LIBOR BENDER TRUST TEACH-IN WORKSHOP

Thursday, October 12TH 2017
WHY DO THE BENDER TRUST PROJECT?

• Build your resume
• Prep for interviews
• Get involved with LIBOR
• Prep for SMF
• Winning presentation and runner-up recognized at LIBOR Finance Summit
• Dinner with Greg Francfort, Portfolio Manager at Neuberger Berman and Co-Founder of LIBOR
DEADLINES

• Application deadline: Wednesday, October 4th, 11:59 PM
• Qualitative deadline: Thursday, October 26th, 11:59 PM
  • Company description
  • Porter’s 5 forces
  • Investment Thesis
    • Have an in-depth understanding of how the company makes money and catalysts for growth in the future
• Quantitative deadline (tentative): Thursday, November 9th, 11:59 PM
  • Valuation (P/E Multiples, Discounted Cash Flow)
• Report deadline: Wednesday, November 15th, 11:59 PM
• Final presentation date: Saturday, November 18th
BENDER TRUST RESEARCH REPORT

- 5 Components:
  - Company Description
  - Competitive Analysis
  - Forecast 2016 EPS
  - Value the stock
    - Investment thesis
  - Data box w/ EPS estimates and P/E ratios
INTRODUCTION TO INVESTING
IDENTIFYING AN OPPORTUNITY
TOP DOWN/BOTTOM UP APPROACHES

- Top Down Approach
  - Start with a promising (dying) industry and find the best (worst) company in that industry
  - Start with an interesting trend and identify the best company by which to exploit the trend
- Bottom Up Approach
  - Start with a particular company, then determine whether or not its macro prospects are promising
  - Whether it’s top down or bottom up – stick to companies and industries that you can understand
  - You need to be able to answer: How does the company make money?
BECOME AN ENGAGED READER

- Identifying General Trends
  - Ex: Tablets Replacing Textbooks or iPhones growing/decreasing in popularity
- Recognize and evaluate corporate strategies
- Reasons to Avoid
  - Poor Management – inconsistencies
  - Few Barriers to Entry (Porter’s Five Forces)
  - Bond Downgrade
  - Overly Optimistic Projections (Are their numbers believable?)
  - Market Overreaction to Positive News
  - Market Under-reaction to Negative News
PERSONAL EXPERIENCE

Products/services you’ve experienced

Fashion brands that are dying
RESEARCHING THE COMPANY

• Where to begin?
  • Read the company Wikipedia and web page for basic working knowledge
    • *How does the company make money? What industry are they in? Who are competitors?*
  • Check out recent company and industry updates to help understand the stock

• What to look for?
  • *Key Information:* stock price, market cap, analyst price estimates, P/E, industry P/E, EV/EBITDA, CEO…

• Suggested sources:
  • Company investor relations site
  • Yahoo Finance (company specifics)
  • Google News (recent developments)
  • IBISWorld (industry reports)
  • Bloomberg Terminal (compiled data, news)
  • Research analysts (experienced insight)
QUALITATIVE ANALYSIS COMPONENT
COMPANY DESCRIPTION

• One paragraph (6-10 sentences)
  • What does the company do to make money?
  • Products/Services?
  • Costs of production?

• Resources
  • 10-K/Q Statements (http://sec.gov/)
    • “Company Description”, “Business”, “Management’s Discussion and Analysis”
  • Company Website
    • “About” or “Company Profile” in Investor Relations section
  • Yahoo! Finance (http://finance.yahoo.com)
    • “Company Profile”
  • Equity Research Reports
Ralph Lauren (RL) is a global retail company focused on the design, marketing and distribution of men’s, women’s and children’s apparel, accessories (including footwear), fragrances and home furnishings. For more than 45 years, the company has boasted a strong reputation and distinctive image, which allows them to succeed as one of the most widely recognized consumer brands. Their notable brand names include Polo by Ralph Lauren, Ralph Lauren Collection, Club Monaco, Black Label, and Blue Label. Ralph Lauren sells its branded merchandise at over 11,000 different retail locations, 474 concessions-based shop-within-shops, and six e-commerce sites throughout the U.S., Canada, Europe, Asia and South America.
COMPETITIVE ANALYSIS

• One page: Porters Five Forces
  • Identify customers / suppliers
  • What are the competitive advantages / disadvantages? Size, market share?
  • Is the business getting more or less competitive?
PORTER’S FIVE FORCES

• Why use the Porter’s Five Forces?
  • Simple but comprehensive tool to better understand the strength of a company’s current competitive position and the industry context in which it operates
• Threat of New Entrants
• Bargaining Power of Suppliers
• Bargaining Power of Buyers
• Threat of Substitute Products
• Degree of Competitive Rivalry in the Industry
PORTER’S FIVE FORCES

