Securities Act § 12-1. The executive and operational authority regarding the

supervision of compliance with the Securities Act is The Financial Supervisory Authority of Norway (FSA)²¹.

The political regime in Norway, as for Sweden and Denmark, is fairly stable, and threats towards the business of Acta due to regulatory amendments should be manageable. The potential effects of such changes in regards to Acta and its business has been considered in chapter 3.2.3 *Regulatory Overlay*.

Economic factors

The most important factors in this category, in Acta's case, are interest rates, inflation and currency rates.

Today the interest rates are historically low and are expected to increase over the next years, cf. figure below.

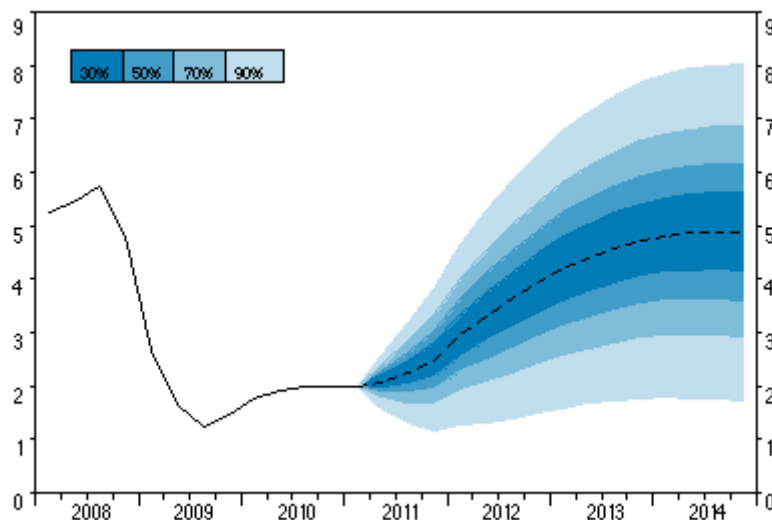


Figure 4: Expected interest rate development in Norway, in percent

Source: www.Norges-Bank.no

The Key Policy Rate will affect the market's interest rates which again will affect the local government and household consumption and investment²². As interest rates increase, local

²¹ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/1999/nou-1999-3/8/2.html?id=351154>

²² <http://www.norges-bank.no/Upload/import/pengepolitikk/rentevirkninger/hoved.html>

government and household investment and consumption tend to decrease, mostly because they have less money left over after servicing their debt which is more expensive due to higher interest rates. Corporate finances are weakened and investment may become less attractive²³. Further, lower demand leads to lower output and employment. Wage growth decrease along with the profit margins. Combined we face reduced inflation.

An increase in interest rates can therefore have a negative impact on the business of Acta. A decrease in corporate and household investment will decrease the business activity and contributions, and at the very least result in less growth. Most likely, the company will face less growth in revenues compared to today's level, followed by a decrease in profit margins due to a relatively high level of fixed costs²⁴.

Acta has in its reports found the strategic risks of a decline in the demand for their products and a reduced profit margin to be two of their main and most threatening sources of future risk. They claim that "The Acta Group has implemented action plans to counteract the negative effects of these risks... and considers the strategic risk factors to be manageable"²⁵. This according to them and without specifying in any detail what these plans are. I find these statements insufficient and without any significant value. Some level of decline in revenue-growth and profit margins can therefore be expected to occur.

In regards to currency changes, Acta has assessed the currency risk as moderated, and has no plans regarding currency hedging at the present time. Should the expected increase in interest rates occur, and this might lead to a weaker Swedish Krone resulting in their operations in Sweden to be less profitable in terms of NOK, the possibility of hedging would reduce this threat²⁶.

The Finance industry is closely linked to the global economy and is affected by the general cyclical movements. A review of the overall economy and its prospects will be added as a supplement to the strategic analysis and devoted a separate section at the end of the external analysis.

²³ <http://www.norges-bank.no/en/price-stability/inflation/effect-of-interest-rate-changes/>

²⁴ Acta's Presentation 1stQ.2011. *Fixed costs relative to total costs.*

²⁵ Acta's Annual report of 2010. *Risk assessment.*

²⁶ The currency risk is mainly linked to the operations in Sweden. The Danish operations constitute a relatively limited share of Acta's total operations.

Sociocultural factors

Sociocultural factors like demographics, educational level and attitudes towards work and leisure, will not affect so much the business of Acta specifically, but rather the general prosperity of our nations. Factors like an increase in the average life expectancy and the annual number of childbirths can influence assumptions about future consumers. A higher educational level in a population can increase the qualified labor, and so on. This should be mentioned as a factor influencing the overall markets, but the uncertainty about a possible effect from sociocultural factors and the extent of such an effect are too uncertain to speculate in. Therefore, the sociocultural environment will be excluded as an influential factor because of expectations about a natural and gradual development.

Technological factors

The market for financial services has been increasingly internationalized, partially through technological development. This internationalization has an impact on the competitive environment of Acta, which has already been addressed in the section on *microenvironment*.

Also, the technological development has made it easier for the industry to communicate with and assist their clients. As an example Acta now assist their clients through different channels according to their client's needs and wants, which also include self-service online. It is crucial for Acta to be a part of this continuous development, and there is nothing to indicate that they won't be. There is reason to believe that such technological development will be a natural part of the company's own development.

Potential sustainable and profitable opportunities from technological advances seems unlikely, in that most of these services are easy to copy and implement.

4.4 The Financial Crisis

This section has been included to shed some light on the specific events causing the downturn in Acta. Questions that will be answered are:

- ✓ How and to what extent did the financial crisis affect Acta and the overall market?
- ✓ Can the financial crisis be identified as the primary cause of the current financial state in Acta?
- ✓ How will future growth be compared to the growth before the crisis occurred?

I have decided to include this section in the strategic analysis because even though historical, it is important to the expectations about- and estimation of future cash flows. Also, insight into the financial crisis is relevant to the next section about current and future markets, which are still colored by the crisis.

First, what is a financial crisis?

Although financial crises have been a reoccurring phenomenon for centuries, there is no single, universally accepted definition of a financial crisis²⁷. It is evident that it has to do with major disruptions in the financial markets and the financial sector, but beyond this the definitions vary. Leaning on the concepts of turmoil, decline and ripple effects, I choose to not make any further attempt to define a crisis, and base this section on the subprime crisis as a benchmark instead.

The cause and the full course of the financial crisis, although important, are too extensive to cover here. I refer to www.regjeringen.no for a full report and analysis, and refrain from including more than what's absolutely necessary to answer the questions above.

The years leading up to the financial crisis showed major growth in revenues and income in Acta's profit statements and 2007 turned out to be their best year so far. The year 2008 started off with optimism, but it quickly turned out to be the most threatening year for Acta's business. In the beginning of 2008 Acta was first introduced to a new regime with the new securities legislation, MiFID. After this the FSA of Norway banned the sale of one of their

²⁷ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/2011/nou-2011-1/4/3.html?id=631168>

most popular products, namely structured products causing a great loss in income. The challenges continued with an on-site review by the FSA and negative media coverage when Acta's founder, owner and board member Fred Ingebrigtsen, was charged for misuse of insider information. Then came the crisis.

The subprime crisis, although commenced some time before, erupted in the fall of 2008, and led to the most severe economic downturn since the 1930's depression²⁸. Despite massive government rescue packages, many financial institutions collapsed. The decline in market-prices inflicted savers and investors huge losses. Distrust between parties and lack of confidence in the overall market made the situation even tenser. As a result, the lending policies of banks became stricter. This again reduced the corporate investments, the household's investments, and so on, reducing the overall activity.

There is a vast difference between nations, to which extent the financial crisis hit. Some countries, like Norway and Canada, seemed to have managed to escape the most severe aspects of the crisis²⁹. Others were not so fortunate. Many of those nations that were hit the hardest had in common a very heavy debt accumulation. This will be addressed in the next section discussing the financial outlook.

The subprime crisis had deep repercussions into the real economy affecting more than just the financial sector. Possibly the greatest risk associated with economic crises is that the population can lose confidence in the society's institutions, organization and governance³⁰. This distrust and turmoil was one of the effects of this crisis causing a decline in market-prices and putting a damper on the distribution and allocation of risk and capital, amongst other. The unemployment rates went up, and the production levels dropped. The corporate and household consumption and investment went down, and the overall growth of the economy stagnated.

