

## COMPARING THE FINANCIAL PERFORMANCE OF MOBILE OPERATOR COMPANIES USING ECONOMIC VALUE ADDED (EVA) AND STOCK RETURN

by:

**Julio Rendy Tandaju**

Faculty of Economics and Business  
International Business Administration (IBA) Program  
University of Sam Ratulangi Manado  
email: [jr.tandaju@gmail.com](mailto:jr.tandaju@gmail.com)

### ABSTRACT

A company has main purpose in running the business activity. Not only maximizing the profit, but also creating value for shareholder. The financial performance could be measured as the company runs in certain period. The objective of this study is to investigate the differences in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk. Economic Value Added (EVA) and Stock Return could be used to measure the financial performance. EVA measures the economic profit of company during a year. Stock Return is reflected the company's ability in maintaining their equity and returning the expected return of investor. Independent sample t-test is used as the method to test the two different independent samples. The population refers to the mobile operator companies that listed in Indonesia Stock Exchange and the financial statements of both companies from 2010 to 2012 are the samples. PT. XL Axiata, Tbk reaches its best performance and has more profit or economic value for the shareholders in 2011 of the period and creates the highest return for the investors in 2010. PT. Indosat, Tbk reaches its best performance and gain more profit or economic value for the shareholders in 2012 of the period and creates the highest return for the investors in 2010.

**Keywords:** *financial performance, economic value added (eva), stock return*

### INTRODUCTION

#### Research Background

Companies have been increasingly focused on their objective, creating value for the shareholders. According to Worthington and West (2001), an accepted financial axiom which is the role of managers is to maximize the wealth of shareholders by the efficient allocation of resource. Yet, there are some challenges that companies need to deal with nowadays; severe competition, financial markets, rapid technological change etc. Moreover, to keep their existence, they need to pass all these challenges.

Manager's ultimate roles are to create and to increase shareholder value. Therefore, they need to do those jobs greatly because shareholders are very particular about their interest into the business and they want management to come with very specific solution. Eakins (2005:396) said shareholders are most interested in how much a firm earns above what is needed to meet its minimum costs. The company will not be able to attract the stakeholders for the equity capital without the value creation of the company itself. The component of success for a company is not only the shareholders but also well-motivated employees, loyal customers, and suppliers. In the end, the company will succeed and successfully reach the objectives.

The financial information is in the form of financial statement in a company. It is a formal report on a business in monetary terms. The financial statement information is also used to forecast the future performance of a company. It could be the tools for the company to communicate information for decision-making, and used by managers, owners, creditors, or government agencies. It provides accounting information, which indicates the financial position and the company's performance as well. Hilton and Platt (2011:583) stated accounting systems are established to record events and provide the framework for internal and external financial reports.

The financial performance measures (traditional and modern value-based) have many type and appear in different variations. This research focuses on the latest innovation, which in the field of internal and external performance is Economic Value Added (EVA). EVA measures of how much the management has added to shareholders' wealth during the year (Brigham et al., 2010:82). It can describe the company's financial performance because it is related to the accounting profit. EVA is a performance measure that is more directly on to the creation of shareholder wealth. At the end, this type of method will reveal some important attributes as the basis of the company's financial performance.

Stock is one of the securities that have a high level of risk and one of the most attractive investment objects in the stock market trading. Investors buy common stocks because they expect a reward (return) on their investment. They need the information that can be used as a basic economic decision, this information is useful in forecasting the earnings or returns (stock returns) that will be earned in the future. Investors' expected rate of return is the sum of the probability of profits on a series that may occur.

The telecommunication business has grown remarkably after the introduction of mobile phones and the mobile operators. The increasing utilization of cellular telecommunication products currently can be seen from the growing mobile operators market in the world, including Indonesia. The number of mobile operator industry has developed rapidly in this last decade in Indonesia. In Indonesia, there are about two-hundred million customers of mobile operator these days and there are many mobile-operator companies as well. Therefore, those companies must be prepared to face the severe competition. They need to show their best performance (including the financial performance) to the customers.

Two mobile-operator companies' information are used in this research, namely, PT. XL Axiata, Tbk and PT. Indosat, Tbk. For the mobile-operator users, these two companies are familiar. Both companies have shown their customers the quality of their products and services. These two companies can be categorized as rivals in the mobile operator industries. From 2010 to 2012, both companies had competed by creating many innovative services. In 2012, PT. XL Axiata, Tbk generated its profit at 2,764 billion Rupiah and PT. Indosat, Tbk 487,4 billion Rupiah. Both companies have proven their existence in the mobile operator industry in Indonesia by generating profit every year.

