SIMON FRASER UNIVERSITY
Faculty of Business Administration

FINAL EXAM

BUS 809 Equity Security Analysis 06-1
Prof. Geoffrey Poitras

EXAM INSTRUCTIONS: Answers are to be typed, single spaced of length of 1 page for each of Questions #1 and #2, 8.5"x11", with 1" margin and type point of not less than 12. (This assignment is typed in 12 point.) For questions with multiple parts, answer all parts. Violations will be subject to deductions. Exam is due in class on April 10, 2006. Deferred exam submissions must be personally approved by the instructor.

1. The Fisher (1975) approach to company analysis emphasizes the importance of "four dimensions" to assess in determining the value of a company's common stock: people factors, business factors, `the investment characteristics of some businesses' and `the price of the investment'. Using these factors to structure your answer, identify the two most outstanding common stock purchases and the least impressive common stock from all of the different sectors that were examined during the in-class presentations. For each of these three companies, what elements of Fisher's factors could not be applied?

2.a) In Memoirs of the Dean of Wall Street (1996), Benjamin Graham observed that:

> "I have little confidence even in the ability of analysts, let alone untrained investors, to select common stocks that will give better than average results. Consequently, I feel that the standard portfolio should be to duplicate, more or less, the DJIA."

Comment on the implications of this statement for the valuation of securities. In your answer be sure to provide an assessment of the validity of the statement as well as a discussion of how investment strategy would have to be formulated if the statement were correct.

b) Warren Buffett (1993), as quoted in Cunningham (2002, p.82), observes:

> "Academics ... like to define investment `risk' differently, averring that it is the relative volatility of a stock or portfolio of stocks – that is, their volatility as compared to a large universe of stocks. Employing data bases and statistical skills, these academics compute with precision the `beta' of a stock – its relative volatility in the past – and then build arcane investment and capital-allocation theories around this calculation. In their hunger for a single statistic to measure risk, however, they forget a fundamental principle: It is better to be approximately right than precisely wrong."

Explain the relevance of this statement to the development of modern portfolio theory. In your answer be sure to provide an assessment of the validity of the statement as well as a discussion of how security valuation would have to be conducted if the statement were correct.