Besides the overall pessimism and decline in demand for products and services, Acta was also involved in a specific case regarding the Lehman Brothers. Lehman Brothers Holding Inc., a

²⁸ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/2011/nou-2011-1/4.html?id=631165>

²⁹ <http://www.regjeringen.no/nb/dep/fin/dok/nouer/2011/nou-2011-1/4.html?id=631165>

³⁰ Finanstilsynet's report on the Risk outlook of 2009.

financial firm founded in 1850, and one of Wall Street's investment giants³¹, filed for chapter 11 bankruptcy protection in 2008. In Sweden Acta had marketed and distributed products that contained a bond portion issued by the Lehman Brothers Treasury B.V, whose parent company was now under bankruptcy protection. The products were arranged by Kaupthing Sweden and Acta thus had no direct exposure to Lehman Brothers. The case still put a major strain on the company and the clients involved. The Swedish organization, and Acta allocated over NOK 10 million and several man-years to help affected clients to best safeguard their investments³². In February 2010 it was announced that Acta Kapitalforvaltning and Kaupthing Bank hf. had reached an agreement regarding the bonds, and more than eighty percent of the affected clients accepted this offer from Kaupthing.

Around 450 of the clients complained to Acta Kapitalforvaltning, but the risk of law suit was considered to be limited considering that Acta only was responsible for the provision of advice and this was given on individual basis. As of 31st of December 2010 Acta still had not made any provisions related to this in their accounts. Regarding reputational damage, much of this was covered by the media in 2008, and the extent of this damage today is uncertain.

The financial crisis affected the overall market by putting a damper on growth, and creating an uncertainty in the market making the distribution of risk and capital hard. The demand for financial and monetary products declined. Acta was affected by the overall market conditions, but also by the particular case regarding the bankruptcy. The repercussions of the financial crisis were severe and Acta was hit hard. To what extent the problems and decline in income can be attributed to the financial crisis and not the firm-specific events, is hard to determine due to the overlap of occurrence. This makes the expectation in recovery-time hard to estimate. Reputation is imperative in this industry, and if the negative press coverage and the turbulence in Acta has caused a damage to their reputation, this may result in less growth in the next few years compared to the overall market. The overall growth in the market will be addressed in the following section.

It should be mentioned that the financial crisis also affected the financial markets by imposing new legislations to ensure a more stable financial sector. These legislations however, have been concluded to have a limited effect on Acta in the future, cf. *Regulatory overlay*.

³¹ http://topics.nytimes.com/top/news/business/companies/lehman_brothers_holdings_inc/index.html

³² Acta's annual report, 2009.

4.5 Financial Outlook

Although the external analysis addressed specific macro-economic factors that may pose a threat or be an opportunity to Acta in the future, the overall expectations about future growth and market conditions will be addressed in this section. The insight from this analysis will be a contributing factor to the estimation of future growth in Acta. The facts and forecasts presented in this section will be based on an analysis performed by the FSA on the financial outlook, and the Norwegian National Budget, cf. List of sources.

The global subprime crisis, which started in the U.S., shows how the securities markets in various countries all over the world are intertwined. This makes the current state and the outlook of the general global economy and markets a crucial factor in developing a forecast.

The financial system's function is to redistribute capital and risk and attend to payment and settlement functions. Financial stability, well-functioning markets and confidence in the financial system are important if the system is to function satisfactory³³. This will be an assessment of trends and factors that can create instabilities and what the expectations are about general growth.

Since the second half of 2009, activity in the international economy has been on the rise again after the crisis hit in 2008, but the growth rate slightly declined during 2010 due to a deceleration in the industrial countries. Overall, the growth rate is expected to be somewhat lower over the next two years³⁴.

The global dichotomy is maintained with high growth rates in emerging countries, particularly in Asia, led by China and India, while the growth impulses in the industrial countries are moderate. This is especially true for the heavily indebted euro countries and Japan, while the outlook for several northern European countries is significantly better. Most industrialized countries have not yet reached their production levels of before the financial crisis.

One of the major sources of uncertainty regarding future growth is the debt burden and budget deficits of many euro-countries. In many euro-countries the public debt burden is so heavy

³³ Finanstilsynet's report, *Risk outlook*, 2009.

³⁴ <http://finansstilsynet.no/no/Venstremeny/Finansielt-utsyn/>

that it cannot be maintained for long. Many countries have implemented austerity measures, but the forecasts point to a further increase in the public debt in 2011. It is difficult for the authorities to tighten their budgets significantly without threatening the upturn in the economy. Also, now that the U.S. is introducing austerity measures, the level of the growth of the American economy is also uncertain. Isolated, austerity measures slow down the growth of the economy, but a positive side-effect however, can be an increased confidence in the economic policies of these countries leading to greater corporate and household consumption and investment.

Another significant risk factor is the recent increase in commodity prices. The price of oil, metals and especially the price of food have risen sharply over the last six months. The rise in oil prices should be viewed in the context of the turmoil in North Africa and the Middle East. If the commodity prices continue to stay high, this will dampen the growth among importers who get their terms of trade significantly reduced. Meanwhile, the rise in commodity prices translates into higher overall inflation that can lead to monetary tightening and slower growth.

During the financial crisis, there was a great unrest in the securities markets, with sharp decline in share prices and interest rates. In 2010 the return was again positive in the stock markets. The relatively low returns in the European markets reflects the great economic problems in the region, while the high returns in the Norwegian, and especially in the American markets indicates an increase in expectations for the future economic development. Still, there is a considerable uncertainty regarding this growth due to the uncertainty in future real economic growth and developments in international financial markets. Development in the Norwegian markets for equities, bonds and money market instruments are closely linked with international developments. On average, however, price changes are larger in Norway, which is largely attributable to a less diversified economic structure.

The Norwegian economy was relatively unharmed by the financial crisis. The fall in GDP was small and Norway is one of the few industrialized countries where production in the mainland economy is once again above the level prevailing before the crisis. This must be viewed in light of the Norwegian commodity export structure getting a boost from the strong growth in emerging markets. In addition, the government initiated support and led an expansionary monetary and fiscal policy. A robust and well regulated financial sector also contributed to limiting the negative effects of the global financial crisis.

The Norwegian government has, in its national budget, found it appropriate to keep the spending from the oil-funds unchanged in real terms from 2010 to 2011, which corresponds to a fiscal tightening of 0.2 per cent of trend GDP for mainland Norway. The budget contributes to curbing the growth in activity in the Norwegian economy next year, after two years of strong stimulus through the fiscal policy.

Growth in the mainland economy is now projected to 3.1 pct. this year. In the Revised National Budget the projections was 2.7 pct., which is broadly aligned with the projected average for the next forty years.

4.6 Summary of the strategic analysis

The internal analysis identified the key resources of Acta, and concluded that per day these resources are not sufficient to create a competitive advantage, but rather bring Acta into a competitive parity. There is however, the potential of competitive advantage if Acta is able to strengthen the brand name, or offer products that are superior and inimitable.

The microeconomic analysis found the threat of rivalry to be most significant, but also the threat of new entrants and buyers to be relevant. As a brand name is built stronger, all of these threats can be reduced, but not eliminated. In the second part of the external analysis, the threat of an increase in interest rates was assessed and found relevant to Acta's future. It's expected to cause a decline in Acta's revenue growth and profit margins.

An assessment of past events and future expectations in the two following sections found the economy facing a small decline in overall growth over the next few years. This is mostly due to a high level of uncertainty and debt accumulation in many national economies. The expected growth in the mainland economy in Norway is expected to be 3.1 pct. in 2011.

5. Financial analysis

This chapter will be a quantitative analysis of Acta’s past performance, based primarily on the company’s financial statements, along with financial theory from Palepu (2010) and lecture notes from MØA220³⁵. The purpose of this analysis is to uncover the underlying financial state and risk of Acta, which will, along with the strategic analysis, be the basis for the prognosis developed in the subsequent chapter.

5.1. Framework

The financial analysis will be divided into four steps, and it will be based on the consolidated financial statements listed in the appendix. In the first step an assessment will be made of whether to adjust for possible errors in measurements. In the second step the financial statements will be reorganized in order to prepare the statements for analysis. The third and fourth step will be a comprehensive analysis of past performance and risk.

