

Free financial analysis essay example

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A fund manager with a portfolio worth \$50 million that has a beta of 0.87 whose employer is concerned about market performance must first evaluate the current market index position. Since the employer is concerned regarding the performance of the market over the next two months and plans to use three-month futures contract on the S&P 500 to hedge the risk that evaluation must consider financial exposure as well as projected performance rates.

Financial exposure is the amount of money at risk in an investment. All investments carry a degree of risk that goes beyond the potential for the loss of capital. While a federally insured CD could prevent capital investment loss, there is no protection against interest rate risk. The S&P 500 carries no guarantee that capital and income could be lost in the process of hedging risk with a three-month futures contract. With a beta of 0.87, the fund faces a downside of 8.7% if the S&P 500 drops by 10%.

Examining probability is the first step in the process of quantifying risk and the resultant financial exposure. The current 3 months US risk-free interest rate stands at 3%, up from its 2% close last week. The Contract Size is the amount of an underlying asset represented by each futures contract. The contract multiplier for the S&P 500 Variance futures contract is \$1 per variance unit. One contract equals one variance unit. (Charles Schwab Staff, 2014).

A fundamental analysis is an assessment of all available news, statistics and economic data of the company combined with global and political information. In regards to the S&P 500, it has seen a progressive gain with a

series of ups and downs. The general global market has also shown progressive gains. The upcoming U. S. National Elections may cause some shake up in the market. This is most likely to occur if one party shows strong gains in the congressional races.

A technical analysis of the asset class shows somewhat erratic movement that is trending towards a pattern of long-term gains. The S&P 500 chart is bullish but reaching the top of the channel. If the trend breaks the top of the channel, it opens the possibility of increasing market gains. If the price fails to break through a substantial drop in value is probable.

A great deal rest upon the results of the upcoming U. S. elections and their impact on American and global markets.

At the time of this writing in October 2014, an analysis of a potential market strategy must be flexible enough to allow for adjustment based upon the upcoming elections and how they play out in regards to nation and international markets. Because this is, also the holiday shopping season the economic influence on the stock markets in general, and the S&P 500 must be taken into account.

When looking at the market trends, the apparent drop in value seen at the end of September was countered by strong gains in mid-October. Since the October highs, there was some back sliding in values. Never the less the general outcome was positive. Because the Fund's value is tied closely with the S&P 500 index, those futures would permit a venue to moderate any downside in the market, which may affect the portfolio. A fund manager's priority is to protect the fund from any downside. S&P 500 futures fulfil the necessary criteria and provide a proper hedging strategy to protect the fund.

References

Charles Schwab Staff, 2014. S&P Variance Futures. [Online] Available at:
http://cfe.cboe.com/Products/Spec_VA.aspx