## Research Objective

There are specific objectives for this research:

1. To analyze company performance in creating value by using EVA and Stock Return at PT. XL Axiata, Tbk during 2010 to 2012.
2. To analyze company performance in creating value by using EVA and Stock Returns at PT. Indosat, Tbk during 2010 to 2012.
3. To investigate whether there is any significant difference of financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk by using EVA during 2010 to 2012.
4. To investigate whether there is any significant difference of financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk based on Stock Return during 2010 to 2012.

## THEORETICAL FRAMEWORK

### Theories

#### Financial Performance

The choice of performance measures is one of the most important challenges that company should face; it plays a key role in developing strategic plans, evaluating the achievement of the objectives managers' compensation (Venanzi, 2010). Penman (2010:33) stated that the form of the financial statements is the way in which the statements, and their component parts, relate to each other. Form is given by a set of accounting relations that express the various components of financial statements in terms of other components. Every corporation should prepare reports of financial activities for the stakeholders (regulators, creditors/lenders, owners, and management) periodically (Gitman, 2006:46). Horngren and Harrison (2007:19) stated that the financial statements summarize the transaction data into a form that's useful for decision making, that are:

1. Income statement. The income statement presents a summary of an entity's revenues and expenses for a period of time, such as a month or a year. The income statement, also called the statement of earnings or statement of operations, is like a video – a moving picture of operations during the period.
2. Statement of owner's equity. The statement of owner's equity shows the changes in owner's equity during a time period, such as a month or a year.
3. Balance sheet. The balance sheet lists the entity's assets, liabilities, and owner's equity as of a specific date, usually the end of a month or a year.
4. Statement of cash flows. The statement of cash flows reports the cash coming in (cash receipts) and the cash going out (cash payments) during a period. Business activities result in a net cash inflow or a net cash outflow. The statement reports the net increase or decrease in cash during the period and the ending cash balance.

Further, the goal of financial statement analysis is to provide helpful insights to forecast future management performance. Financial statement analysis seeks for management performance evaluation in several important areas; profitability, efficiency, and risk (Reilly and Brown, 2012:265).

### **Economic Value Added**

Economic Value Added is a measure of financial performance based on the concept that all capital has a cost that earning more than the cost of capital creates value for shareholders (Alam and Nizamuddin, 2012). Venanzi (2010) stated that EVA is a modified version of residual income where the modifications consist of accounting adjustments designed to convert accounting income and accounting capital to economic income and economic capital. Further, EVA is a measure of the amount of the profit remaining after accounting for the return expected by the firm's investors. As such, EVA is said to be an estimate of true economic profit, or the amount by which earnings exceed or fall short of the required minimum rate of return investors could get investing in other securities of comparable risk (Gallagher and Andrew, 2003:108).

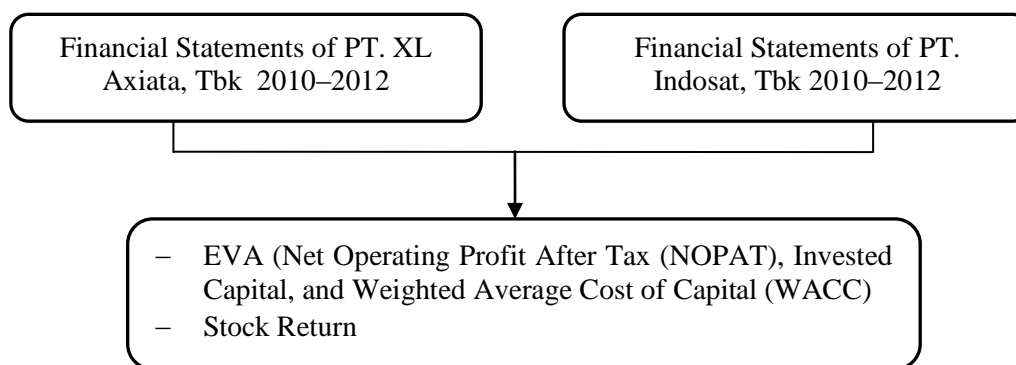
### **Stock Return**

According to Gitman (2006:226), return is the total gain or loss experienced on an investment over a given period of time; calculated by dividing the asset's cash distributions during the period, plus change in value, by its beginning-of-period investment value. Further, return is a reward for investing or the level of profit (Gitman and Joehnk, 2008:159).

