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SECURITY ANALYSIS AND PORTFOLIO MANAGEMENT –PMF05 CASE STUDY

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MASTER OF BUSINESS ADMINISTRATION
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Case Study Number	**I**
Level of teaching	**L3**
Program outcomes covered	**P01, P02, P04, P05, P06,**
Course outcomes covered	**C305.1**

AN ANALYSIS OF SMALL SAVINGS SCHEMES IN INDIA

In India, there are multiple investment avenues available to meet the differing needs of investors. These investment options differ from each other based on their returns, maturity period, and the risk-taking capacity of the investors, among other things. In terms of their returns, they can be classified into high-return and low-return classes. However, risk and returns go hand-in-hand, the higher the risk involved, the higher the returns to be expected. Investors who aspire for higher returns have to bear a high-level of risk as well. An example is an investment made in the highly volatile stock market. As far as the time aspect of the investment is concerned, there are financial instruments which are short-term in nature and these include savings bank accounts, money market or liquid funds, and fixed deposits with banks. On the other hand, there are some financial instruments which offer a long-term horizon for investment. These include post office savings, Public Provident Fund (PPF), company fixed deposits, bonds and mutual funds. Small savings schemes in India are framed and enacted by the central government under the Government Savings Bank Act, 1873 and Government Savings Certificate Act, 1959. Small savings schemes came into existence after independence with the objective of providing safe and simple investment opportunities to the lower and middle income groups. These schemes were channelized and administered by government institutions, such as post offices and nationalized banks. With the same objective, the PPF was established in 1968 for individuals to save for their investments. There are various schemes offered by the Government of India (GoI) through post offices across the country. These schemes include the post-office Savings Account, the post-office Recurring Deposit Account, the post-office Time Deposit Account, the post-office Monthly Income Account, the post-office Public Provident Fund Account, the Kisan Vikas Patra, the National Savings Certificate, and the Senior Citizens Savings Scheme. The maturity period of these schemes varies from very short as in the case of a savings deposit to over 15 years as in the case of PPF. However, all these investment options come under the same risk class as all of them have fixed returns and are guaranteed by the GoI. The returns vary between schemes based on their features and maturity period. The responsibility of promoting and mobilizing small savings schemes rests with the National Savings Institute (NSI), a division of the ministry of finance. The NSI markets the small savings schemes on a nationwide basis and provides the government with feedback from customers. The small savings scheme program aims at promoting the savings habit and providing safe investment avenues to people with limited income and savings potential. These schemes are operated through about 160,000 post offices across the country. The PPF scheme is also operated through more than 8000 branches of public sector banks. Monthly Income Scheme (MIS) The post office Monthly Income Scheme (MIS) provides for monthly payment of interest income to investors. Recurring Deposit (RD) APost Office Recurring DepositAccount (RDA) is a banking service offered by India Post at all post office counters in the country. Kisan Vikas Patra The Kisan Vikas Patra (KVP) is another safe and secure avenue for investment floated by the GoI under the post office schemes, according to analysts. Public Provident Fund (PPF) PPF is one of the investment plans that suit salaried as well as self-employed people, according to experts. National Savings Certificate (NSC) The National Savings Certificate scheme is another option in the government savings schemes, which offers a tax advantage to investors This case study aims at providing insights into the prevailing small savings schemes in India. At the same time, it also takes a look at the financial aspect of the schemes based on their tax rebate, post-tax returns, tenure of the schemes, etc. The decision, which scheme to invest in depends totally upon the liquidity needs of the investor. The decision to invest is also determined by the return offered by the scheme and its tax implications. Every scheme has its benefits for the investor

Questions

1. What are the issues of small saving schemes?

2. Who frames and enacts small savings schemes in India?

3. What are the various schemes offered by the Government of India (GoI) through post offices across the country?

Case Study Number	II
Level of teaching	L3
Program outcomes covered	P01, P02, P05, P06,
Course outcomes covered	C305.1