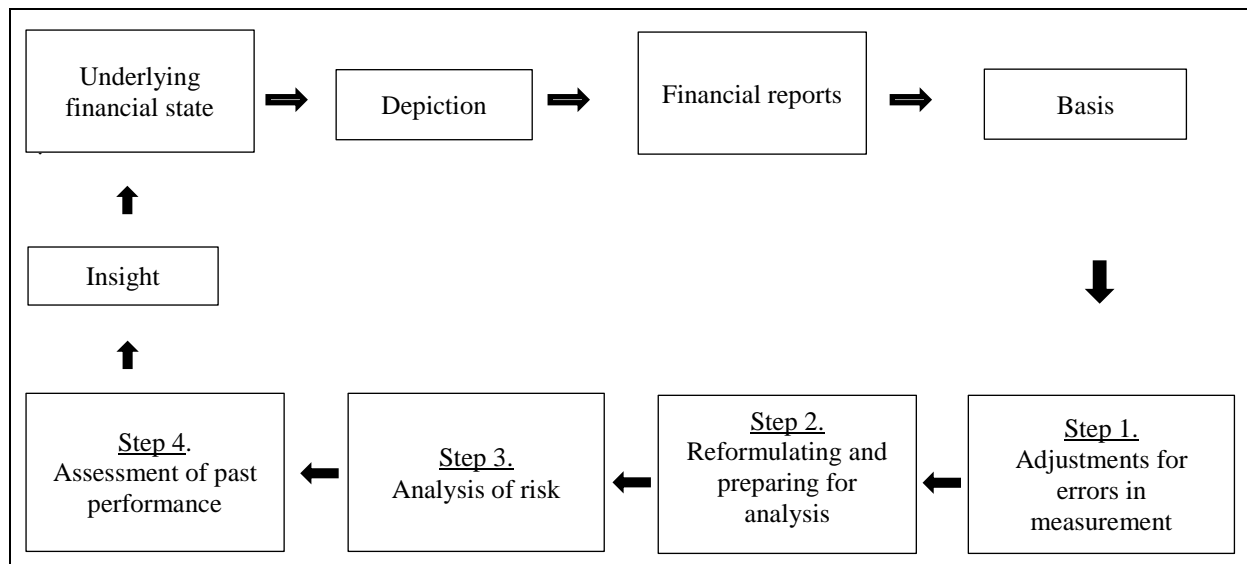


Figure5: Framework: Financial analysis.

Source: Based on lecture notes from the class MØA220

³⁵ MØA220, *Finansiell rapportering og Analyse*. Led by Arnold Drange

5.1.1. Historical Data – Choice of period for the analysis

The length of the annual historical data to be collected depends on the company's stability and structure over time. Acta has gone through changes and restructuring several times during the last decade, which indicates a narrow period of stable reporting and hence a small window of normalized data suitable for analysis.

Even though Acta has been around since 1990, the years leading up to 2003 has been turbulent in regards to restructuring and other major changes, and hence the financial reports as a basis for this analysis, are therefore excluded on this basis. In 2005 the Acta group changed their accounting policies from NGAAP to be in accordance with the International Financial Reporting Standards (IFRS).

Despite the current events influencing Acta's financial reports, a thorough analysis requires updated information and a sufficient number of years to be of any quality. Therefore, I find the reporting periods from 2005 to the year 2010 to be suitable for this analysis, but I will take into account the abnormal trends affecting the statements after 2007. The financial crisis and the negative earnings resulting from this crisis will be addressed and dealt with to make the analysis and the final outcome as accurate as possible.

5.1.4. Level of data collected

The Acta group consists of the parent company Acta Holding ASA and its five fully owned subsidiaries. One of these subsidiaries and a few branches are located abroad. The optimal approach to valuing groups with different operations and operations located under different laws is to value each division separately. With limited time and limited access to the information necessary to perform such a thorough analysis, this analysis will be based on the group as a whole with the consolidated reports as the analytical tool.

5.1.3. Analytical perspective

The purpose of this dissertation is to value Acta Holding ASA and to propose a trading strategy for the Acta stock, which implies the target group to be current and potential investors. Acta's reports are in accordance with the International Financial Reporting Standards (IFRS), and have also been *prepared fairly, in all material respects*³⁶, which indicate a more creditor-oriented configuration of the financial reports with focus on solvency and risk. I will need to assure that these statements reflect the investor perspective before performing the analysis. This entails focusing on normalized value creation and separating operating- from financing activities.

5.2. Presentation of Financial reports

The financial analysis will primarily be based on the company's consolidated income statement and balance sheet for the period 2005-2010. These tables, along with the rest of Acta's financial statements for the relevant period are enclosed in the appendix. The statements are present as raw historical data, with only minor adjustments made to the terminology and classification to make the statements more consistent. The financial figures from 2004, which will be used as a tool in certain calculations, are also enclosed in the appendix.

5.3. Adjustments for errors in measurements

Measurement errors³⁷ should be mentioned as a possible threat to the financial analysis as it can skew estimates, or even make the overall foundation misleading. Still, there are no indications of such errors and hence there is no need for adjustments in this case. The rationale for this is based on the fact that most assets are close to fair value, and there are no indications of creative accounting, cf. auditor's report.

³⁶ Acta's Annual reports: Auditor's Report.

³⁷ Lecture notes. UiS. MØA220, *Finansiell rapportering og Analyse*. Three common errors in measurement.

5.4. Preparing the statements for analysis

The prospective cash flows as a basis for the net present value of Acta will be developed by combining the insight from the strategic analysis and the analysis of past and present financial performance. To be able to analyze past and present performance the financial statements need to be reorganized to portray the sustainable value created by operations.

First, we need to identify the dirty surplus in order to depict the complete income to equity. Dirty surplus is a violation of the accounting principle stating that all income and expenses should be recognized in the income statement. Entries made directly on the equity have been reclassified to distinguish between the transactions with the owners from the comprehensive income. Comprehensive income has been added as a separate line item to the consolidated income statements in the appendix.

To be able to depict the sustainable value generation in Acta we need to separate the normal and sustainable items from the unusual and transitory items. The financing activities and assets should also be separated from the operating activities and assets, seeing that the only activities that generate value are operating and investment activities. In Acta's case the latter can be difficult seeing that it is a financial company. A rationale for some of the classifications will therefore be appropriate.

Bank deposits and marketable securities

Normally these items are investments to store excess cash until it can be invested in operations later, hence classified as financial assets. Still, the same items may be classified as operating assets if they are non-interest-bearing or paid indirectly through the price of goods or services, or used as a buffer to pay bills as they fall due (Penman 2010). Just as a firm needs to invest in plant and equipment to carry out operations, it also has to invest in working cash. Acta is a financial company and operations creating value includes investment advisory and investments in value creating assets. The cash and cash equivalents are used to carry out these operations and pay bills as they fall due: *Bank deposits and short-term investments include bank deposits and government certificates where the purpose is to fulfill short-term*

payment obligations (Annual reports, Acta). The cash and marketable securities are classified as operating assets.

Income accrued from these assets will therefore be classified as operating income.

Overdraft facilities and other short-term debt

The overdraft facilities and other short-term financing are also related to operations in Acta, and hence will be classified as operating liabilities.

Interest expenses accrued from these assets will therefore be classified as operating expenses.

Normalized operating income and Net Operating Assets

Now, the transitory and unusual items must be recognized, and separated from the income statement as they are not relevant for the future. The only non-sustainable items are write-downs and currency translation differences. Also, the overall income statements in the period 2008-2010 are affected by a non-recurring event and should be noted as abnormal.

Transitory items	2004	2005	2006	2007	2008	2009	2010
write-downs	0	-1 250	0	0	-920	-3 523	-1 878
tax on transitory items	0	-352	0	0	-296	-680	-225
Dirty surplus	-750	531	9 373	-7 776	2 796	-339	1 959
Transitory Income	-750	-367	9 373	-7 776	2 172	-3 182	306

Table 3: Transitory items, Acta.

The year 2004 has been included in these tables because the figures from 2004 will be used in some calculations.

Tax allocation	2004	2005	2006	2007	2008	2009	2010
Reported tax	43773	183551	265294	313895	52750	-8691	-2547
28% tax on fin. income	0	0	0	0	0	0	0
Total operating Income	283 315	652 676	936 854	1 106 250	164 174	-45 059	-21 226
Tax on OI	0,15	0,28	0,28	0,28	0,32	0,19	0,12
Average tax							0,247
Average tax Norm.Per.							0,251

Table 4: Tax allocation.

Average tax was calculated based on the period 2005-2010, whilst the *average tax normal period* was calculated based on the normal period of 2004-2007.

