

ASSIGNMENT 1: WHAT IS IT WORTH?

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**APPLE INC: WHAT IS IT WORTH?**

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**FINANCIAL MANAGEMENT II**

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## ASSIGNMENT 1: WHAT IS IT WORTH? 1

### ABSTRACT

Effective corporate governance helps a company in discretely making decisions that are desirable to all stakeholders. More than often, companies make catastrophic decisions as a result of poor corporate governance, leaving the burden of decision-making to the government. In one way or another, stakeholders would significantly be affected by inappropriate decision-making by the board of director. The papers; thus, investigates the qualities of effective corporate governance.

This was a case study where Apple Inc., an American technology company headquartered in Cupertino, California is being financially analyzed to evaluate its true worth. In determining the real value of Apple, its competitive advantage, bond affairs, and stock prices had to be reviewed. Furthermore, the income statements and stock values over the last 5 years were also studied.

## INTRODUCTION

Marashdeh (2014) maintains that organizational prosperity is a function of effective corporate governance; that is, the system through which for-profit organizations are directed and controlled. The interests of stakeholders – creditors, directors, employees, shareholders, government, unions, suppliers, and the society – should be fairly balanced to ensure that none feels oppressed. Corporate governance exists in two models: (1) the Anglo-Saxon model – applied in UK, US, Australia and New Zealand and (2) the Continental model which has found great use in Sweden, Finland, Denmark, France, Germany, Austria, Switzerland, and the Netherlands. Apple Inc. use the Anglo-Saxon model in its corporate governance strategy and the effectiveness of the same is reflected in the company's financial performance.

The insider (Anglo-Saxon) model of corporate governance is characterized by extreme dependence on bank finance, weak disclosure, concentrated ownership, limited freedom to merger or acquire weak legal protection of minority shareholders, and a dominate part for the stakeholders in the ownership and management in the firms (Maassen, 2002 & Marashdeh, 2014). On the hand, the outsider (the Continental) model relies mostly on equity finance, strong requirement for disclosure, distributed ownership, generous merging and acquisition freedom, reduced role of employees, creditors and other stakeholders, and strong bankruptcy regulations.

### **Apple's Competitive Advantage**

**Brand Loyalty:** Steve Jobs was and is still the man who instilled the I-just-can't-do-without-it culture for apple brands. Apple's products are based on improvement of existing ones, but the inspired designs make consumers think every idea is original. Apple is still the most celebrated brand in America and the entire world and everyone would do anything to land their hands on at least one Apple's products (Bajarin, 2011).

## ASSIGNMENT 1: WHAT IS IT WORTH? 3

**High Quality:** Although Apple outsources the better part of its operations to China, the quality of its products is still second to none. This enhances consumer trust and further explains why the company is continuing to enjoy brand loyalty (Bajarin, 2011).

**Diversity:** Apple's innovative culture makes it an almost get-everything-from-here firm. They offer products and services, both of which are superior to its competitors'.

Apple Inc. makes smartphones (iPhone), laptops (MacBook), music players (iPod), tablet (iPad), Apple TV (digital media player and a micro-console), OS X and iOS (Operating Systems), iWork (a version of MS Office), iLife (Apple Creativity Apps such as iMovie and iDVD, iWeb, iPhoto, and GarageBand) and watches (Apple Watch). The \$3.1 billion acquisition of Beats Electronics enables the company to manufacture radios and audio accessories that are sold worldwide (Johnson et al., 2012).

In addition Apple does offer services in its iTunes Store (music retail store), Apple Store (retails computers and consumer electronics), Apple Store Online, iBooks, iCloud (cloud computing and cloud storage service), iOS App Store (digital distribution system for mobile applications on iOS), and Apple Music (music streaming service) to millions of its consumers. All these services are created and maintained by Apple Inc. ("Apple Inc.: Group Written Case Synopsis").

### **Stock Performance of Total & Trailing Returns (06/30/2010-06/30/2015)**

The stock value of a company can be ascertained by investigating the financial dynamics of its stock as follows.

## ASSIGNMENT 1: WHAT IS IT WORTH? 4

<b>Total Return (07/24/2015)</b>						
	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>
<b>AAPL</b>	53.07	25.56	32.71	7.64	40.03	14.53
<b>Consumer Electronics</b>	41.41	9.79	29.81	10.95	33.38	12.94
<b>S&amp;P 500 TR USD</b>	15.06	2.11	16	32.39	13.69	1.23
<b>+/- Consumer Electronics</b>	11.66	15.77	2.9	-3.31	6.64	1.59
<b>+/- S&amp;P 500 TR USD</b>	38	23.45	16.71	-24.75	26.34	13.3
<b>Dividend Yield</b>	NILL	NILL	1.00%	2.10%	1.67%	1.54%
<b>Market Cap \$ (000,000)</b>	297,089	377,547	499,696	500,741	643,120	715,600

Source: <http://www.financial.morningstar.com>

<b>Total Return % (07/24/2015)</b>						
	<b>YTD</b>	<b>1-YEAR</b>	<b>3-YEAR</b>	<b>5-YEAR</b>	<b>10-YEAR</b>	<b>15-YEAR</b>
<b>AAPL</b>	13.96%	30.30%	14.77%	28.44%	35.36%	27.29%
<b>Consumer Electronics</b>	12.13%	26.22%	15.37%	23.40%	21.21%	10.58%
<b>S&amp;P 500 TR USD</b>	2.14%	6.775	18.31%	15.95%	7.61%	4.37%
<b>+/- Consumer Electronics</b>	1.55%	4.08%	-0.60%	5.03%	14.15% <sup>^</sup>	16.71%
<b>+/- S&amp;P 500 TR USD</b>	11.55%	23.53%	-3.55%	12.48%	27.75%	22.92%

Source: <http://www.financial.morningstar.com>

### Apple's Real-Time Stock Value

The stock value is the same as share price. Since its incorporation in 1977, Apple has been performing tremendously in matters of share value.