INVESTMENT MANAGEMENT AT HARVARD MANAGEMENT COMPANY

On February 17, 2009, 1,600 non-faculty employees of Harvard University (Harvard) received a crimson folder containing details of the early retirement benefits offered to them. Earlier, on February 11, 2009, Harvard had announced the eligibility4 criteria for those employees who would be offered early retirement. The objective of the move was to save on operating expenses. The University also announced other cost-cutting measures that included budget cuts varying between 10% and 15% in all Harvard departments. Besides, it announced a 3.5% increase in tuition fees for the academic year 2009-10. The University attributed these cost-cutting measures to the losses incurred by Harvard Management Company (HMC). HMC managed Harvard's endowment funds, the largest in the industry. As of June 30, 2008, it managed assets worth US$ 36.9 billion. Harvard reported that the value of the assets had fallen by 22% in the four months of fiscal 2008-09 that ended on October 31, 2008. The losses reported in this case did not include HMC's investments in real assets and private equity. Harvard depended on its endowment to fund more than one-third of its operational budget every year. It withdrew US$ 1.6 billion from its endowment fund in the fiscal year 2008 that ended on June 30, 2008. This marked HMC's largest ever endowment payout to the university. Harvard estimated a loss of 30% on the assets of HMC for the current fiscal year that would end on June 30, 2009. This would be the worst loss reported by HMC, since 1974, when it had posted a loss of 12.2%. HMC announced that it would lay off 25% of its 200 employees as a part of its reorganization and rebalancing strategy. HMC was regarded as one of the most profitable managers of endowment funds(Refer to Table I for returns generated by top four endowments in the US for the financial years 2005 to 2008). It consistently outperformed the average returns posted by the industry, which invested in similar asset classes in which HMC invested. For instance, HMC posted a positive return of 8.6% on its funds for the year ended June 2008 as compared to a 13% negative return posted by the S&P 500 index5 during the same period. HMC was renowned for its asset-allocation strategy. It followed a hybrid model in managing its funds.HMC was incorporated in 1974 to manage the endowments, pension assets, working capital, and non-cash gifts of Harvard. Its objective was to provide financial support to the operations of Harvard. To conform to that objective, HMC's Board and the management laid down the investment philosophy to allocate assets across various markets and asset classes in their efforts to generate the optimum rate of return in line with Harvard's risk tolerance level. HMC also worked on the premise that in addition to earning income to support the activities of the University, it had to generate capital appreciation on the assets it held over a long-term. Asset allocation HMC had managed the largest university endowment fund in the world, since its inception. (Refer to Exhibit IV for Top Ten University Endowments in the US by the End of June 2008). It followed a well-diversified asset-allocation strategy. For instance, for the fiscal ended June 2008, HMC had investments in 12 non-cash asset classes. Fund management at HMC Walter Cabot (Cabot) was nominated as the first President and CEO for HMC in 1974. HMC's assets grew from US$ 1.3 billion in 1974 to US$ 4.7 billion in 1990 under his leadership. Cabot resigned from HMC after his 16-year tenure in 1990, when Meyer was nominated as his successor. Meyer led HMC between 1990 and 2005 and grew HMC's asset value from US$ 4.7 billion to US$ 22.6 billion. HMC nominated Mohammed El-Erian (El-Erian) as successor to Meyer.

Questions

1. What does the case examine?

2. What are the various issues of HMC?

3. When did Harvard University receive a crimson folder containing details of the early retirement benefits offered to them?

Case Study Number	III
Level of teaching	L3
Program outcomes covered	P01, P02, P04, P05, P06,
Course outcomes covered	C305.2