The allocation of taxes was performed using the following calculations:

$$\text{Tax on Operating Income} = \frac{\text{Reported Income taxes} - 28\% (\text{NFI b.t.})}{\text{OI b.t.}}$$

Where

NFI b.t. = Net Financial Income before tax

OI b.t. = Operating Income before tax

The tables of the normalized statements are enclosed in the appendix.

5.5. Risk assessment

This subchapter will examine the risk associated with Acta. First, the short-term risk will be assessed when conducting a liquidity analysis. Then, the solvency analysis will identify the long-term risk of Acta.

5.5.1. Liquidity analysis

An analysis of the short-term liquidity risk in Acta will determine if there is a possibility that the company will not be able to pay bills as they fall due. The assessment of the current- and cash ratios will be sufficient in this case.

The current ratio is the key index of a firm's short-term liquidity, and is viewed as sufficient if larger than one. However, this depends on the line of business and maturities and needs to be assessed individually in each case. This ratio will be abbreviated CR1, and measures the current assets to the current liabilities.

The cash ratio, CR2, measures the cash and cash equivalents to the current liabilities, and measures the firm's ability to cover its current liabilities from liquid assets, and hence is a better indication of the risk in case of an emergency.

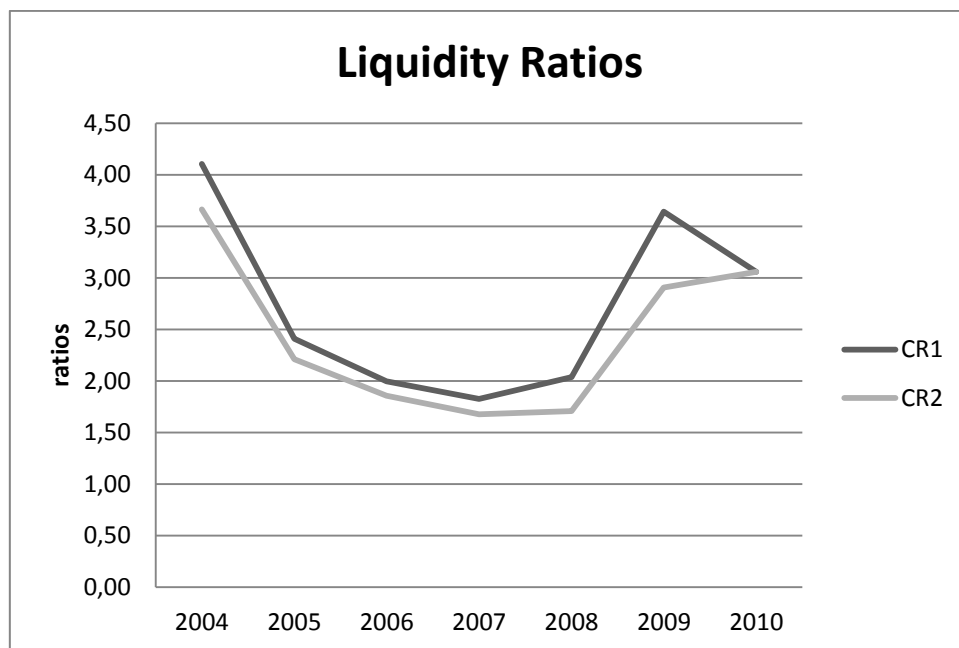


Figure 6: Liquidity ratios of Acta

Both the current and cash ratios have remained sufficient throughout the period, and there is no indications of short-term risk as even the most critical of these ratios, CR2, is above three at the moment.

5.5.2. Solvency risk

This analysis will uncover the long-term risk of Acta and review its ability to withstand any losses.

Normally, this kind of analysis would consider the historical relationship between the debt and equity financing, and address the long-term credit risk. Because Acta has no long-term debt, the focus will be on the capital adequacy requirements instead, where the risk-weighted capital will replace the focus on debt.

The capital adequacy requirements are imposed by law and the consolidated requirements for subordinated capital as of 31 December 2010 were estimated based on the highest of the requirements for securities companies, plus cover for credit risk calculated based on the Group's combined assets. Net equity and subordinated capital was in 2010 estimated at NOK 65 million and showed a surplus of NOK 182 million with regard to the authorities' requirement of 8 per cent of the calculation bases.

Capital Adequacy						
(Thousand NOK)	2005	2006	2007	2008	2009	2010
Capital adequacy, percentage	410,90 %	355 %	284,8 %	162,2 %	183,5 %	159,30 %
Required by authorities, percentage	8 %	8 %	8 %	8 %	8 %	8 %
Subordinated capital surplus	561,2	714,3	850,3	153,2	193,6	182,0

Table 5: Capital Adequacy, Acta.

The required capital adequacy has not only been met, but as the table shows, the margins are well above sufficient, indicating a large enough buffer of risk-adjusted capital.

The risk assessment does not indicate any signs of bankruptcy in the near future. However, this provided that the positive development continue and the assumption about a quick turnaround is met. There are no indications stating otherwise, and so the conclusion stands.

5.6. Analysis of historical performance

The assumption is that the past is relevant to the future, and the insight into historical performance should set the tone for the expectations about future performance.

5.6.1. Historical Cost of capital

The required rate of return will be used as a measure against ROE, to be able to say something about the company's profitability.

All cash flows in this valuation is in nominal terms, after tax, hence the cost of equity will be calculated from nominal after-tax rates.

Risk-free rate

For an investment to be risk free there can be no variance around the expected return or any default risk, which indicates the use of government bonds. Also, there should be no reinvestment risk, advocating the use of a zero-coupon bond with the same duration as the analysis. The cost of equity extracted from this calculation will be used to measure the past annual profitability, and the risk-less rate used here, should therefore be the past annual risk-less rates. The annual nominal Norwegian Inter Bank Offered Rate (NIBOR) for the corresponding year is the best match.

Historical Risk-less rate							
	2004	2005	2006	2007	2008	2009	2010
Rf b.t.	0,022	0,026	0,035	0,053	0,062	0,029	0,030
- 28% tax	0,006	0,007	0,010	0,015	0,017	0,008	0,008
= Rf after tax	0,016	0,019	0,025	0,038	0,045	0,021	0,022

Table 6: Annual nominal NIBOR, after tax. Abbr. Rf.

Source: www.Norges-Bank.no

Market risk premium, MRP

Investment theory is based on the assumption that the marginal investor is risk averse³⁸, and therefore has to be compensated with a risk premium for the non-diversifiable risk undertaken above the riskless investment. The market risk premium could be calculated with the use of models, but none of these models has gained universal acceptance³⁹. Also, in practice the risk premium used is the historical risk premium (Damodaran, 2002).

The underlying assumption when using a historical risk premium is that the risk premium will revert back to the historical norm, and that the time period used is the right norm. The historical risk premium calculated from 1967 to 1994 against the total index at Oslo Børs was 6 percent, on average (Dahl et. al). Seeing that investors are more diversified now because of globalization, there is reason to believe that the risk premium will be below six percent. According to Koller (2010) the market premium varies continually between 4,5 and 5,5 percent.

A historical MRP of 5,5 % will be applied.

Beta, β

The beta measures the volatility, or systematic risk, of a security or a portfolio relative to the market as a whole. The regression beta should be calculated using monthly returns and at least 60 data points⁴⁰, which indicates at least five years of data. Monthly returns are preferred to daily returns because of less noise (standard errors) in the estimate.

The regression beta calculated using monthly returns from 29.03.2006-29.03.2011, on the Acta stock against the Oslo Børs Benchmark Index, OSEBX, was 1,18.

Many analysts adjust the beta according to the Merrill-Lynch method, where it's adjusted to reflect the tendency of the beta to be mean-reverting. This is discussed further in the

³⁸ Damodaran, (2002)

³⁹ (Koller et. Al (2010)) p. 242.

⁴⁰ (Koller et.al, 2010; Gjesdal og Johnsen, 1997)

prospective analysis, for the calculation of future cost of equity, but is not relevant here. This because Acta is currently in a vulnerable state, sensitive to the general economic cycles, and this should be reflected in a higher beta⁴¹.

The historical beta of 1,18 is therefore considered reasonable and will be used in the calculation of the cost of equity.

Liquidity premium

Because investors are risk averse, it could be argued that investors should be compensated for holding assets that are less liquid. Since the OSE in 2004 replaced its previous grouping of companies by line of business with grouping by liquidity, Acta has been in the Match category, which contains the most liquid companies, that also has a minimum of ten trades per day⁴². This indicates sufficient liquidity in the Acta stock, and a liquidity premium will therefore not be included in the cost of equity.