### **Previous Researches**

Bhasin (2013) found that EVACE, ROCE, ROE, and EPS of sample companies differ significantly. In addition, the differences between the original and trend values were not very significant in statistical sense and the same is attributed to sample fluctuations. Arabsalehi and Mahmoodi (2012) found that ROA ( $R^2=24.89$  percent) is more associated with stock return that, in addition, REVA has the biggest explanatory power among value-based measures that REVA outperforms EVA. Sharma and Kumar (2010) presented a comprehensive literature review and critical analysis to move towards the advances in EVA where empirical research methodology accounted 71 percent among all four methodologies, only 4 percent studies have used exploratory cross-sectional method, 7 percent have used conceptual, 18 percent with descriptive approaches, 58 papers discussed the empirical evidences on EVA, stock return, & firm performance based on EVA's literature. Alam and Nizamuddin (2012) showed the relationship between EVA and MVA; the advantages of EVA compared to traditional measures and other value-based measures; steps in EVA computation; and advantages and limitations of EVA, thus, EVA is required to be tailored in line with accounting system, management philosophy and the degree of demand of such system.





**Figure 1. Conceptual Framework**

### Research Hypotheses

Based on the third and fourth research problems, the hypotheses are:

1.  $H_1$ : There is a significant difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk by using EVA.
2.  $H_2$ : There is a significant difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk based on Stock Return.

## RESEARCH METHOD

### Type of Research

The type of research is descriptive research. The companies' financial statements (PT. XL Axiata, Tbk and PT. Indosat, Tbk) from 2010 to 2012 had been analyzed and described. Sekaran and Bougie (2010:105,106) stated that a descriptive study is undertaken in order to ascertain and be able to describe the characteristics of the variables of interest in a situation.

### Place and Time of Research

The study is conducted in Sam Ratulangi University in Manado during June to July 2013. The data was collected on the study hours in June at Indonesia stock exchange.

### Population and Sample

According to Sekaran and Bougie (2010:262), the population refers to the entire group of people, events, or things of interest that the researcher wishes to investigate. That is, the population of this research is the Indonesian companies that are listed on Indonesia Stock Exchange (IDX), specified to mobile operator companies that have "go public" or IPO.

A sample is a relatively small subset of the population. Purposive sampling method is considered to be used in this research. It is a type of non-probability sampling and it allows information from the specific target groups or criteria. The criteria of the company that provide the sample in this research were: (1) companies listed as Mobile Operator companies, (2) companies that have gone public or IPO, (3) companies that are listed on Indonesia Stock Exchange (IDX), and (4) companies that have published the annual financial statements during 2010 to 2012. Based on these criteria, therefore, the samples of this research are the financial statements of PT.XL Axiata, Tbk and PT. Indosat, Tbk from 2010 to 2012.

### Data Collection Method

This part explains the type of data and source of data. Since this research uses an approach of financial analysis, therefore the data used are quantitative in nature. This research uses financial statements or financial database. The secondary type of data are used in this research, because it is suitable with the approach of

financial analysis. Secondary data offer the possibility of achieving the comparative analysis when such analyses would be impossible or expensive (Hair et al., 2007:129).

Data and other supportive information for this research were gathered from several kinds of resources that related to this research. The data and information had been collected from the companies' and IDX website; published articles; books and other sources that related with this research.

### Operational Definition of Research Variables

The variables that are used in this research are the companies' value financial performance that measured by Economic Value Added from mobile operators companies' financial statements and Stock Returns from companies' trading data. The definitions of primary variables used in this research are as follows:

1. Economic Value Added (EVA) can be described as the profit measurement or the financial performance measure of a firm from operating activities by subtracting the cost of capital and invested capital from the net operating profit after tax in certain year.
2. Stock Return is the expected return of investing stock over period of time (year).

### Data analysis Method

#### Normality Test

The normality test that used is Kolmogorov – Smirnov Test. (K-S Test) is a nonparametric test for the equality of continues. It is one of the tests for the goodness of fit. If the  $H_0$  is accepted, it means the data values are normally distributed and if the  $H_a$  is accepted instead, that the data values are not normally distributed.

