

W. P. CAREY

SCHOOL *of* BUSINESS

ARIZONA STATE UNIVERSITY

**MBA SIM**

**Fund**



*Board Presentation*

*May 1, 2009*

# 2008-2009 Student Managers



*Colin Nelson*  
*W.P. Carey MBA*  
*Finance*  
*Class of 2009*



*Jeremy Kelstrom*  
*W.P. Carey MBA*  
*Finance & Real Estate*  
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*Bill Pappa*  
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*Real Estate*  
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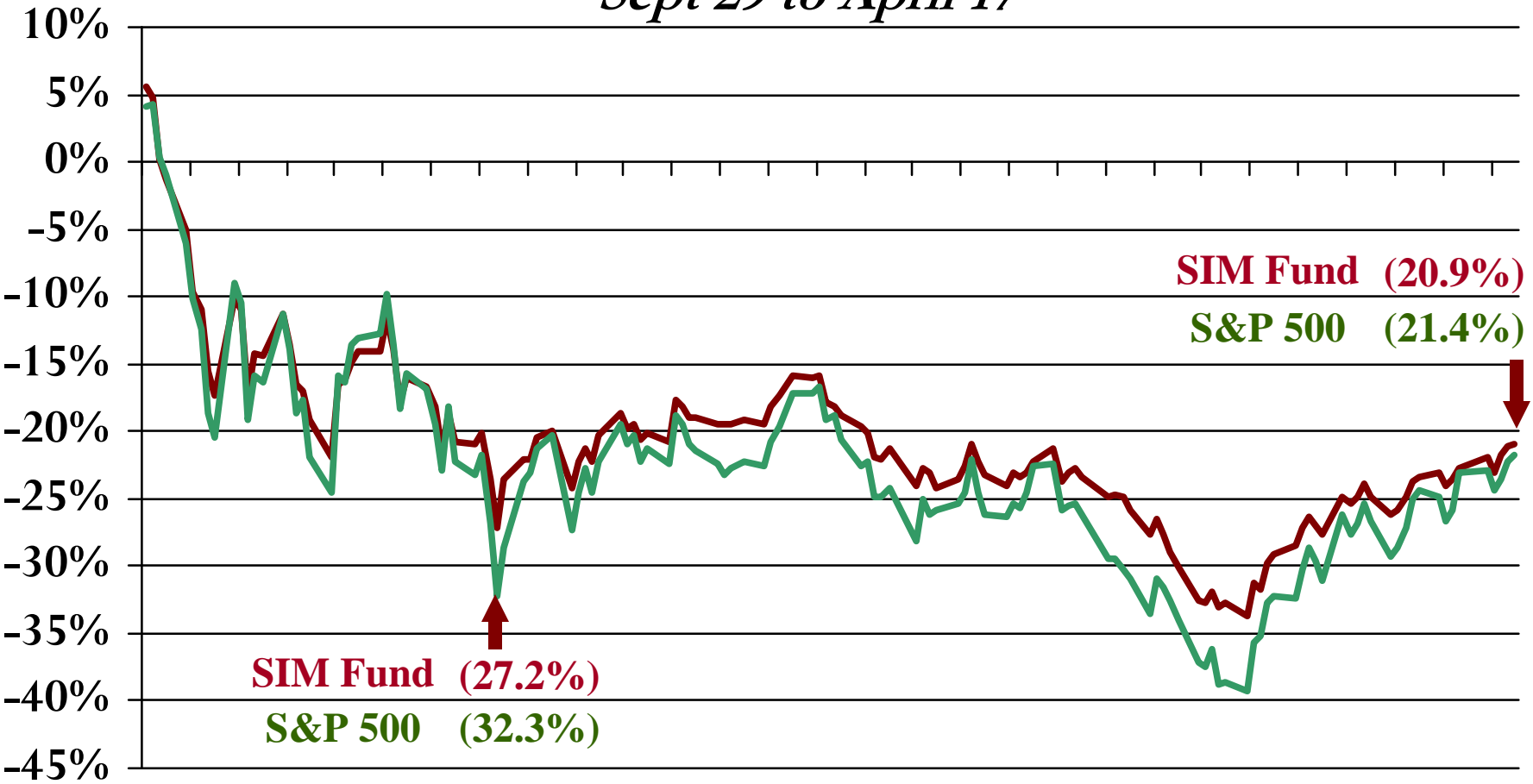


*Jay Krumme*  
*W.P. Carey MBA*  
*Finance*  
*Class of 2009*

- Overview
  - Fund Objectives
  - Economic Outlook
- Portfolio Holdings
  - Additions and Removals
  - Selected Stocks
- Performance
  - Portfolio
  - Attribution

## Returns

*Sept 29 to April 17*





# Overview

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- Long-term investment strategy
- Minimum 70% equity
- Low cash reserve
- No short selling
- \$750MM market cap
- Limits on derivatives

- Screening criteria for stocks
  - Low beta relative to industry
  - High dividend yield
  - Industry leaders
  - International exposure
  - High balance sheet cash relative to debt
  - Strong capital expenditure

# Fund Characteristics

	SIM Fund	S&P 500
Market Cap (\$B)	55.83	64.48
Dividend Yield	4.89	3.15
Price/Earnings	12.14	14.25
Forward PE	11.82	14.59
ROE	26.32	19.16
Price/Cash Flow	7.91	8.29
5 Year Beta vs S&P 500	0.72	0.96



- Based on finance capstone project
- Economic model inferred from historic economic indicators
- Model Drivers



- Model Predictions
  - GDP Recovery in Q3 2009
  - End of Bear Market early Q2 2009

- Was our forecast right?
  - Current market shows some signs of stabilization
  - PCE ticks up in January and February
  - Dow rebounds from low of 6,547 on March 9

