

Finance report example

Business, Company



Portfolio Management

Part 1)

Compare your portfolio's return over the investment period with the Market Portfolio. Did you outperform the Market Portfolio? What if you take the CAPM result into account? Show all calculations used. What might be some reasons your portfolio either outperformed or underperformed vis á vis the Market Portfolio?

Answer)

Portfolio Construction and outcome

The portfolio was constructed using three stocks from different industries where the objective was to analyze their performance in comparison to the market index, S&P 500. The three stocks selected by us were Apple Inc., Starbucks and Tesla Motors with weights allocated as 22. 19%, 52. 66% and 25. 15%, respectively.

Referring to our calculation in the excel spreadsheet, we found that we were successful in beating the market as during the 50 day period, our portfolio earned holding period return of 6. 89% while the S&P 500 produced return of 6. 02%. On an annualized basis, the returns were 62. 61% and 53. 21%, respectively. Important to note, on the basis of Capital Asset Pricing Model(CAPM), the expected return of our portfolio came out to be 62. 19% that was only marginally less than the annualized return calculated by us.

Reason for outperformance

As we already stated that our three asset portfolio outperformed the market by 9. 40% as while our portfolio earned 62. 61% on annualized basis, S&P

returned 53.21% on annualized basis. Here, the probable reason for us beating the market is the successful portfolio diversification strategy employed by us and also high beta of the stocks that rewarded us with higher return.

At the time of construction of our portfolio, we followed the old tradition of “don’t put all your eggs in one basket” and selected the stocks with least correlation to each other. Below is the correlation between each pair of the stock in our portfolio:

- Apple-Starbucks: 0.2275

- Apple-Tesla: 0.4261

- Starbucks-Tesla: 0.2609

Hence, by including stocks in our portfolio with less than positive correlation, we were able to eliminate the unsystematic risk(to an extent) and were left only with systematic risk(measured through beta). In addition, with each of the stock having higher risk than the market(as measured by the beta), our portfolio was expected to perform better than the markets at the time of increasing prices. Below is the summary of beta and closing price for each of the stock

*Here the term Beta measures the volatility of the stock returns in relation to the market index. For instance, since Apple has beta of 1.26, this indicates that the company’s stock is 26% more volatile than the market.

CAPM Model

CAPM is undoubtedly the most fundamental model in the financial industry but it also suffers from some disadvantages which we witnessed at the time of its computation In our portfolio model.

- i) Value of beta of a company varies from website to website and from publication to publication. Hence, as we change the beta value, the computed beta also changes, thus varying the CAPM multiple.
- ii) The model also depends on assumptions related to risk free rate and market returns. For Instance, in our model, we assumed the risk-free rate to be 3 month treasury bill rate.

We hope that our clients are satisfied with the performance of our portfolio over the 50 day period. During this period, we were able to beat the market as our annualized return of 62. 61% exceeded that of the market which produced an annualized return of 53. 21%. We will continue this portfolio allocation in the coming days although weights of each stock will be re-considered as we will now weight more on Apple than Tesla Motors.

Part 2:

About the company: Apple Inc.

Headquartered in California, Apple Inc. is an American multination company known for its innovative products in the consumer electronic and software industry. The company is listed on NASDAQ under the ticker sign of ‘ AAPL’. Incorporated in the year 1997 by Steve Jobs, Steve Wozniak and Ronald Wayne, the company was renamed from Apple Computers Inc. to Apple Inc. in 2007. At present, it is the world’s biggest corporation with the market capitalization of \$674. 46 Billion.

Products and Services

The company is known for the range of products it sells. The list begins with the IPOD media player that revolutionized the music industry in early 2000’s

followed by iPhone that changed the smartphone industry in 2008. In 2009, the company introduced its first ever tablet computer, iPad. The company also sells the Macline computers and laptop popularly known as Macbook series and provides paid multimedia services, iTunes.

Financial Ratios

In this section, we will be laying out the financial ratios of the company for the past three years. The section will be subdivided into three sections:

a)Liquidity Ratios

i)Current Ratio: $\text{Current Assets} / \text{Current Liabilities}$

ii) Quick Ratio: $\text{Cash} + \text{Receivables} / \text{Current Liabilities}$

b)Profitability Ratios

i) Operating Profit Margin: $\text{Operating Income} / \text{Revenue}$

ii)Earning per Share: $(\text{Net Income} - \text{Pref Dividends}) / \text{Weighted Average Common Shares}$

c)Efficiency Ratios

i)Inventory Turnover Ratio: $\text{COGS} / \text{Average Inventory}$

ii)Receivable Turnover Ratio: $\text{Revenue} / \text{Average Receivables}$

Dividend Policy

Apple Inc. has always been paying healthy dividends to its shareholders. May market analysts have also rated it as a top dividend stock providing income stream to the shareholders in addition to the capital appreciation. The dividend payment of the company comes from its massive cash hoarding of more than \$160 Billion and also its increasing net income that induce the

company to share its profits with the shareholders. Below is the recent dividend payment history of the company:

Corporate Structure

Part 3:

Q: Assess your performance during the investment period. Did you achieve your goals given your stated investment strategy? Would you propose any changes at the end of this period given your results and your forecast of the direction of the markets?

Answer:

Just as any other investor, even our goal was to beat the market through effective asset allocation and in order to do so, we relied on portfolio diversification strategy where in order to eliminate the unsystematic risk from our portfolio, we selected stocks with least correlation to each other. In addition, another consideration in order to beat the market was to include high beta stocks so as to balance our risk-reward profile. By the end of 50 day period, our strategy turned successful and we were able to beat the market by 9.40% on annualized basis. The success came not only from the portfolio diversification that reduced the unsystematic risk but also from a positive exposure of higher beta stock that performed well than the market movement.

Works Cited

Apple Price-Target Rises to \$140. (2014, December 1). Retrieved December 5, 2014, from Barrons: <http://online.barrons.com/articles/apple-price-target-rises-to-140-1417470121>

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