#### Economic Value Added

Calculating EVA:

$$\text{Net Operating Profit After Tax (NOPAT)} \\ - (\text{Invested Capital} \times \text{Weighted Average Cost of Capital (WACC)})$$

#### Stock Return

Calculating Stock Return:

$$R_{it} = \frac{P_{it} - P_{it-1}}{P_{it-1}}$$

$R_{it}$  is the rate of stock  $i$  on  $t$  period

$P_{it}$  is the closing price of stock  $i$  on  $t$  period

$P_{it-1}$  is the closing price of stock  $i$  on previous period ( $t-1$ )

#### Independent Sample T-Test

Independent sample t-test is run in order to see the significant differences in the means between two groups in the variable (Sekaran and Bougie, 2010:345). It is used to test the two means from two independent or unrelated samples. Results from decision step are to test whether to accept the  $H_0$  or to reject  $H_0$ . The step to accept or reject  $H_0$  is by seeing the probability score compared to the alpha ( $\alpha$ ) that used with some criteria, which are: if the P-value (significance)  $> 0.05$  ( $\alpha$ ) then  $H_0$  is accepted and if the P-value (significance)  $< 0.05$  ( $\alpha$ ) then  $H_a$  is accepted. If the  $H_0$  is accepted, it means there is no difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk and if the  $H_a$  is accepted instead, that there is significant difference in financial performance between both companies.

## RESULTS AND DISCUSSION

### Result

#### Normality Test

The Asymp. Sig value of EVA is .915 (.915 > 0.05). Therefore, the conclusion is the data distribution of EVA score is normally distributed and the  $H_0$  is chosen. The Asymp. Sig value of Stock Return is .445 (.445 > 0.05) and the conclusion is to choose the  $H_0$  as well because the data distribution of Stock Return is normally distributed.

#### Economic Value Added

This section discloses the results of Net Operating Profit After Tax (NOPAT), Invested Capital, and Weighted Average of Cost Of Capital (WACC). These components' results will help to obtain the outcome of Economic Value Added from both companies. Each of the component is compared with to company's value to get the comparison result.

**Table 1. Economic Value Added**

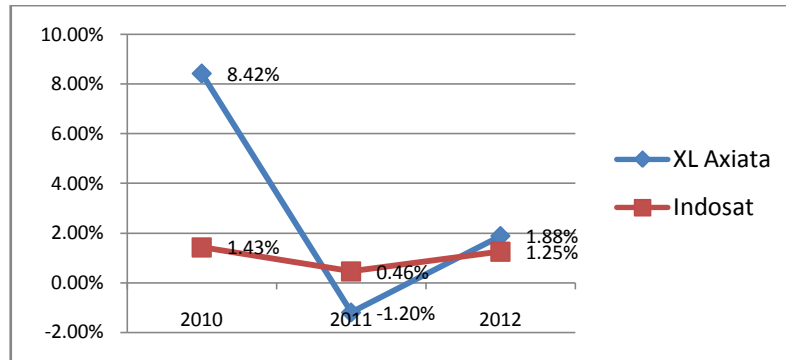
Company	Description	2010	2011	2012
PT. XL Axiata, Tbk	NOPAT	3,700,981	3,625,344	3,428,069
	Invested Capital	22,688,248	22,442,442	26,715,709
	WACC	4.78%	3.17%	3.85%
	EVA	2,616,759	2,914,668	2,399,479
PT. Indosat, Tbk	NOPAT	2,303,165	2,535,389	3,011,745
	Invested Capital	41,300,179	41,264,945	44,209,310
	WACC	3.08%	3.86%	2.82%
	EVA	1,031,994	940,917	1,764,390

Source: data processed 2013

Table 1 indicates the results of EVA calculation from 2010 to 2012 are inconsistent. In 2010, PT. XL Axiata, Tbk earned Rp. 2,616,759,- million as its EVA, and reached the highest at Rp. 2,914,668,- in 2011. However, the company could not keep the trend and its EVA fell to Rp. 2,399,479,- million. By in contrast, PT. Indosat earned its highest EVA in 2012 with Rp. 1,764,390,- million. In 2010 the company generated EVA by Rp. 1,031,994,-. But, company has its lowest EVA in 2011 with only Rp. 940,917,- million.

#### Stock Return

Companies could not control the stock price in the stock market generally. Many factors may determine the movement of stock's price and lead to the change of stock return. Internal factors that come from the company, such as the internal developments can affect the price of its stock. However, companies can not control the factors that come from outside. Company stock prices and the stock market can be influenced generally by the world events.



**Figure 2. Stock Return**

Source: data processed 2013

The average stock return of PT. XL Axiata, Tbk has a negative percentage in 2011 with -1.20%, but it generates 8.42% in 2010. It means there has been a steep fall of stock return from 2010 to 2011. On the other hand, PT. Indosat, Tbk only has 1.43% of stock return as its high and 0.46% in 2011 as its low. PT. XL Axiata, Tbk has a better performance in generating the stock return; however, PT. Indosat, Tbk has stable stock return.