# Retrospective

**Dec. 23<sup>rd</sup>** – Oil hits low price per barrel of \$30.28

**Feb 17<sup>th</sup>** – Economic Recovery and Stimulus Act

**March 9<sup>th</sup>** – Dow and S&P hit lows of 6,547.05 and 676.53, respectively

**April 2<sup>nd</sup>** – Mark-to-Market rules eased by FASB

Zoom: [1d](#) [5d](#) [1m](#) [3m](#) [6m](#) [YTD](#) [1y](#) [5y](#) [10y](#) [Max](#)

Nov 20, 2008 - Apr 17, 2009 +134.05 (1.68%)



**Jan 20<sup>th</sup>** – Senator Obama inaugurated as President

**Feb. 25<sup>th</sup>** – Bank stress tests announced

**March 18<sup>th</sup>** – Fed announces quantitative easing

**April 17<sup>th</sup>** – Bank of America, Citigroup, and JPMorgan earnings week

Source: Google Finance



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# Portfolio Holdings

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# Additions and Removals



Source: Google Finance

## Reasons for Hold

- Low beta stock
  - Additionally, low beta during last recession
- International Exposure
- Defensive play given discount food
- Strong dividend yield

# McDonald's (MCD)



- Has held up well vs. S&P

Source: Google Finance



## **Reasons for Addition**

- Initially there was a debt payment concern
- We performed a cash flow analysis based on the following assumptions
  - \$35 per barrel of oil
  - \$2.50 per MMBtu of natural gas
  - \$15 billion in long-term debt

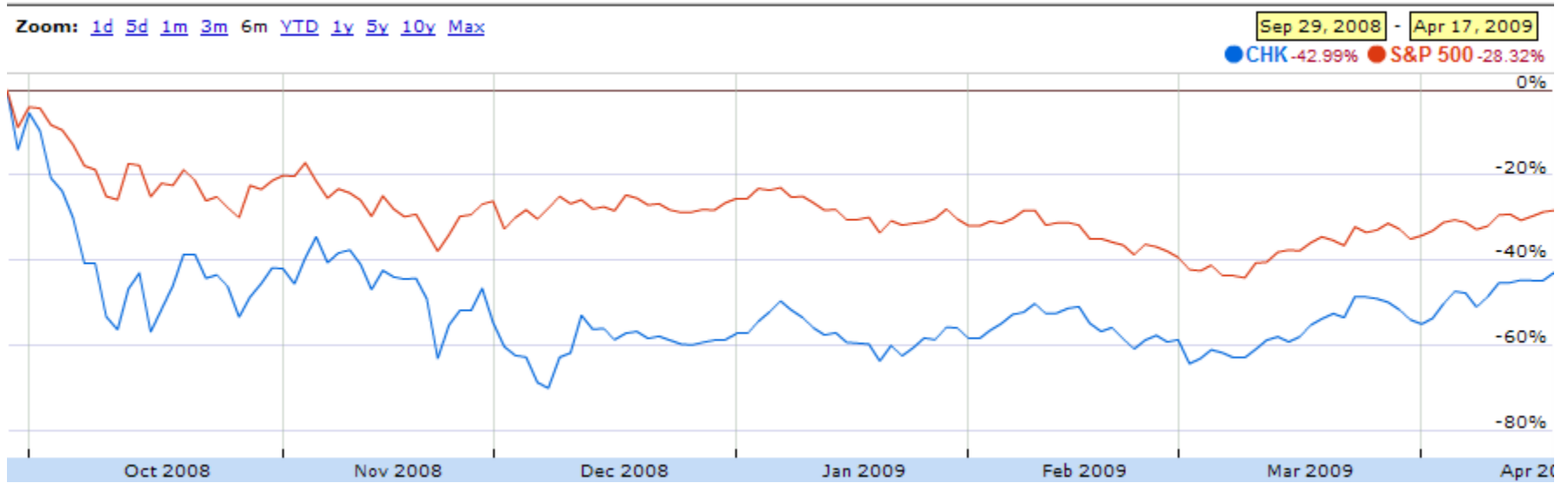
## Reasons for Addition

- Under this worse case scenario the cash from operations to debt ratio is over 2\*
- Based on this analysis we determined that CHK's stock price was unnecessarily low
- We purchased 300 more shares at \$16.35
- CHK is currently trading at \$20.80

*\*See appendix for detailed ratio analysis*

# Chesapeake (CHK)

*Sept 29 to April 17*



- Chesapeake has been highly volatile with the price of energy
- Natural Gas is currently at \$3.297 / MMBtu

Source: Google Finance

# Chesapeake (CHK)

*Nov 20 to April 17*



Source: Google Finance

## Reasons for Addition

- Diversified industrial giant
- Global exposure
- Growing operating income and ROE
- Concerns with financial unit, but assurances that capital was “adequate” (AAA credit rating)
- Beta 0.65
- Dividend yield near 5%, (later, near 10%)
- Trading at a 10-year low of \$25 at first purchase

# General Electric (GE)

**Oct 1<sup>st</sup>** – \$3B Buffet infusion, \$12B equity offering

**Dec 16<sup>th</sup>** – Immelt reiterates 31¢ dividend

**Jan 23<sup>rd</sup>** – Earnings released, 37¢ EPS. Committed to \$1.24 dividend, AAA rating

**Feb 6<sup>th</sup>** – Immelt promises “continued attractive dividends”

Zoom: [1d](#) [5d](#) [1m](#) [3m](#) [6m](#) [YTD](#) [1y](#) [5y](#) [10y](#) [Max](#)

Sep 29, 2008 - Apr 17, 2009  
 ● GE -50.92% ● S&P 500 -28.22%



**Dec 2<sup>nd</sup>** – Moodys affirms Aaa rating

**Dec 17<sup>th</sup>** – S&P affirms AAA rating, negative outlook

**Jan 27<sup>th</sup>** – Moodys puts on ratings review

Source: Google Finance

# General Electric (GE)

Feb 27<sup>th</sup> – Dividend cut  
from 31¢ to 10¢



Mar 12<sup>th</sup> – S&P cuts  
from AAA to AA+  
(stable outlook)

