Assignment #7: Multiples valuation

Date due:

- April 20, 2015, 12noon : 1) the write-up for the question numbers 1 through 5
  2) the initial draft of your recommendation. Please bring a printed copy to class

- April 22, 2015, 12noon : the final draft of your recommendation

Total Points:

- For this assignment: 100 for the write-up for question numbers 1 through 5;
  100 for the final recommendation

- If you get called upon to present: The presentation grade is a maximum of 10 points and will count towards class participation. Who will present is chosen at random. So, if you are not around to present, your presentation grade will be zero.

General instructions:

- ✓ For question numbers 1 through 5, please prepare a write-up, minimum of 2 pages, excluding tables, explaining your analysis and valuation. Double-space. Please use Times New Roman font 11 and submit the write-up via Turnitin.
- ✓ For the final draft, please follow the instructions on the template posted on the class website and submit via Turnitin.

1. Discuss the historical valuation of your stock using the multiples. Be sure to explain unusually high or low valuations (for example, SBUX's 2013 P/E is 500x and the TTM P/E is 222.2 due to a litigation charge in 2013. You want to explain whether these are one-off or continuing events.) Use data from Morningstar, and please fill in the table below.

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	TTM
Price/Earnings											
Price/Sales											
Price/Book											

2. Calculate your own historical P/E and P/S multiples for SBUX. Use the EPS reported in the income statement as the denominator in the P/E ratio. Use the revenue figures divided by basic shares outstanding (i.e., sales per share) as the denominator in the P/S ratio. You can get stock price information from finance.yahoo.com.
   - Stock price
     i. You may use a range of stock prices within the fiscal year, so you can have a range of P/Es, and P/Ss. For example, you can use the minimum and maximum stock price in a fiscal year to come up with a bracket for the multiples, you can use the average stock price to come up with an average P/E (or P/S), the median for a median P/E (or P/S), the mode for the most common P/E (or P/S).
     ii. <u>Please use the close price and not the adjusted close price.</u> Yahoo adjusts *previous* prices for any dividends and stock splits. This means that if you have a stock split in 2008, all previous adjusted close prices will be adjusted for the split; if you have a dividend in 2009 all previous adjusted close prices will be adjusted for the dividend; if you have a dividend in 2010, all previous adjusted close prices will be adjusted for the dividend, and so on. If you look in Yahoo, this week's close price and adjusted close price will likely be the same (unless your company paid dividends or had a split within the week). But if you go back two, three years or longer, there is a huge difference between the close and adjusted close price. This is because of the adjustments I just described.
     iii. So, what to do? <u>Use the close price.</u> If SBUX had a stock split within fiscal year 2010, please restrict your range of stock prices to between when the split happened and the end of the year. For example (assuming a FY end of 12/31), if within 2006-2012, your company only had a split on June 14, 2010, then for 2010, please restrict yourself to stock prices between June 15, 2010 - December 31, 2010. The same procedure will apply if the stock splits again in 2012.

You can use the following format as a guide

	2009A	2010A	2011A	2012A	2013A	2014A	Average	Median
Stock price								
Low								
High								
Average								
Median								
Basic EPS								
Sales								
Basic shares outstanding								
Sales per share (basic)								
P/E								
Low								
High								
Average								
Median								
P/S								
Low								
High								
Average								
Median								

3. Discuss the current valuation of SBUX relative to its peers. Current multiples are available from Morningstar, Yahoo Finance, and Google Finance. You can use the previous sources, the company's 10-K and other competitors you found while doing industry research for the list of competitors. Please fill in the table below.

Current Multiples (TTM)	P/E (trailing)	P/E (forward)	PEG	P/S	P/B	EV/Sales	EV/EBITDA
SBUX							
Competitor 1							
Competitor 2							
Competitor 3							
Competitor 4							
Competitor 5							

4. Using your forecast for FY 2015 or 2016, calculate a target price. Use your revenue forecast divided by basic shares outstanding to calculate a forecast sales per share. Use your forecast comprehensive operating income divided basic shares outstanding to calculate a forecast EPS. You may use any of the P/E and P/S multiples you calculated in #2 above as a basis for the future multiple that you will apply to calculate the target price. You may use the average, median, or any year/s multiple that you think would be representative of your company's future prospects. For example, if your company's best-selling product in 2006 was hotcakes and your company is planning on discontinuing the product, the multiples in 2006 may not be a good way to value the company going forward. You may also "handicap" the multiples based on some other information, but please explain your reasons for doing so. Please also fill in the table below.

	2009A	2010A	2011A	2012A	2013A	2014A	2015F	2016F
Stock price								
Basic EPS								
Sales								
Sales per share (basic)								
P/E								
P/S								

5. Choose one target price that you think best represents the most likely scenario for SBUX. Please explain your choice.

6. Please write your recommendation for the stock you are covering. The template is posted on the class website.

7. You don't need to put this in the write-up but you should know the implied expected return given by your price target. Just as a review, the formula for the total holding period return for a stock is

$$HPR = \frac{P_E - P_B + Div}{P_B}$$

You can also rewrite the HPR equation as

$$HPR = \frac{P_E - P_B}{P_B} + \frac{Div}{P_B}$$

Or, in other words,

$$HPR = capital\ gains\ yield + dividend\ yield$$

Use your target price as the ending price and today's stock price as the beginning price to calculate the capital gains yield. You can use the dividend yield from Yahoo!Finance as the expected dividend yield.