**Independent Sample T-Test**

**Table 2. Independent Sample T-Test Result**

t-Test For Equality Means			
	Firm	t	Sig (2-tailed)
EVA	XL Axiata	5.937	.004
	Indosat	5.937	.007

Source: SPSS Statistics 17.0

Table 2 indicates there is a difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk. It is shown by the mean of EVA of PT. XL Axiata, Tbk equal to 2.6436E6 and PT. Indosat, Tbk is 1.01122E6. Based on the F score and the sig value ( $\alpha$ ), the decision is to choose  $H_0$  (.470 > 0.05). Therefore, the Equal Variances Assumed is chosen to compare the means. The score of  $t_{count}$  on Equal Variances Assumed is 5.937 with the Sig (2-tailed) value is .004 (.004 < 0.05). This result means that in testing first hypothesis is to accept  $H_a$  and to reject  $H_0$ . The conclusion of hypothesis testing is there is a significant difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk by using EVA.

**Table 3. Independent Sample T-Test Result**

t-Test For Equality Means			
	Firm	t	Sig (2-tailed)
Stock Return	XL Axiata	.697	.524
	Indosat	.697	.557

Source: SPSS Statistics 17.0

Table 3 shows the mean of stock of PT. XL Axiata Tbk is .0303 and PT. Indosat, Tbk is .0105. It means there is difference between both companies based on Stock Return. F score is 6.365 and the sig value ( $\alpha$ ) is .065 (> 0.05). Based on this result,  $H_0$  is accepted and to reject  $H_a$ . Therefore, the Equal Variances Assumed is chosen to compare the means. The  $t_{count}$  on Equal Variances Assumed area is .697 with the Sig (2-tailed) value is .524 (.524 > 0.05). Finally, the next step is to choose  $H_0$ , and it can be concluded that there is no significant difference between PT. XL Axiata, Tbk and PT. Indosat, Tbk by using Stock Return.



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**Discussion****Financial Performance of PT. XL Axiata, Tbk and PT. Indosat, Tbk Using Economic Value Added (EVA)**

It is the proof for the “go public” companies if they can create the value added . Because the value added indicates that the companies can bring the return for the investors who invest their money. Creating value added is a compulsory job for mobile operator company, especially for PT. XL Axiata, Tbk and PT. Indosat, Tbk. They should preserve the financial position to achieve their objective.

The previous results reveal that PT. XL Axiata, Tbk has higher operating income than PT. Indosat, Tbk that produce better NOPAT. Operating income shows investors how much revenue will eventually become profitable for the companies. Since PT. Indosat, Tbk has more in assets and current liabilities; it exceeds the invested capital of PT. XL Axiata, Tbk. Using the invested capital to activities and projects that show higher operating performance can also help in improving Economic Value Added. PT. Indosat, Tbk has relative higher funds to capitalize a particular project. However, based on the performance of PT. Indosat, Tbk, it did not use the assets efficiently because it produced low operating income compared to PT. XL Axiata, Tbk that produced higher operating income with fewer assets. This situation could discourage the investor or shareholder.

The firm’s capital cost is largely determined by outside forces and has little control over it essentially (Russ, 2001). Companies use WACC as a way to gauge the expense of funding future projects. Company’s WACC is the overall required return on the firm as a whole and it is often used internally by company directors. The lower the companies’ WACC, the cheaper it is for companies to fund new projects. The WACC increases as the beta and rate of return on equity increases. Based on the result, both companies have little difference in WACC. Nevertheless, PT. Indosat, Tbk creates lower WACC, and it caused by the components of WACC. A company should increase its use of cheaper financing sources in order to decrease the WACC.

It is clear that both companies have financial performance differences for all of these aspects, especially based on the Economic Value Added (EVA). Based on the results in the previous section, both companies have positive value in generating EVA for three-year periods and PT. XL Axiata has preeminent EVA compared to PT. Indosat, Tbk It means that the earned-returns have exceeded the cost of capital, which is what investors expect and the companies to succeed in making the shareholder value. A negative EVA suggests that significant change may be required, by EVA, these changes could be focused and driven for maximum impact on profit and value creation (Bielinski, 1996). Statistically (by independent sample t-test), the results of data analysis with EVA approach show a significant difference in financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk.