Mar 23<sup>rd</sup> –  
Moody's cuts  
from Aaa to Aa2  
(stable outlook)

Source: Google Finance

## **Reasons for Sell**

- Stock price fell additional 8% as market rallied from November low
- Earnings warning in early December with reduced ongoing forecast
- Increased competition
- Fit with Fund?
- Add to cash position for future investments



# Research in Motion (RIMM)



- Sold on Dec 17<sup>th</sup> (38.55% loss overall)
  - Dec 18<sup>th</sup> - Q4 guidance above estimates
  - Feb 11<sup>th</sup> - Guidance incorrect

Source: Google Finance

## Reasons for Purchase

- Dividends (Safe ones!) – 7.8%
- Recession resistant, low beta (.31)
- Brand Portfolio (#1 in major segments)
- Near monopoly (50.4% of cigarette market)
- Diversification (28.5% of SABMiller)

# Altria (MO)



- Up 16.21% overall
  - March 5<sup>th</sup> - Cigarette price change announcement
  - Recently beat estimates, no change to stock

Source: Google Finance

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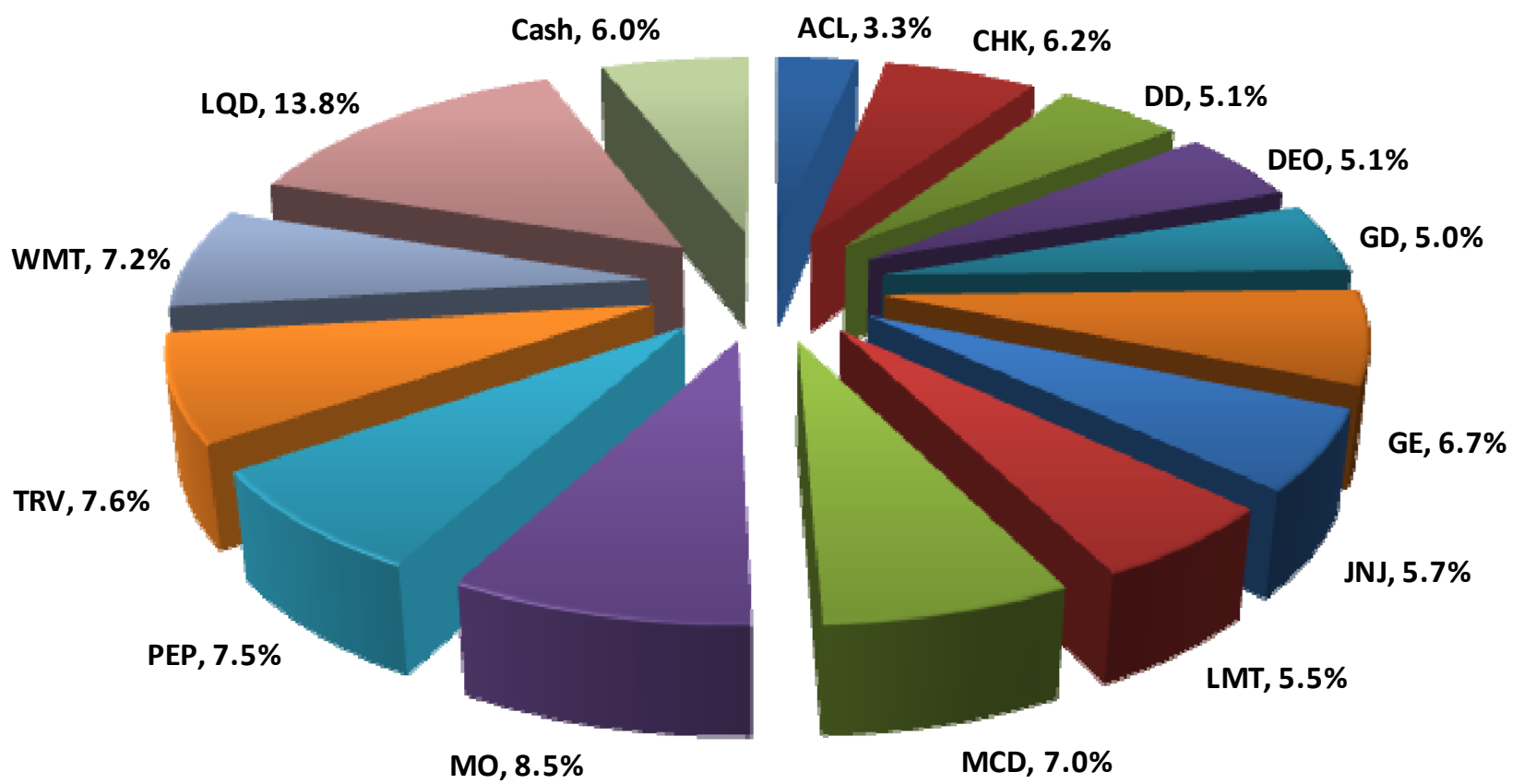
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# Portfolio Analysis