GLOBAL CONGLOMERATES BONUS SHARE SCRUTINY

ABC Ltd. is a global leader in technology services and consulting. It has enable clients in45 countries to create and execute strategies for their digital transformation. From engineering to application development, knowledge management and business process management, it helps their clients find the right problems to solve, and to solve these effectively. Their team of 198,000+ innovators, across the globe, is differentiated by the imagination, knowledge and experience, across industries and technologies that they bring to every project they undertake. Today, businesses operate in an unprecedentedly fluid environment. The technology landscape is turning highly complex as it evolves to meet the demands of a competitive marketplace and an experiential economy. At the same time, customers are increasingly demanding simple, new, and convenient experiences.ABC Consulting helps global corporations - in over 20 countries - develop unique solutions to address their complex business challenges and create value through sustainable innovation. As pragmatic consultants with an eye on execution, they help you design and achieve market-leading performance roadmaps by combining creative thinking, technology expertise, and global reach. The Company has allotted 1, 14, 84,72,332 fully paid-up equity shares of face value ` 5 each in June 2015 to the shareholders of the Company in proportion of 1:1 and consequently, the number of shares increased from 1,14,84,72,332 to 2,29,69,44,664.The Company allotted 57,42,36,166 fully paid up equity shares of face value ` 5 each in December 2014 to the shareholders of the Company in proportion of 1:1 and consequently, the number of shares increased from 57,42,36,166 to 1,14, 84,72,332.It was on October 10, 2014, that the company had recommended a bonus issue of one equity share for every equity share held (1:1 bonus issue).It fixed December 3, 2014, as the record date for the purpose of allotment of bonus shares / stock dividend. The company has mentioned in the Board of Directors report that sufficient cash balance has been kept by the company to meet its strategic objectives. The company presently generates sufficient cash internally to finance all its operational, financing and investment requirements. The

Announcement date of Bonus Issue – 24/4/2015 and Ex-Bonus Date – 15/6/2015

QUESTIONS

1. Determine the total number of subscribed shares of ABC Ltd. in November 2014.

2. Find out if there is any possibility of arbitrage opportunity both domestically and internationally.

3. How market has reacted to the bonus announcement and what may be the reason for the same.

4. Explain with reasons the effect of EPS on the Bonus Issue

5. Discuss by referring to relevant regulations of SEBI the following:

- Board of Director's meeting regarding bonus issue was held on 1st April, 2015. Within what period the bonus issue shall be implemented. Also, discuss the necessary approvals required in this respect.
- Basic earnings per share and diluted earnings per share are equal. Discuss the reason for this effect.
- The company has decided to make a bonus issue. However, later it wants to withdraw it. Can it do so?

Case Study Number	**IV**
Level of teaching	**L3**
Program outcomes covered	**P02,P03, P04, P05, P06,**
Course outcomes covered	**C305.2**

AUTOMATION OR INSIDER TRADING MANAGEMENT SYSTEM

One fine morning Zahir woke with the beep sound of What Sapp message in his mobile. Half woke up thinking it to be some urgent message from his boss read the message from his one friend Joseph who accidently sent the same to him instead of Tahir. Joseph who is lawyer by profession and employed with a leading law firm handling the legal matters listed companies. Last year he was also handling a legal case of Rajendra Holidays. Since Zahir has no interest in the Stock Market without understanding the message further forwarded the same to his friend Kanjibhai (a jobber in stock market).A few days later Zahir received a call from Kanjibhai inviting him on a party bash at coming Saturday at one of the 5 Star Hotel of the city. To the utter surprise of Zahir, Kanjibhai who never offered a cup of tea to anyone and always in debt is organizing such a big party. Zahir called back Kanjibhai to know the exact of organizing such party. Kanjibhai expressed there is no special occasion only few of his friends have been invited as a matter of change from daily life. On Saturday evening Zahir reached the venue of party where other friend was already there. On asking what is reason for this party from all friends, Kanji told he made a huge profit from the stock market and after repaying his old debts now he is buying a small office of his own to work as sub-broker. During the party after consuming a lot of alcohol Kanji gone out of control and started shouting it is because Zahir who made him rich. Since earlier one or two occasions Kanji had gone out of control after consuming alcohol no one paid heed to his loose talks. Next morning as a daily routine Zahir was enjoying reading a financial daily. One news catches his attention. Although Zahir had no interest in the Stock Market but the amount of penalty was enough to further read the news. Further he compiled some of actual information of these listed companies from website.

Questions

After reading the news he approaches you requesting you to provide him a report on the under-mentioned five questions. How the financials of the company depicts about the unfair role of insider trading in the stock market and what course of action can be followed by such insiders on receiving such information? Why is it so difficult to monitor messages passed on through What Sapp? What is the way out to track such messages?

1. What is the meaning of the term ‘insider’ and ‘unpublished price sensitive information’ in SEBI Guidelines?

2. What amendments have been made Government to curb the practice of Insider Trading?

3. Whether Joseph can be called as insider trader or not?

4. How the introduction of Automation or Insider Trading Management System (ITMS) seems to curb the menace of insider trading?