Historical Cost of equity

Cost of equity							
	2004	2005	2006	2007	2008	2009	2010
Risk-less rate	0,016	0,019	0,025	0,038	0,045	0,021	0,022
MRP	0,055	0,055	0,055	0,055	0,055	0,055	0,055
Beta	1,18	1,18	1,18	1,18	1,18	1,18	1,18
Cost of <i>capital</i>	8,1 %	8,3 %	9,0 %	10,3 %	11,0 %	8,5 %	8,7 %

Table 7: Historical cost of equity, Acta.

⁴¹ (Dahl et.al, 1997)

⁴² <https://www.acta.no/en/Investor-Relations/Investor-Relations/Shareholder-Services/Listing-on-Stock-Exchange--Indices/>

5.6.2. Analysis of profitability

A firm's performance can be measured by ROE, the return on equity, which is a comprehensive indicator of how well managers are employing the funds invested by the firm's shareholders to generate returns.

Decomposing the historical ROE

ROA, and in this case also ROE because the operating assets are equal to total equity, can be decomposed into net operating profit margin and operating asset turnover.

Net Operating Profit Margin, or Return On Sales (ROS), which is net profit divided by sales, indicates how much the company is able to keep as profits for each krone it makes.

Asset turnover, which is sales divided by assets, is a measure of how many kroner the firm is able to generate for each krone of its assets.

$$\text{ROA} = \text{ROS} * \text{T.NOA}$$

$$\text{ROA} = \frac{OI_t}{OR_t} * \frac{OR_t}{NOA_{t-1} + (\Delta NOA_t - OI_t) / 2}$$

	2005	2006	2007	2008	2009	2010	Average
OI	470 023	671 560	792 355	112 048	-33 525	-17 026	
OR	1 241 566	1 832 124	2 312 570	988 325	497 832	433 966	
ROS	0,379	0,367	0,343	0,113	-0,067	-0,039	0,363
OR _t	1 241 566	1 832 124	2 312 570	988 325	497 832	433 966	
NOA _{t-1}	434 320	589 381	766 946	884 567	356 992	321 360	
ΔNOA _t	155 061	177 565	117 621	-527 575	-35 632	6 455	
T.NOA	4,48	5,35	5,38	1,75	1,40	1,30	5,07
ROA	170 %	196 %	184 %	20 %	-9 %	-5 %	

Table 8: Historical ROA.

The average ROS and T.NOA is based on the normal period of 2005-2007.

The calculated ROA does not imply whether this return is adequate or not, but by comparing the actual return with the required return we will be able to say something about the firm's performance.

Abnormal ROE

	2005	2006	2007	2008	2009	2010
ROE	170 %	196 %	184 %	20 %	-9 %	-5 %
Cost of equity	8,3 %	9,0 %	10,3 %	11,0 %	8,5 %	8,7 %
Abnormal ROE	161 %	187 %	174 %	9 %	-18 %	-14 %

Table 9: Abnormal ROE

The ROE of the normal period is way above what was expected in the normal period (Marked in grey). The supernormal profitability could have many sources, but it is also possible that the estimates are skewed by for example accounting principles making the quality of the findings questionable. It is therefore important to be critical of these findings. Still, the ROE could be very high due to for example the strong markets that reigned before the crisis, the willingness to invest, and the fact that the business of Acta requires less capital investment to deliver high results compared to a manufacturing firm. This abnormal ROE has to be viewed in conjunction with the threat of new entrants. A ROE this size should attract new entrants pushing the future ROE downwards, assuming that as ROE returns to normal the threat of new entrants should increase. This should be incorporated into the estimates of future revenues.

5.6.3. Growth analysis

Growth is here defined as the percentage increase in an accounting measure from one year to the next. The purpose of this analysis is to review past performance and growth under the assumption that the past is relevant to the future. The basis for this analysis is the normalized statements.

Annual growth	2005	2006	2007	2008	2009	2010
Revenues from sales	87 %	47 %	25 %	-59 %	-48 %	-13 %
Interest Income	122 %	142 %	136 %	18 %	-83 %	-26 %
Total Revenues	87 %	48 %	26 %	-57 %	-50 %	-13 %
Wages and salaries	72 %	57 %	37 %	-46 %	-41 %	-12 %
Depreciations	-5 %	-27 %	12 %	85 %	23 %	-11 %
Other op. expenses	25 %	47 %	25 %	11 %	-31 %	-15 %
Interest expenses	-47 %	-77 %	2119 %	105 %	51 %	-98 %
Operating Exp.	55 %	52 %	35 %	-32 %	-34 %	-16 %
OI	131 %	43 %	18 %	-85 %	-125 %	-53 %
Taxes	320 %	44 %	18 %	-83 %	-115 %	-71 %
Net OI	96 %	43 %	18 %	-86 %	-130 %	-49 %

Table 10: Time Series Analysis.

The percentage growth is the growth in one item compared to the same item the previous year. In terms of growth in revenues from sales the normal period of 2005-2007 show an arithmetic average of 53 percent. The last fiscal year before the crisis had a sales revenue growth of merely 25 percent. It seems as though the growth in both revenues and operating income was moving towards a more sustainable level, as it declined over the period despite 2006 and 2007 being Acta's best years so far. This information is useful when estimating future growth in inter alia revenues.

5.7 Summary of the financial analysis

Even though the strategic analysis portray a firm in trouble, the financial analysis show a diverse picture of the business. Because past performance represented by the normal period could be threatened by the market conditions illuminated in the strategic analysis, it is doubtful that these figures are representable to the future. Also, the abnormal ROE could indicate that the accounting of Acta does not capture the underlying business reality. The findings are questionable and should not be used indiscriminately.

6. Prospective analysis

The purpose of this chapter is to budget future drivers and cash flows. The foundation was created when evaluating past performance in the financial analysis, and the knowledge obtained from the strategic analysis will help build on this.

6.1 Framework

Key drivers will be budgeted in order to be able to create a prospective cash flow. Then the future cost of capital will be estimated, before we move on to the next chapter where these figures will be used as inputs in the DCF valuation model. But first, some refinements are necessary.

6.1.1. Horizon

Seeing as the value that will be compared to the Acta share price of 05.31.2011 has to be the present value at the same point in time, the starting point of the valuation and budgets will be June 1st 2011. This leaves seven months of the first year, which will be referred to as the 2nd half of 2011, or just the *budgets of 2011*. After this, the budgets will be assigned its traditional annual layout. The budgets will be developed for the period 2011- year T. Year T will be the basis for the estimation of the terminal value, indicating that the company will be in steady state at this point.

The length of the budgeting period depends on the maturity and growth of Acta. Because Acta is not yet a company in a mature stage of their business cycle, a longer period till steady state will be in order. But, the budgeting period should be kept under ten years due to too much uncertainty about the far future. Because Acta has got a long way to go before entering a mature state, the longest budgeting period will be applied, hence 10 years. In this case, I will

add two different periods to the budgeting period. Due to the current circumstances in Acta, and the expected change, I will have to add a normalizing period, NP. This will be a period with high growth and stabilization. The rationale for this is that they are already on their way up, and with negative earnings they will have to resolve this situation quickly in order to survive. The second period of the budgeting horizon will be referred to as the growth period, GP, and will be a period of growth and development based on estimates obtained from the financial outlook and the strategic analysis. This period will last until period T, steady state.

NP: 2nd half of 2011- 2015
GP: 2014-2019
STEADY STATE: 2020

6.1.2 Adjustments and assumptions

The assumption made earlier about the issue of going concern will be applied, and this implies that the negative earnings is a temporary situation for Acta. Because the company has to resolve quickly in order to continue its operations, there has been added a period of high growth, called the normalizing period, N.P.

6.2 Budgeting

To be able to develop expected cash flows, the key drivers and growth estimates needs to be budgeted. These drivers are revenue growth, operating margin growth and net operating asset turnover growth.

Operating Revenue

Even though interest income from cash placements etc. can be classified as operating income, the growth in this income should be expected to depend mostly on interest rate changes and not increase in sales. This is because Acta should keep its cash balance at a relatively steady

level as they pay out all excess cash flows as dividend and only hold back enough to cover working cash. But, because Acta’s cash balance is expected to increase along with operations, until it reaches a sustainable level of cash and operating assets, the interest income will grow at a higher rate before depending only on the growth rate of the economy from steady state and out.