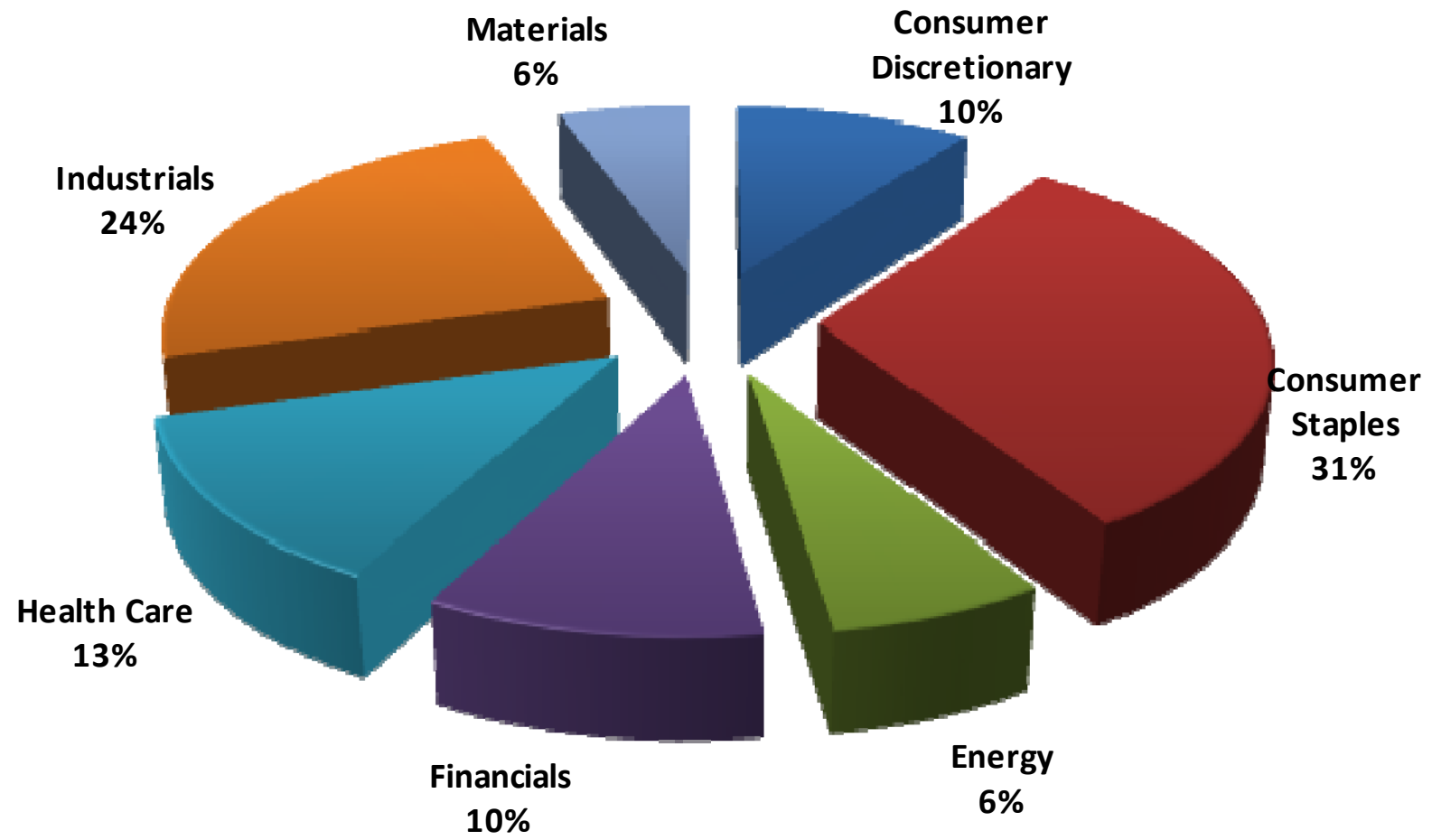
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# Asset Allocation