SUPPLIER POWER
- Supplier concentration
- Importance of volume to supplier
- Differentiation of inputs
- Impact of inputs on cost or differentiation
- Switching costs of firms in the industry
- Presence of substitute inputs
- Threat of forward integration
- Cost relative to total purchases in industry

THREAT OF NEW ENTRANTS
Barriers to Entry
- Proprietary learning curve
- Absolute cost advantages
- Access to inputs
- Government policy
- Economies of scale
- Capital requirements
- Brand identity
- Switching costs
- Access to distribution
- Expected retaliation
- Proprietary products

Rivalry

THREAT OF SUBSTITUTES
- Switching costs
- Buyer inclination to substitute
- Price-performance trade-off of substitutes

BUYER POWER
- Bargaining leverage
- Buyer volume
- Brand identity
- Price sensitivity
- Threat of backward integration
- Product differentiation
- Buyer concentration vs. industry
- Substitutes available
- Buyers’ incentives

DEGREE OF RIVALRY
- Exit barriers
- Industry concentration
- Fixed costs/Value added
- Industry growth
- Product differences
- Switching costs
- Brand identity
THREAT OF NEW ENTRANTS
MEDIUM-HIGH THREAT

• No barriers to entry, changing retail landscape
• Margins low for apparel
• Economies of scale
  • Mature relationship with wholesalers
  • Global brand recognition
• Strong customer loyalty in apparel industry
  • High brand equity
THREAT OF SUBSTITUTE PRODUCTS

HIGH THREAT

- High number of substitute products available in the apparel market
  - U.S. Polo Association
- Changes in consumer preferences and trends
- Buyer inclination to substitute is high
  - Consumers are very price sensitive
  - Competing for limited disposable income dollars
Suppliers have weak bargaining power
  - RL sources raw material and production from over 400 manufacturers
Minimal switching costs
  - No one manufacturer provides more than 8% of total RL production
  - Can dissolve business relationship and find another manufacturer
Low threat of forward integration
  - Difficult to compete with established brands
Recent volatility of cotton prices
BARGAINING POWER OF BUYERS

High power

- High bargaining power due to no switching costs
- High quantity and concentration of buyers
- Relatively homogeneous product
  - Competitors have products that are similar to that of RL’s
INTENSITY OF COMPETITIVE RIVALRY

MODERATE-HIGH COMPETITION

- Many competitors in the industry (i.e. The Jones Group, Liz Claiborne, etc.)
- Low switching costs
  - Can purchase products from competitors based on the consumer’s fashion preferences
- Moderate level of product differentiation
  - Powerful branding strategy with the “POLO” name
  - High product quality with desirable fashion styles
- Relatively low exit barriers
  - Inventory can be applied to retail or wholesaled
ADDITIONAL RESOURCES

• Equity Research Reports
  • Can be found via Bloomberg Terminal (AAPL US Equity BRC<GO>)
  • Online brokerage services (TD Ameritrade, etc.)

• Company Presentations and Quarterly Earnings Call
  • Through the company’s Investor Relations website

• More information on Porter’s Five Forces
  • http://www.quickmba.com/strategy/porter.shtml
QUANTITATIVE ANALYSIS COMPONENT
3 STATEMENTS

- **Income Statement**
  - Revenues – Expenses = Net Income
- **Cash Flow Statement**
- **Balance Sheet**
  - Assets = Liabilities + Shareholders’ Equity
WHAT IS AN INCOME STATEMENT?

- Revenue – Expenses – Taxes = Net Income
- Shows financial performance of a company over a given time period
  - Pretty good indication of strength for a given company
  - Part of SEC filings both quarterly and annually (10-Q & 10-K)

- This 2 minute video gives a great example of how an income statement is made for a simple lemonade stand
  - [http://www.youtube.com/watch?v=2RupCSFcY7w](http://www.youtube.com/watch?v=2RupCSFcY7w)
SIMPLE EXAMPLE OF INCOME STATEMENT

- Revenue – COGS leads to
  - Gross Profit
- Then you subtract “operating” costs
  - SG&A (marketing, salaries, rent)
  - Also known as overhead
- You then get
  - Operating profit (profit for running the business)
  - Sometimes called EBITDA (if D&A isn’t subtracted)
- Subtract taxes and interest
  - You have net income!
WHAT IS THE QUANTITATIVE COMPONENT OF BENDER TRUST?