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Interest	0,06	0,065	0,070	0,075	0,08	0,074	0,068	0,062	0,056	0,05

Table 11: Expected growth in interest income

As for the recurring revenues, these should show a steady increase going forward as the portfolio account will continue to replace the existing business model, with accretive effect on average recurring fees. This should reduce some risk in regards to future cycles, but otherwise show limited effects on revenue growth. This is because the increase in recurring revenues should be somewhat offset by the decrease in transaction-based income. The operating revenues were growing at 47% and 25% in the two years before the crisis, but this would be an unrealistic expectation today. Given the Q1 2011 report combined with the financial prospects, the expected increase in revenues this year is expected to be 15%, before a steady decrease towards the general growth rate of the economy. The decline in growth is due to factors that have been undergone previously. For example, the financial analysis revealed an abnormally high ROE that will attract new competitors to the arena, reducing overall sales. The strategic analysis supports the expected decline in the growth rate as interest rates are expected to increase, reducing sales and profit margins. The general perception about future long-lasting growth is that this growth is unlikely to surpass the general growth of the economy, leaving the steady state with a growth rate of 5%, given an expected inflation level of 2,5%⁴³ and a real growth rate, measured by expected growth in GDP, of 2,5%.

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
OR growth	0,15	0,14	0,13	0,12	0,11	0,094	0,083	0,072	0,061	0,05

Table 12: Expected growth in revenues from sales

⁴³ <http://www.norges-bank.no/no/prisstabilitet/inflasjon/>

Net Operating Profit Margin, ROS

The historical net operating margins were found when decomposing ROA, but these figures are not useful as a benchmark in this case. The profit margin will, based on the Q1 2011 report and past trends, reach 0,034 in 2011 which is up from the negative margins from last year. It's expected to keep a steady increase during the N.P. period, before a decline over the G.P. period. This is because Acta will first stabilize during the N.P period, before a steady decline towards a sustainable level in steady state. The rationale for the decline, as uncovered in the strategic analysis, is due to factors affecting the market whilst Acta retains a high level of fixed costs.

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
ROS	0,03	0,08	0,13	0,18	0,23	0,21	0,18	0,15	0,13	0,10

Table 13: Expected ROS, Net Operating Margins.

Net Operating Asset Turnover

The historical net operating asset turnover was also found when decomposing operating ROA, but these figures cannot be expected to apply to the post-crisis period either. Because the NOA turnover is a measure of the company's ability to generate revenues per unit of invested capital, it's expected to decrease as the company grows and the revenues are threatened by new entrants, existing competitors and a weaker market. Per 2011 the NOA turnover is expected to reach 1,5. In the N.P. period the NOA.T. is expected to increase and it will reach a maximum of 2,0 in 2015 before a steady decline towards steady state. The spread between the annual NOA.T. should be relatively small when the invested capital will remain fairly stable after the N.P. period because of the aggressive dividend policy and the revenues are gradually and simultaneously affected by less growth.

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
NOA.T.	1,50	1,78	1,85	1,93	2,00	1,92	1,84	1,76	1,68	1,60

Table 14: Expected future NOA turnover

6.2.1 Budgeted financial statements and free cash flows

The Q1 report has been published at www.acta.no, but the rest of the income statement has been estimated based on these figures, past trends, and expectations about growth. Note that the second column is not Q2, but 2nd period of 2011 which consist of two-thirds of one fiscal quarter.

	1 Q2011	2 p.2011E	1st half 2011E	2nd half 2011E	Total 2011E
Revenues	129 600	86 400	216 000	275 886	491 886
Expenses	-119 800	-84 440	-204 240	-264 858	-468 805
Operating Income	9 800	1 960	11 760	11 028	23 081
Net Interest	-1 200	1 493	293		-
OI before tax	8 600	3 454	12 054	11 028	23 081
(Income) Taxes	-2 400	-964	-3 364	-3 077	-6 441
OI after tax	6 200	2 490	8 690	7 950	16 640

Table 15: Budgeted income statement, 2011.

The comprehensive income in the first quarter of 2011 is NOK 6.700,- as the translation differences amounted to NOK 500,- this period.

	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Sales	560 204	631 785	705 493	779 962	853 625	924 761	991 549	1 052 144	1 104 751
Interest	7 043	7 536	8 101	8 750	9 397	10 036	10 658	11 255	11 818
OR	567 247	639 321	713 595	788 712	863 022	934 797	1 002 207	1 063 399	1 116 569
OI	47 552	85 560	131 179	184 423	178 700	168 541	153 870	134 803	111 657

Table 16: Budgeted income statement.

	06.01. 2011E	05.31. 2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
NOA	311 253	319 203	345 321	370 566	394 356	449 491	508 042	569 436	632 975	697 855	732 748
Equity	311 253	319 203	345 321	370 566	394 356	449 491	508 042	569 436	632 975	697 855	732 748

Table 17: Budgeted Balance sheet

The equity in the first half of 2011 was estimated based on the equity in the closing balance of 2010, and by adding the income and subtracting out the proposed dividend of NOK 0,10 per share, with an ex-dividend day of 05.26.2011.

(thousand NOK)	2nd h.2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Net OI	7 950	47 552	85 560	131 179	184 423	178 700	168 541	153 870	134 803	111 657
ΔNOA	7 950	26 118	25 244	23 790	55 135	58 551	61 394	63 540	64 880	34 893
FCFE	-0	21 433	60 315	107 389	129 289	120 149	107 147	90 331	69 923	76 764

Table 18: Budgeted FCFE.

6.3 Future cost of capital and discount rates

The valuation, and future cash flows, is in nominal terms after tax. The cost of capital should reflect this.

Risk-free rate

A 10 year government bond will be applied, which best will match the entire cash flow stream being valued. The risk-free rate that will be applied is the 10 year Norwegian Government bond rate, which is at 3,52%⁴⁴ before tax, and approximately 2,53% after tax.

Risk-less rate	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
10 year government bond	0,04	0,04	0,04	0,04	0,04	0,04	0,04	0,04	0,04	0,04
28% tax	0,01	0,01	0,01	0,01	0,01	0,01	0,01	0,01	0,01	0,01
Rf After tax	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025

Table 19: Riskless rate.

Source: www.Norges-Bank.no

Market risk premium

The assumptions made about the market risk premium applied in the historical cost of capital also apply here, and will be set to 5,5%.

⁴⁴ www.Norges-Bank.no. Government bonds with a 10 year duration.

Beta

The beta found in the financial analysis will be applied to the budgeting period up until and including period T-1. In period T, steady state, the beta will be adjusted using the Merrill-Lynch method where the beta is weighted to reflect the common assumption about the beta to be mean reverting. After weighting the estimated beta with 2/3, and the average beta of 1 with 1/3, the new beta for the steady state period is 1,12.

Expected cost of capital and discount rates

Cost of capital	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Risk-less rate	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025	0,025
MRP	0,055	0,055	0,055	0,055	0,055	0,055	0,055	0,055	0,055	0,055
Beta	1,18	1,18	1,18	1,18	1,18	1,18	1,18	1,18	1,18	1,12
k_e , annual	0,090	0,090	0,090	0,090	0,090	0,090	0,090	0,090	0,090	0,087
k_e , 7 months	0,051									
Discounting factor	1,05	1,09	1,19	1,30	1,41	1,54	1,68	1,83	1,99	0,04

Table 20: Future cost of capital

All discounting factors between 2012 and 2019 were calculated based on December 31st 2011 being the base year, before the aggregated cash flows then are discounted back to present time by the seven month discount rate displayed in the first column.

Part 5

7. Fundamental valuation

First, the equity DCF method will determine the value of Acta and the Acta share. Then a sensitivity analysis will be conducted to assess the quality of the result.

By discounting the FCFE at the cost of equity, you get the value of the equity in Acta.

$$\text{Value of equity} = \sum_{t=1}^{t=n} \frac{CF \text{ to equity}_t}{(1 + k_e)^t}$$

(thousands of NOK)	05.31.2011	2nd h.2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
PV.31.12.2011 (2011-2019)	471 115										
FCFE from operations	-	-0	21 433	60 315	107 389	129 289	120 149	107 147	90 331	69 923	76 764
Discounting factor	1,05	1,00	1,09	1,19	1,30	1,41	1,54	1,68	1,83	1,99	0,04
Present Value	448 452	-0	19 661	50 751	82 888	91 538	78 032	63 832	49 363	35 051	2 080 888

PV N.P and G.P	448 452
PV Terminal value	992 926
Present value of Equity	1 441 378
Number of shares	257 531
Value per share	5,60

Table 21: DCF valuation

The value of Acta is estimated to be NOK 1,4 billion and the value of the Acta share came to NOK 5,60 per share.