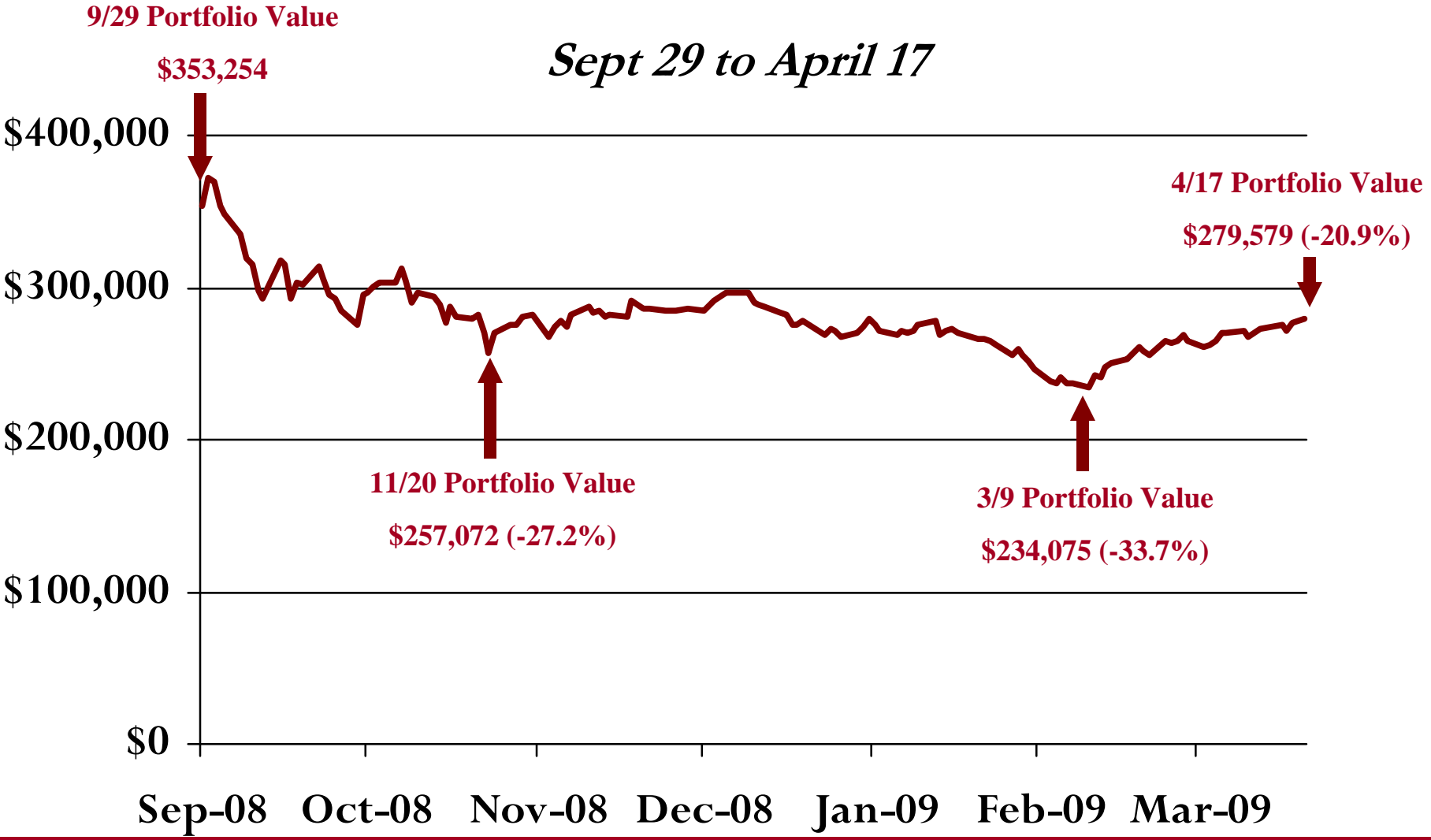


# Sector Allocation



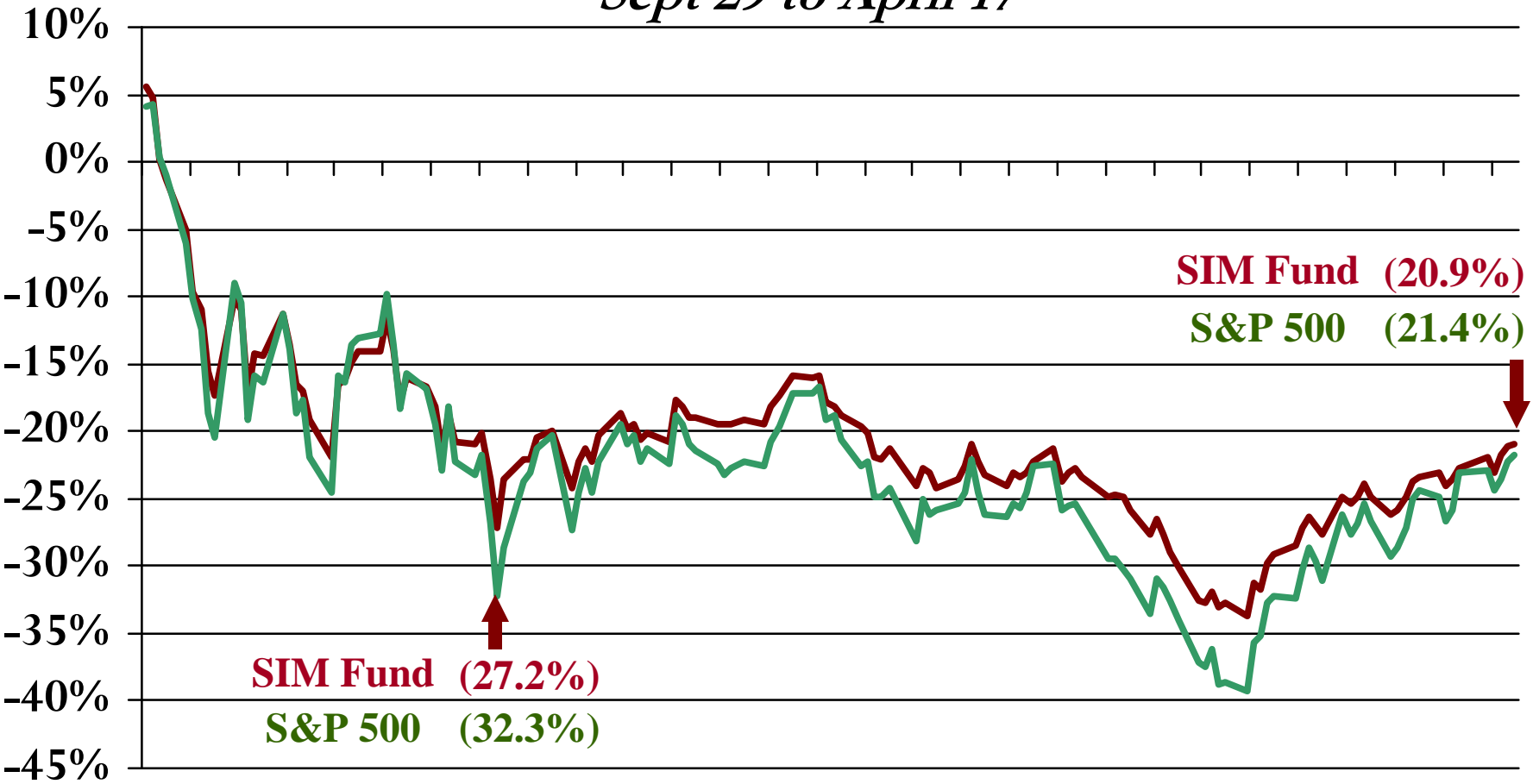
*Note: Equities only*

## Portfolio Value *Sept 29 to April 17*



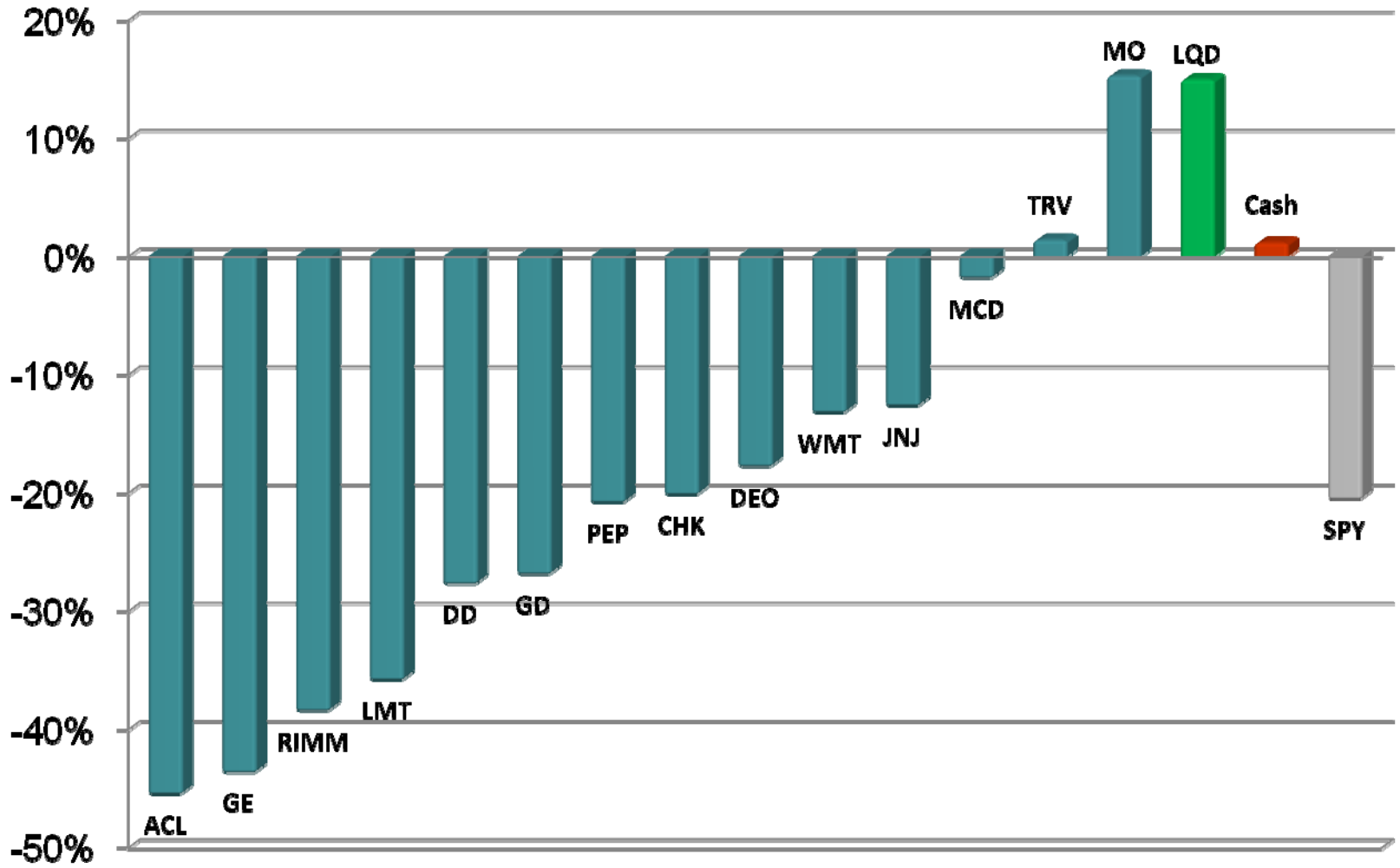
## Returns

*Sept 29 to April 17*

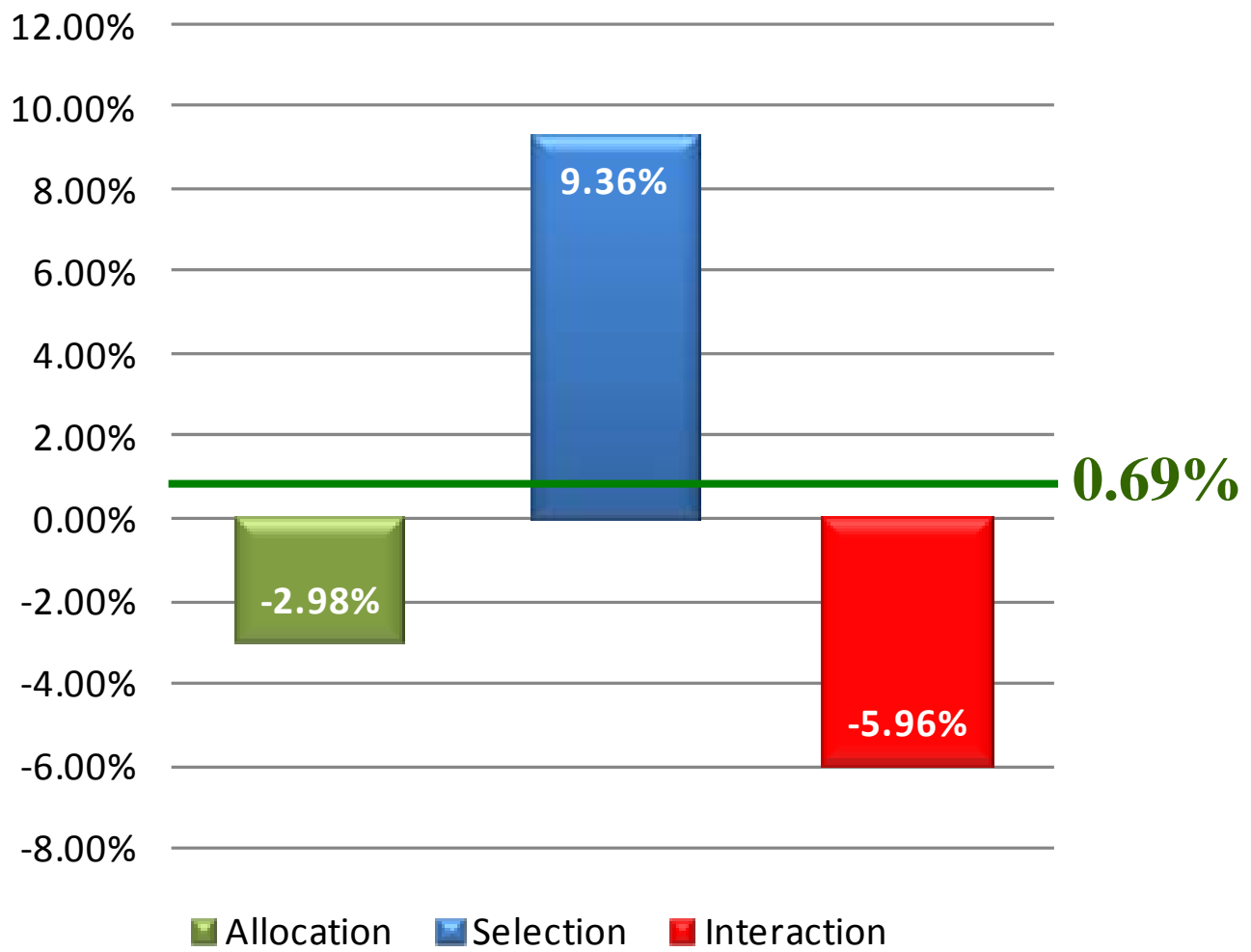




# Holding Period Returns by Security

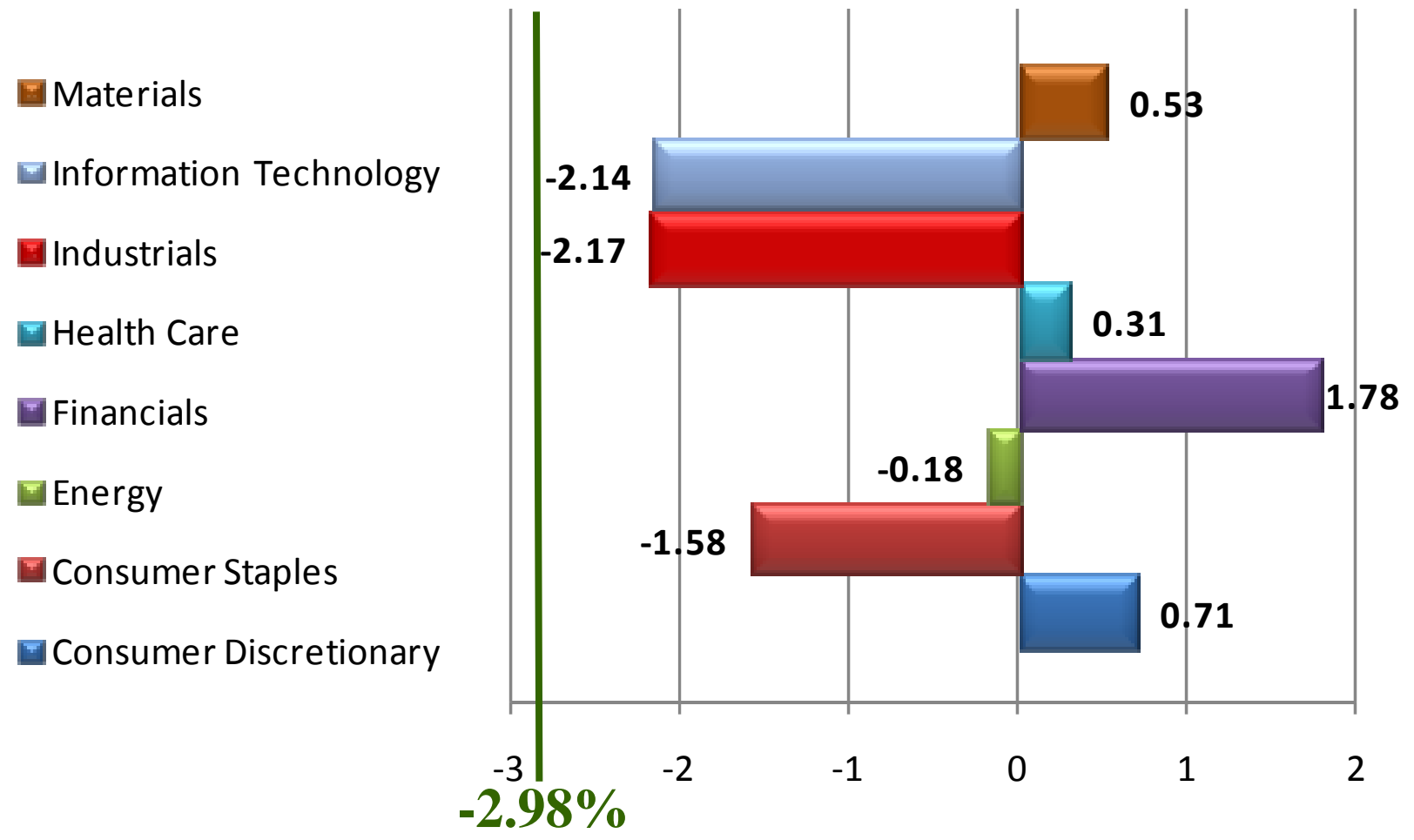


# Performance Attribution



*Note: Equities only*

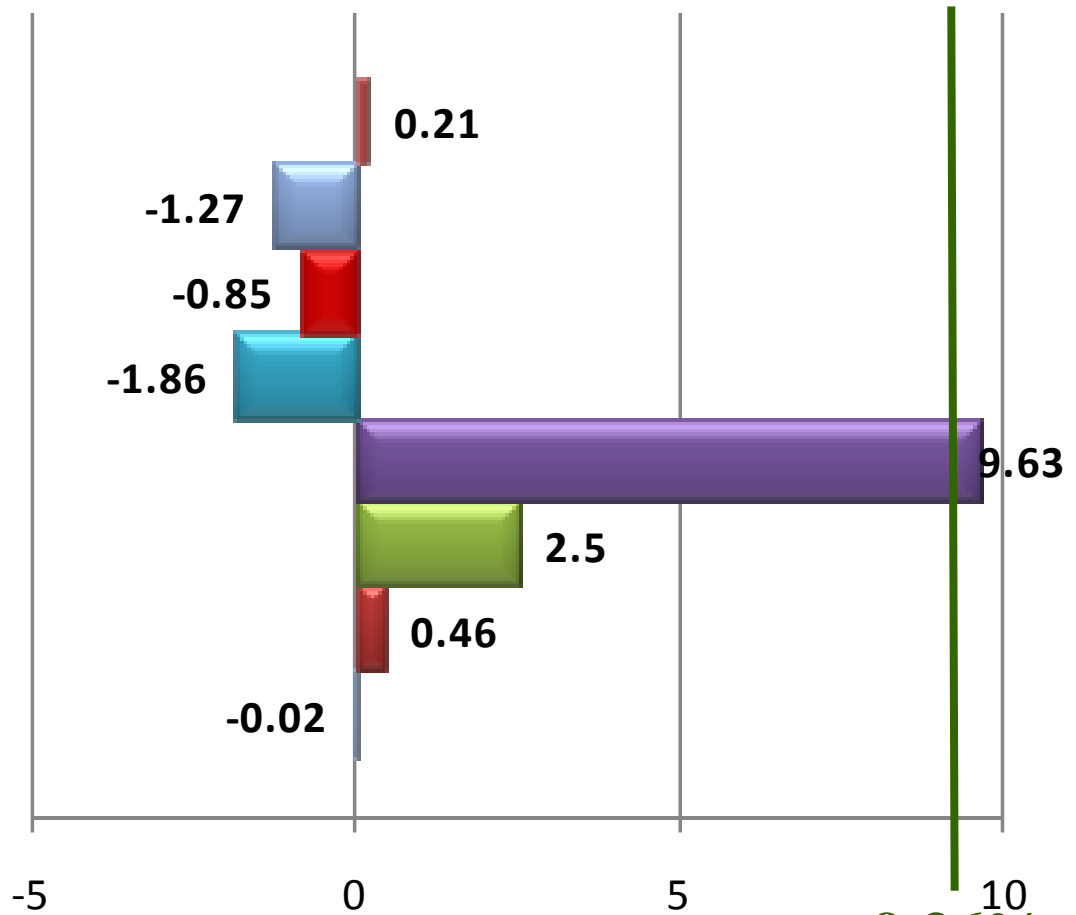
# Allocation Effect



Note: Equities only

# Selection Effect

- Materials
- Information Technology
- Industrials
- Health Care
- Financials
- Energy
- Consumer Staples
- Consumer Discretionary



9.36%

Note: Equities only

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# Takeaways