Case Study Number	V
Level of teaching	L3
Program outcomes covered	P01, P02, P04, P05, P06,
Course outcomes covered	C305.5

RISK EXPLORATION USING CAPM EXEMPLARY

CIP is a non-listed company. The Board of Directors has convened a special Board meeting to review two investment opportunities and, at the request of the new Finance Director, decide on an appropriate discount rate, or rates, to use in the evaluation of these investments. Each of the two investments being considered is in a non-listed company and will be financed 100% by equity. In the past, CIP has used an estimated post-tax weighted average cost of capital of 12% to calculate the net present value (NPV) of all investments. The Managing Director thinks this rate should continue to be used, adjusted if necessary by plus or minus 1% or 2% to reflect greater or lesser risk than the “average” investment. The Finance Director disagrees and suggests using the capital asset pricing model (CAPM) to determine a discount rate that reflects the systematic risk of each of the proposed investments based on proxy companies that operate in similar businesses. The Finance Director has obtained the betas of two listed companies (Company A and Company B) that could be used as proxies. These are

Particular	Beta value
Company A (proxy for Investment 1)	1.3
Company B (proxy for Investment 2)	0.9

The expected annual post-tax return on the market is 8% and the risk-free rate is 3%. The Managing Director and the other Board members are confused about the terminology being used in the CAPM calculation and do not understand why they are being asked to consider a different method of calculating discount rates for use in evaluating the proposed investments.

Case Study Number	VI
Level of teaching	L3
Program outcomes covered	P01, P02, P04, P05, P06,
Course outcomes covered	C305.3

STOCK MARKET FLOTATION DENIGRATION

SB plc (SB) is an unquoted entity that provides technical advisory services and human resources to the oil exploration industry. It is based in the UK, but operates worldwide. It has been trading for 15 years. The four founding directors work full time in the business. Other employees are a combination of full time technical consultants and managers, and experts retained for specific contracts. Recruiting and retaining qualified consultants is a challenge and SB has to offer very competitive remuneration packages. The market for the type of services that SB offers is growing. The large multinational oil entities are currently looking at exploration possibilities in the Caribbean. This will open up substantial new opportunities for SB which will require additional funding. However, the concessions for operating in this region are still under discussion with the various Caribbean governments and the oil multinationals have not yet started formal bidding. In recent years, SB has been informally approached by some of its competitors and also its major customers to sell out. The directors have so far rejected these trade sale approaches but are now re-considering the possibilities. An alternative also being considered is an Initial Public Offering (IPO), that is, a stock market flotation. Assume today is 1 January 2009

Current Financial information

• Revenue in the year to 31 December 2008 was £40,250,000 and earnings (profit after tax) were £20,188,000. There are five million shares in issue owned equally by the four directors. No dividends have been paid in any year to date

. • Net book value of buildings, equipment and vehicles plus net working capital is £22,595,000. The book valuations are considered to reflect current realizable values.

• SB is currently all equity financed. Forecast Financial information

• Sales revenue for the year to 31 December 2009 is expected to be £52,250,000.

• Growth in revenue in the years to 31 December 2010 and 2011 is expected to be 20% per annum.

• Operating costs, inclusive of depreciation, are expected in the future to average 60% of revenue each year.

• Assume that book depreciation equals tax depreciation and that profit after tax equals cash flow.

• The marginal rate of tax is expected to remain at 28% per annum, payable in the year in which the liability arises.

• Assume from 2012 onwards that the 2011 pre-discounted cash flow will grow at 6% per annum indefinitely. This assumes that no new long-term capital is raised. If the entity is to grow at a faster rate then new financing will be needed. Industry statistics The average P/E ratio for the industry, using a very broad definition, is 12 with a range of 9 to 25. The average cost of capital for the industry is 12%. Cost of capital figures by individual entity is not available. Analysis Market value of the firm

Case Study Number	**VII**
Level of teaching	**L3**
Program outcomes covered	**P01, P02, P05, P06,**
Course outcomes covered	**C305.3**