These value estimates are based entirely on the assumptions made and the forecast developed throughout this dissertation, and is not in any way intended as definitive result.

7.1 Sensitivity analysis

The value obtained from the DCF approach suggests a stock price of NOK 5,60. This value is based on the estimates of key drivers developed by combining accounting figures with several assumptions about the business and its prospects. The sensitivity analysis will assess how sensitive this stock value is to changes in the key drivers by changing these +/- 10, 20 and 30 percent.

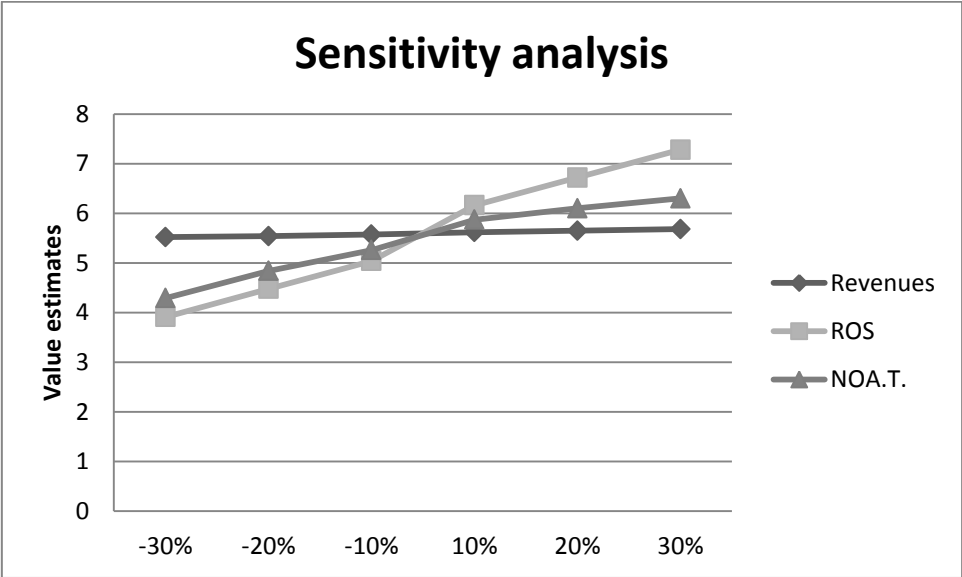


Figure 7: Sensitivity analysis.

These figures apply to changes on the horizon. As the figure shows, when all else remain the same, changes in revenue growth will have marginal effects on the share value. However, the value estimate is very sensitive to changes in the operating margin, ROS, and even a small reduction in NOA.T. could bring the share value down under five. This shows that the value estimate is highly uncertain.

8. Conclusion

The purpose of this dissertation was to value Acta Holding ASA, which was done by conducting a fundamental valuation. The knowledge obtained from the strategic analysis depicts an industry that has been severely affected by the subprime crisis and is still influenced by the repercussions. Acta was also found to be in competitive parity, and the competition will probably just grow stronger by time. The financial analysis showed no signs of either short-term liquidity risk or long-term solvency risk, but like the other findings from the normal period, these could not be used indiscriminately. This is because past performance does not seem to correspond well with current performance and the expectations about the future.

The value estimate came to NOK 5,60 per share.

In terms of a response to the problem statement; the issues of valuing Acta, as a financial service firm with negative earnings, did not only call for modifications to the valuation process and model, but also makes the numerical outcome questionable. For example, the regulatory environment which could have a huge impact on Acta's business and future growth is not easy to account for. These changes could occur and change the business of Acta, or just hamper growth. Or the changes may occur but not incur any changes to the business of Acta, and so on. Either way, the risk of such an uncertainty could possibly reduce the value of Acta significantly, by either a higher cost of capital or lower growth estimates. The regulatory restrictions were not accounted for in this analysis due to too much uncertainty about a possible estimate, but this might be one of the reasons that the stock price obtained from the DCF model is higher than the market value on Oslo Børs, indicating that such a measure should be incorporated in the valuation. The specific issues regarding Acta should probably promote a share value of less than NOK 5,00, but it should still exceed the market price of NOK 3,14.

It is important to emphasize that the value estimate is highly uncertain, and small changes in the estimated drivers can provide a very different result. It is not possible to predict the future, and so the value estimate is only based on assumptions about the future according to the static image of the situation per day. By the time Acta presents the next financial report, or even by tomorrow, the situation might change, and so will the share price. This value is therefore just an indication of the situation per day, and should also be viewed in context with the written assessments.

8.1 Disclaimer and other remarks

The value estimate of the Acta stock came to NOK 5,60, and compared to the market price of 3,14 on May 31st 2011, the stock seems to be very much undervalued by the market. But, considering the uncertainty of the value estimate, given the findings in the sensitivity analysis, the uncertainty in the markets, other limitations of this dissertation and the fact that the prices are highly volatile, this estimate does not necessarily propose a strong buy recommendation. The value should range somewhere between the two prices, and if no new information is revealed and the share price drops, this would suggest a buy strategy, or hold.

A few remarks are in order. This analysis has its weaknesses, as it did not incorporate information that could provide a different value estimate. Also, the dissertation has not compared Acta to the overall industry under the assumption that the current financial information necessary to perform such a comparison or an estimate of the industry average most likely will be skewed as the entire industry has been affected by a recession and cannot be used as a benchmark. Other delimitations and assumptions for this dissertation was listed previously, and should also be considered when considering to buy, sell, or hold the Acta stock.

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11.1. Consolidated Income statement, 2004-2005. Raw historical data

CONSOLIDATED INCOME STATEMENT - IFRS							
<i>(All amounts in thousand NOK)</i>	2004	2005	2006	2007	2008	2009	2010
Operating Revenues	659 367	1 234 057	1 813 975	2 269 648	937 567	489 382	427 727
Wages and salaries	-252 685	-434 096	-680 728	-934 202	-507 118	-301 542	-265 048
Depreciations	-13 148	-12 510	-9 113	-10 224	-18 885	-23 186	-20 693
write-downs	0	-1 250	0	0	-920	-3 523	-1 878
Other operating expenses	-111 536	-139 952	-205 176	-256 279	-285 723	-197 249	-167 286
				-1 200			
Total operating expenses	-377 369	-587 808	-895 017	705	-812 646	-525 501	-454 905
Operating income	281 998	646 249	918 959	1 068 943	124 921	-36 119	-27 178
Financial income	3 375	7 509	18 149	42 922	50 758	8 450	6 239
Financial expenses	-2 058	-1 082	-253	-5 615	-11 505	-17 391	-287
Net financial items	1 317	6 427	17 895	37 308	39 252	-8 941	5 952
Net income before tax	283 315	652 676	936 854	1 106 251	164 173	-45 059	-21 225
(Income) Taxes	-43 773	-183 551	-265 294	-313 895	-52 750	8 691	2 547
Net income	239 542	469 125	671 560	792 356	111 423	-36 369	-18 678
Currency translation diff.	-750	531	9 373	-7 776	2 796	-339	1 959
Comprehensive income	238 792	469 656	680 933	784 580	114 219	-36 708	-16 719