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- Corporate statements are useful, but there is no substitute for doing your own in-depth research
- Interpret CEO statements in light of their role
- Fund strategy must be driven by an understanding of economic fundamentals
- Be aware of current events, but keep a long-term view – returns are noisy

- Thank you to
  - Keith Wirtz, Justin Dammal, and Fifth Third
  - Chuck Michaels
  - Board of Directors
  - Herb Kaufman

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# Questions

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# 2009-2010 Student Managers



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*Eric Dalbom*  
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*Matt Pendleton*  
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# Appendix

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# Chesapeake Ratio Analysis

## Assumptions

Percent of Product Sold from 2007	90%
Price per barrel of oil	\$ 35.00
Price per million cubic feet of natural gas	\$ 2.50
Price growth	0%
DDA drop	80%
Interest Rate	6%

## Income Statement

	2007*	2009	2010	2011
Oil (\$ per barrel)	\$ 68.64	\$ 35.00	\$ 35.00	\$ 35.00
Amount Sold (Oil)	6,293,706	5,664,336	5,097,902	4,588,112
Oil (Sales \$)	\$ 432.00	\$ 198.25	\$ 178.43	\$ 160.58
Natural Gas (\$ per mcf)	\$ 6.29	\$ 2.50	\$ 2.50	\$ 2.50
Amount Sold (Gas)	825,437,202	742,893,482	668,604,134	601,743,720
Natural Gas (Sales \$)	\$ 5,192.00	\$ 1,857.23	\$ 1,671.51	\$ 1,504.36
Total Oil and Gas Sales	\$ 5,624	\$ 2,055	\$ 1,850	\$ 1,665
Oil and Natural Gas Marketing (Sales \$)	\$ 2,040	\$ 746	\$ 671	\$ 604