INVESTMENT MARKET FINANCING MODEL

Poshpaws is a company which has recently been listed on the Alternative Investment Market. Its main business is developing new applications for the iPhone and it is currently looking to develop a new application that allows players to throw wet sponges at various contemporary villains (politicians feature highly). This new application requires that £20m of new finance should be raised. Until now, the company has used simple methods of evaluating investments such as payback. However, now that they are listed, the recently newly appointed accountant believes that they should be considering a more scientific method of evaluating investment opportunities. He also believes that the capital structure should be considered as a tool for maximizing shareholder value rather than just a way of getting money as easily as possible. The accountant, being a graduate of only a few years, can remember his old professor of finance explaining about theories developed by Modigliani and Miller and believes his employer can benefit from the insights that arise from these theories of capital structure. The Poshpaws Company is financed using the following methods: 1. Equity. The company has 10 million shares, which are trading at £8.00 per share. It has an equity beta of 1.2. 2. Preference shares. Poshpaws has ten million £1 5% preference shares, which are trading at £0.90. 3. Debt. Poshpaws has £10m (at par value) of 10% debentures, which are redeemable at par in five years' time. The debentures are currently trading at £105. The return on the market is 8% per cent and risk free government gilts are currently trading at 3%. The corporate tax rate is 30 per cent. The new accountant believes that adding substantial debt will be more beneficial than raising extra equity. However, the Chief Executive believes that the least debt the better and cannot see any merit in adding to what he already believes is too much debt.

Case Study Number	**VIII**
Level of teaching	**L3**
Program outcomes covered	**P01, P02, P05, P06,**
Course outcomes covered	**C305.3**

MAXIMIZING SHAREHOLDER PAYOUT EXPLORATION

Blue is a multinational furniture retailer listed on its local stock exchange. It has experienced rapid growth in recent years, partly via acquisitions and partly by generic growth. A substantial proportion of the shareholders are institutional investors but there is also a significant proportion of shares held by private individuals. Blue follows a conservative dividend policy, paying a relatively low dividend with a small but steady growth in dividend levels. This has led to the accumulation of surplus funds. Mr B, a director of a major institutional shareholder of Blue, has recently requested that surplus funds be returned to shareholders. The Directors of Blue are currently considering this request. Green is a privately-owned, family-run small furniture retail chain with just 10 shareholders. Historically, Green's dividend payouts have varied considerably year-on year. Recent payouts have been between 10% and 50% of profit for the year, largely depending on investment opportunities available. In the current year, the shareholders have not been able to agree on an appropriate level of dividend. Mr G, one of the shareholders, is planning a major extension on his house and has requested a large dividend payment. However, the other shareholders wish to retain cash within the company for investment in future projects. Both Blue and Green have the primary financial objective of maximizing shareholder value.Jusitfy your comment

Case Study Number	IX
Level of teaching	L3
Program outcomes covered	P02, P05, P06,
Course outcomes covered	C305.3

NEW VENTURES EXPANSION

Computer Tech Ltd. is one of the leading information technology outsourcing services providers in India. The company provides business consultancy and outsourcing services to its clients. Over the past five years the company has been paying dividends at high rate to its shareholders. However, this year, although the earnings of the company are high, its liquidity position is not so good. Moreover, the company plans to undertake new ventures in order to expand its business. In context of the above case:

1. Give any three reasons because of which you think Computer Tech Ltd. has been paying dividends at high rate to its shareholders over the past five years.
2. Comment upon the likely dividend policy of the company this year by stating any two reasons in support of your answer

Case Study Number	X
Level of teaching	L3
Program outcomes covered	P02, P05, P06,
Course outcomes covered	C305.1

SHORT TERM CAPITAL REQUIREMENTS OF BUSINESS.

Bhutan inherited a very large area of agricultural land in Haryana after the death of his grandfather. He plans to sell this piece of land and use the money to set up a small scale paper factory to manufacture all kinds of stationary items from recycled paper. Being an amateur in business, he decides to consult his friend Subhash who works in a financial consultancy firm. Subhash helps him to prepare a blue print of his future business operations on the basis of sales forecast in next five years. Based on these estimates, he helps Bhutan to assess the fixed and working capital requirements of business.

In context of the above case:

1. Identify the type of financial service that Subhash has offered to Bhutan.
2. Briefly state any four points highlighting the importance of the type of financial service.