11.2. Consolidated Balance Sheet, 2004-2005. Raw historical data

CONSOLIDATED BALANCE SHEET. 31st of December - IFRS							
<i>(All amounts in thousand NOK)</i>	2004	2005	2006	2007	2008	2009	2010
Goodwill	12 234	8 123	6 131	6 131	6 131	6 131	14 954
Other intangible assets	461	0	0	0	42 295	46 147	45 006
Deferred tax asset	61 129	8 888	30 095	3 545	6 144	12 585	20 436
Property, plant and equip.	20 436	17 676	22 309	51 816	35 627	18 831	13 965
Total long-term assets	94 260	34 687	58 535	61 492	90 196	83 693	94 361
Total receivables	48 236	77 637	100 711	146 861	84 652	66 109	100 516
T-bills/Other financial assets	179 300	537 578	795 681	704 685	0	0	1 181
Bank deposits	222 092	333 293	521 587	969 071	439 417	261 520	245 162
Total current assets	449 628	948 508	1 417 979	1 820 617	524 069	327 629	346 859
TOTAL ASSETS	543 888	983 195	1 476 514	1 882 109	614 266	411 322	441 220
EQUITY AND LIABILITIES							
Share capital	43 498	45 303	45 303	45 303	45 303	45 303	46 356
Share premium account	2 947	11 168	11 168	11 168	11 168	11 168	27 786
Additional paid-in equity	10 020	0	0	0	0	1 075	6 581
Total paid-in equity	56 465	56 471	56 471	56 471	56 471	57 546	80 723
Other equity	377 855	532 909	710 475	828 095	300 521	263 812	247 093
Total retained earnings	377 855	532 909	710 475	828 095	300 521	263 812	247 093
Total equity	434 320	589 380	766 947	884 566	356 992	321 358	327 816
Accounts payable	6 401	10 738	24 139	20 623	12 760	14 158	11 555
Debt to credit institutions	0	13 629	29 670	101 520	34 841	0	0
Taxes payable	0	128 018	286 674	354 771	89 978	0	8 622
Taxes and public fees payable	26 345	43 395	32 618	73 965	29 661	18 089	16 810
Other current liabilities	76 822	198 034	336 467	446 663	90 034	57 716	76 418
Total current liabilities	109 568	393 815	709 567	997 542	257 274	89 963	113 404
Total liabilities	109 568	393 815	709 567	997 542	257 274	89 963	113 404
TOTAL EQUITY AND LIABILITIES	543 888	983 195	1 476 514	1 882 109	614 266	411 322	441 220

11.3 Consolidated changes in equity

CONSOLIDATED STATEMENT OF CHANGE IN EQUITY - Only <i>total equity</i> listed							
<i>All Amounts in thousand NOK</i>	2004	2005	2006	2007	2008	2009	2010
Balance as of Jan. 1st year X	183 754	434 320	589 380	766 947	884 566	356 992	321 358
Share issues year X	1 400	10	-	-	-	-	17 671
Share options red. empl.	414	-	-	-	-	-	-
Issue warrants	10 020	-	-	-	-	-	-
Share issue expenses	-60	-3	-	-	-	-	-
Currency conversion loss/gain	-750	531	9 374	-7 776	2 796	-339	1 959
Net Income for the year	239 542	469 125	671 560	792 356	111 423	-36 369	-18 678
Dividend to shareholders yX	-	-314 604	-503 367	-666 961	-641 793	-	-
Stock options to employees	-	-	-	-	-	1 075	5 506
Balance as of Dec. 31st year X	434 320	589 380	766 947	884 566	356 992	321 358	327 816

11.4 Consolidated cash flow statement

<i>(In thousands of NOK)</i>	2004	2005	2006	2007	2008	2009	2010
Operating activities							
Net Income b.t.	283 315	652 676	936 854	1 106 251	164 173	-45 059	-21 225
Taxes paid /rec. govern.Package	0	0	-128 354	-218 651	-315 675	-89 978	5 489
Depreciation and write-downs	13 148	13 760	9 113	10 224	19 805	26 710	22 571
Change in accounts payable	1 062	4 338	13 401	-3 516	-7 863	1 398	-2 603
Change in other accruals	36 228	108 959	107 082	104 798	-342 855	-21 037	-14 300
Stock options	0	0	0	0	0	1 388	5 506
CF from operating activities	333 752	779 733	938 096	999 106	-482 415	-126 580	-4 563
Investing activities							
Acquisition of fixed assets	-6 371	-9 289	-13 747	-39 732	-45 911	-16 137	-13 531
Investments in subsidiaries	-1 750	0	0	0	-337	0	-14 935
Acq. of other Financial Assets	0	0	0	0	0	0	-1 000
CF from investing activities	-8 121	-9 289	-13 747	-39 732	-46 248	-16 137	-29 466
Financing activities							
Repayment of long-term debt	-21 651	0	0	0	0	0	0
Payment of dividends	0	-314 604	-503 367	-666 961	-641 793	0	0
Paid in equity (net proceeds)	11 775	10	0	0	0	0	17 671
CF from financing activities	-9 876	-314 594	-503 367	-666 961	-641 793	0	17 671
Bank deposits, etc., Jan.1st	85 637	401 393	857 243	1 287 598	1 572 236	404 576	261 520
Net change	315 756	455 850	420 982	292 414	-1 170 455	-142 717	-16 358
Effect from currency rate ch.	0	0	9 374	-7 776	2 796	-339	0
Bank deposits, etc., 31 Dec.	401 393	857 243	1 287 598	1 572 236	404 577	261 520	245 162

11.5 Presentation of normalized operating income, OI.

Normalized OI	2004	2005	2006	2007	2008	2009	2010
Revenues from sales	659 367	1 234 057	1 813 975	2 269 648	937 567	489 382	427 727
Interest Income	3 375	7 509	18 149	42 922	50 758	8 450	6 239
Total Revenues	662 742	1 241 566	1 832 124	2 312 570	988 325	497 832	433 966
Wages and salaries	-252 685	-434 096	-680 728	-934 202	-507 118	-301 542	-265 048
Depreciations	-13 148	-12 510	-9 113	-10 224	-18 885	-23 186	-20 693
Other op. expenses	-111 536	-139 952	-205 176	-256 279	-285 723	-197 249	-167 286
Interest expenses	-2 058	-1 082	-253	-5 615	-11 505	-17 391	-287
Operating Expenses	-379 427	-587 640	-895 270	-1 206 320	-823 231	-539 368	-453 314
Operating Income	283 315	653 926	936 854	1 106 250	165 094	-41 536	-19 348
(Income) Taxes	-43 773	-183 903	-265 294	-313 895	-53 046	8 011	2 322
OI after tax (Normal)	239 542	470 023	671 560	792 355	112 048	-33 525	-17 026

11.6 Presentation of Net Operating assets, NOA.

Reformulated BALANCE SHEET							
<i>(In thousand NOK)</i>	2004	2005	2006	2007	2008	2009	2010
Working cash	401 392	870 871	1 317 268	1 673 756	439 417	261 520	246 343
Total receivables	48 236	77 637	100 711	146 861	84 652	66 109	100 516
Property, plant and eq.	20 436	17 676	22 309	51 816	35 627	18 831	13 965
Goodwill	12 234	8 123	6 131	6 131	6 131	6 131	14 954
Other intangible assets	461	0	0	0	42 295	46 147	45 006
Deferred tax asset	61 129	8 888	30 095	3 545	6 144	12 585	20 436
OPERATING assets	543 888	983 195	1 476 514	1 882 109	614 266	411 323	441 220
Accounts payable	6 401	10 738	24 139	20 623	12 760	14 158	11 555
Taxes payable	0	128 018	286 674	354 771	89 978	0	8 622
Public fees payable	26 345	43 395	32 618	73 965	29 661	18 089	16 810
Other current liabilities	76 822	198 034	336 467	446 663	90 034	57 716	76 418
Debt to credit inst.	0	13 629	29 670	101 520	34 841	0	0
OPERATING liabilities	109 568	393 814	709 568	997 542	257 274	89 963	113 405
NOA (Net Oper. Assets)	434 320	589 381	766 946	884 567	356 992	321 360	327 815
Total equity	434 320	589 380	766 947	884 566	356 992	321 358	327 816
Net Operating capital	434 320	589 380	766 947	884 566	356 992	321 358	327 816

Abbreviations

a.t.	= After tax
β	= Beta
b.t.	= Before tax
CB	= Closing Balance. (i.e., balance as of December 31 st .)
CR1	= Current ratio (Current Assets/Current Liabilities)
CR2	= Cash Ratio (Cash and cash eq. /Current Liabilities)
DCF	= Discounted Cash Flow
EPS	= Earnings Per Share
FCF	= Free Cash Flow
FCFE	= Free Cash Flow to Equity
FCFF	= Free Cash Flow to Firm
IPO	= Initial Public Offering
k_e	= Cost of equity
Market cap	= Market capitalization
MRP	= Market Risk Premium
NOA	= Net Operating Assets
NOPM	= Net Operating Profit Margin
OB	= Opening balance. (i.e., balance as of January 1 st .)
OI	= Operating Income
OR	= Operating Revenues
PESTEL	= Political, Economic, Sociocultural, Technological, Environmental, Legislative
Rf	= Risk-free rate
ROA	= Return on Assets
ROCE	= Return on Common Equity
ROE	= Return on equity
ROS	= Return on Sales (Net Income/Sales)
t	= Time period t
T	= Year T
VRIO	= Valuable, Rare, Imitable, Organized.