Requirements May use “Excel & Bloomberg”.

Select any three stocks traded on any regular exchange and apply on them the following valuation models:

I. Relative valuation models

1. Price earnings ratio (P/E)

a. Compute the market P/E for each stock using twelve-month trailing EPS and leading EPS. Compare P/E of stocks with a benchmark P/E to identify relatively over-, under-, and overly-valued stocks. What are your recommendations for the investors?

b. Determine P/E for each stock based on forecasted fundamentals. Compare the results with the market P/E to identify over-, under-, and overly-valued stocks. What are your recommendations for the investors?

2. Price book value ratio (P/B) Compute the market P/B and P/B based on forecasted fundamentals for each stock. Compare each stock’s two P/B values identify over-, under-, and overly-valued stocks. What are your recommendations for the investors?  Compare the results obtained in (1) and (2)

II. Absolute valuation models

Determine the intrinsic value of each of stock using the following valuation models.

1. Dividend discount model

2. Free cash flow to firm model

3. Free cash flow to equity model

Note: a) Use CAPM to estimate the required rate of return for each stock, and b) use sales growth rate and/or sustainable growth rate where required.

Based on the results obtained in each of (1), (2) and (3):

1. Identity relatively over-, under-, and overly-valued stocks. What are your recommendations on each stock?

2. Explain the possible reasons for any difference in the intrinsic values yielded by the three absolute valuation models.