Some important indicators must be considered by PT. XL Axiata, Tbk and PT. Indosat, Tbk in order to get the positive value of EVA incessantly. According to Stewart (1994) cited by Bhasin (2013), to increase EVA, companies must utilize their existing resources more efficiently to improve their performance and this leads to higher rates of interest on existing capitals. The first thing to do in preventing negative EVA is to improve the operating performance such as the operating profit margin and the asset turnover ratios. Moreover, companies should invest additional capital in only these projects where return is more than the cost of capital; to withdraw capital from the unprofitable projects; to employ an optimal capital structure to drive down the cost of capital.

**Financial Performance of PT. XL Axiata, Tbk and PT. Indosat, Tbk Using Stock Return**

It is important for the “go public” company to generate return of stock to the investor. Stock return indicates the company’s ability in returning investors’ capital or money. The stock return could be a profit (positive) or loss (negative). This situation could be happened anytime in the stock market. Simply, if the adjusted closed-price in certain period is greater than the previous, there is a profit in stock return and for the opposite. Many factors can affect stock prices that lead to the stock return. The stock price of the companies in the same industry tends to move in tandem with each other. It is because the market condition generally affects the companies in the same industry the same way. The company news and performance, investor sentiment, inflation, and the economic factors could be affecting the stock prices.



The results show PT. XL Axiata, Tbk has a relatively higher stock return in 2010 compared to the other two years and PT. Indosat, Tbk. The stock return could be affected by the stock monthly prices. To maintain good stock return, the companies do not have much control the outside factor. In the stock market, the market and the investor is the key role. The companies only keep their best performance to get investors' attention.

As investors, based on the stock return, they could be investing to PT. XL Axiata, Tbk because it is more promising. However, investor should see the trends of stock return from this company. On the other hand, PT. Indosat, Tbk has slower or more stable in stock return. This could be another choice to invest, because this company has less fluctuation in stock return. Investors may choose the company to invest in based on their capital and income. In addition, dividends can be the factor that investor pay attention to in order to buy a stock. Dividend provides an impulse to own stock in stable company even it is not experiencing much growth. Dividends are not the requirement for companies, but they motivate the investor to invest in company. PT. XL Axiata only pays dividend in 2011 and 2012 for the period three years, but actually, it has a relatively higher stock return in 2010. PT. XL Axiata could reinvest its profit to help sustain higher growth or used the profit to other projects. However, this situation could lessen the investors' attention to buy stock for the next year. In fact, in 2011 the stock return fell steeply. Meanwhile, PT. Indosat, Tbk paid dividends for three years in that period. Therefore, it is more stable in the stock return. However, there is little difference between the two companies statistically, because the trends of stock return. This may be caused by the similar price of the stock from both companies and the market respond, and these companies are in the same level and in the mobile operator industry.

## CONCLUSION AND RECOMMENDATION

### Conclusions

The conclusions of this study are:

1. PT. XL Axiata, Tbk created its highest economic value added in 2011 and the lowest in 2012 and the company generated the highest stock return in 2010. The company reaches its best performance and has more profit or economic value for the shareholders in 2011 of the period. It creates the highest return for the investors in 2010.
2. PT. Indosat, Tbk created the highest economic value added in 2012 and the lowest in 2011 and the company generated the highest stock return in 2010. The company extends its best performance and gain more profit or economic value for the shareholders in 2012 of the period. It creates the highest return for the investors in 2010.
3. There is a significant difference of financial performance between PT. XL, Axiata, Tbk and PT. Indosat, Tbk based on EVA. After the EVA calculation, PT. XL Axiata, Tbk has more economic value added than PT. Indosat, Tbk.
4. There is no significant difference of financial performance between PT. XL Axiata, Tbk and PT. Indosat, Tbk based on Stock Return. Both companies has similar movement of stock return because the stock prices of them are alike.

### Recommendations

There are some recommendations in this research:

1. PT. XL Axiata, Tbk and PT. Indosat, Tbk might apply the concept of Economic Value Added (EVA) in order to generate their profit or measure the financial performance. With the positive value of EVA that both companies produce, it does not mean they would stop creating value in the future. They should be able to maintain or even to improve their performance, in order to be the best mobile operator companies;
2. Based on the stock return, the investor should be careful with the price fluctuation. Even the companies cannot do much in terms to control the price in the market. They should improve the performance to get the trust of investor; and
3. The future research should improve the sample of the companies. It might use the other companies or sectors, so the result will be more comprehensive. In addition, further research could add other approaches for comparison, such as Market Value Added, Earning per Share, Return on Sales, etc.

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