Total Sales	\$ 7,664	\$ 2,801	\$ 2,521	\$ 2,269
Total Operating Expenses	\$ 5,151	\$ 1,883	\$ 1,694	\$ 1,525
Operating Profit	\$ 2,513	\$ 918	\$ 827	\$ 744
Other expense	\$ 308	\$ 308	\$ 308	\$ 308
EBIT	\$ 2,205	\$ 610	\$ 519	\$ 436
Taxes	\$ 772	\$ 214	\$ 182	\$ 153
EBI	\$ 1,433	\$ 397	\$ 337	\$ 283

Source: Chesapeake 2007 10-K

# Chesapeake Ratio Analysis

## Cash Flow

	2007*	2009	2010	2011
EBI	\$ 1,433	\$ 397	\$ 337	\$ 283
DDA	\$ 1,971	\$ 1,577	\$ 1,577	\$ 1,577
Deferred Taxes	\$ 835	\$ -	\$ -	\$ -
Derivatives	\$ 415	\$ -	\$ -	\$ -
Cash from Operations	\$ 4,654	\$ 1,974	\$ 1,914	\$ 1,860

## Ratio Calculation

Long-Term Debt	\$ 10,000	\$ 15,000	\$ 15,000	\$ 15,000
Interest	\$ 406	\$ 900	\$ 900	\$ 900
<b>Coverage Ratio</b>	<b>11.46</b>	<b>2.19</b>	<b>2.13</b>	<b>2.07</b>

Source: Chesapeake 2007 10-K