• Modeling an income statement
  • Forecast- make predictions to what may happen in the future
  • Shows how a company makes profits!
  • Why?
    • To determine growth profile
  • At the end
    • Compare EPS diluted with Wall St. estimates (Yahoo! Finance)
STEP 0: UNDERSTAND THE COMPANY

- Part I of the BenderTrust
- How they make money
- What their plans are
- Answer
  - How will they grow?
  - How will they stay competitive?
  - What are the new drivers for the industry?
STEP 1: LOOK AT THE 10-K

- Go into the 10-K and get the 3-5 year financial history of the company
  - Income Statement: just copy the info down into Microsoft Excel!
    - For things like Gross Profit, Operating Profit, and Net Income USE EQUATIONS FOR THESE LINE ITEMS!
  - This will allow you to:
    - See trends in the company
    - See how the company has grown in (recessions & booms)
      - Major events? Why does the company have negative revenue in one year?
      - Big jumps in revenue in another?
    - How margins have been effected (grown, shrunk?)
STEP 2: BREAK DOWN THE REVENUE (MAJORITY OF TIME)

- Example Costco
  - Revenue is broken down by
    1. Number of Stores
    2. Membership fees
    3. Sales
- Thesis on revenue?
  - More stores they open = more membership fees and sales
  - Management said - they want to increase premium members
HOW DO YOU FIND THE INFO/IDEAS FOR REVENUE?

• Where to get ideas?
  • What management planned/discussed
  • Look into the notes of the 10-K
  • Look in Seeking Alpha, abnormal returns, equity research reports, etc.
  • You can even use your own opinion!
    • OPPORTUNITY FOR FIELD RESEARCH (your own unique look!)
WHAT SHOULD YOU TRY AND SAY?

• Will volumes increase?
• Margins increase?
• Or both?
• Or none?

• ...WHY?
THE “EXPENSES”

- COGS- usually a percentage of revenue
- SG&A- wages and overhead costs
- D&A- Depreciation and amortization (allocation of cost, so look into the 10-k)
- Interest expense- payment for debt (like your student loan, credit card)
- Other items (one times loses, income from sale of operations, etc.)
THE MARGINS

- Margins represent how much a certain line item takes away (expense items) or represents (income line items) in respect to sales
  - Ex: Operating Margin = Operating Profit / Sales
    - Allows you to compare a company's efficiency, or quality of operations, to that of other companies. Operating margin is a measurement of what proportion of a company's revenue is left over after paying for variable costs of production, such as wages, raw materials, etc.
  - Ex: Profit Margin = Net Income / Sales (revenue)
    - Measures how much out of every dollar in sales a company actually keeps in earnings. Profit margin is very useful when comparing companies in similar industries.
**STEP 3: FORECAST THE LINE ITEMS USING YOUR ASSUMPTIONS**

### Income Statement Assumptions

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STEP 4: GET THE NET INCOME

- Once you subtract all of your expenses, you will end up with “operating profit”
  - Subtract operating profit by interest expense and taxes

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<td>392</td>
<td>951</td>
<td>1,258</td>
<td>1,401</td>
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<td>$0.50</td>
<td>$1.19</td>
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- Compare your EPS (diluted) to the Wall St. Estimates of EPS (diluted)
  - Your EPS > Wall St. (BUY rating)
  - Your EPS < Wall St. (SELL rating)
WHAT IS EXPECTED?

• A modeled and forecasted Income Statement
  • Show at least 3 years of financial history
  • Forecast at least 1 year but a maximum of 5 years
  • Have an assumptions page
    • Shows how much you think sales will grow, COGs, SG&A, etc.
• Be able to defend every number in the model
  • Know why revenue went up x%
  • Don’t just plug in random numbers!
STEP 5: CREATE A DATA BOX

- Use modeled and forecasted Income Statement to record EPS
- Find up-to-date data on:
  - Stock price
  - S&P 500
  - 52 week high
  - 52 week low
- Calculate historical and projected:
  - P/E
  - S&P EPS
  - S&P P/E
  - Relative P/E
Price: $102.33

S&P 500: $1,460.91

52 Week High: $137.38

52 Week Low: $82.15

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<td>149%</td>
<td>131%</td>
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DESIGNING YOUR INVESTMENT THESIS

• **Recommendation**: buy, sell, or hold?

• **Reason**: 2-3 main points of detail
  - These key points tell the story of why you want to buy, sell or hold
  - Each main point is derived by the info found in your research, both qualitative and quantitative
  - Attempt to categorize all of the reasons why you chose your recommendation
  - Ex: “I recommend CVS as a buy because the company is well-positioned to reap the benefits from a changing industry landscape, as well as its recent strategic acquisitions”

• Ask yourself: “does this story make sense to me?”
  - If you aren’t convinced, your interviewer won’t be either
  - Play Devil’s Advocate to cross-check your own argument
SUMMARY

• Maximum three pages
• Five minute presentation
  • Only the important information
• More effort = more knowledge
## POSSIBLE STOCK LIST

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<th>Company Name</th>
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<td>CAR</td>
<td>Fedex</td>
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<td>Mediaset Espana</td>
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RESOURCES

- EDGAR
  - 10-K, 10-Q, etc.
- Company websites
- Customers, employees, competitors, suppliers
- Creative intellect!
QUESTIONS?

• After you apply, you will receive weekly updates and reminders of deadlines
• Please feel free to reach out to Paul Chamesian at pchamesian@gmail.com with any further questions