<b>APPLE INC. REAL-TIME STOCK VALUE</b>		
<i>As of 7/28/2015</i>		
<b>\$123.1484</b>	<b>0.3784</b>	<b>0.31%</b>
<b>Today's High</b>	<b>\$124.30</b>	
<b>52-Week High</b>	<b>\$134.54</b>	
<b>Share Volume</b>	<b>\$2,669,646</b>	
<b>Today's Low</b>	<b>\$122.77</b>	
<b>52-Week Low</b>	<b>\$93.28</b>	
<b>Previous Close</b>	<b>\$122.77</b>	

Source: <http://www.nasdaq.com>

## ASSIGNMENT 1: WHAT IS IT WORTH? 5

### Financial Analysis of Apple

Apple's performance has been improving every year. Its revenues upped from \$170.9 billion to \$182.8 billion.

<b>APPLE INCOME STATEMENT (\$000,000)</b>				
	<b>9/29/2011</b>	<b>9/29/2012</b>	<b>9/29/2013</b>	<b>9/29/2014</b>
<b>Total Revenues</b>	\$108,249	\$156,508	\$170,910	\$182,795
<b>Cost of Goods Sold</b>	\$64,431	\$87,846	\$106,606	\$112,258
<b>GROSS PROFIT</b>	\$43,818	\$68,662	\$64,304	\$70,537
<b>Total Selling General &amp; Admin Expenses</b>	\$7,599	\$10,040	\$10,830	\$11,993
<b>R&amp;D Expenses</b>	\$2,429	\$3,381	\$4,475	\$6,041
<b>Total Other Operating Expenses</b>	\$10,028	\$13,421	\$15,305	\$18,034
<b>Operating Income</b>	\$33,790	\$55,241	\$48,999	\$52,503
<b>Interest Expense</b>	NILL	NILL	(\$136)	(\$384)
<b>Interest &amp; Investment Income</b>	\$519	\$1,088	\$1,616	\$1,795
<b>Net Interest Expense</b>	\$519	\$1,088	\$1,480	\$1,411
<b>Currency Exchange Gains(Loss)</b>	NILL	(\$658)	(\$301)	(\$105)
<b>Other Non-Operating Income Expenses</b>	(\$104)	(\$92)	(\$23)	(\$121)
<b>EBT, Excluding Unusual Items</b>	\$34,205	\$55,763	\$50,155	\$53,688
<b>Gain (Loss) On Sale Of Investments</b>	NILL	NILL	NILL	(\$205)
<b>EBT, Including Unusual Items</b>	\$34,205	\$55,763	\$50,155	\$53,483
<b>Income Tax Expense</b>	\$8,283	\$14,030	\$13,118	\$13,973
<b>Earnings From Continuing Operations</b>	\$25,922	\$41,733	\$37,037	\$39,510
<b>Net Income</b>	\$25,922	\$41,733	\$37,037	\$39,510
<b>Net Income To Common Including Extra</b>	\$25,922	\$41,733	\$37,037	\$39,510
<b>Net Income To Common Excluding Extra</b>	\$25,922	\$41,733	\$37,037	\$39,510

Source: <http://www.bloomberg.com>

In addition, it has brought down the percentage of sales devoted to cost of goods sold from 62.38% to 61.41%. This factor helped Apple realize a bottom line growth from \$37.0

## ASSIGNMENT 1: WHAT IS IT WORTH? 6

billion to \$39.5 billion. Currently, Apple, Inc. nets at \$730 billion. The above table discloses the income statement of Apple between 9/29/2011 and 9/29/2014.

### Financial Ratio of Apple

#### P/E: Price-to-Earnings Ratio

Higher P/E ratios show that stocks are expensive, while lower ones indicate the stocks are cheap.

The table below demonstrates that Apple had the highest stock value in 2010 (18.7) and the lowest in 2013 (12). However, the company had been doing well stock-wise since 2010.

P/E RATIO	APPLE	
	2010	18.7
2011	13.8	
2012	15.1	
2013	12	
2014	15.7	

Source: <http://www.investopedia.com>

In 2012, Apple CEO Tim Cook authenticated dividend issuance to its shareholders for the first time in 17 years. At that time, Apple had a \$97.6 billion cash pile to give its investors dividends. The payout ratio and dividend yield are still at 23.10% and 1.63% respectively.

#### Apple Bonds

Burne and Cherney (2013) reported that Apple Inc. sold the biggest corporate-bond deal in history, \$17 billion. The bond demand was; however' \$52 billion. Deutsche Bank AG and Goldman Sachs Group Inc. sold debt for Apple to investors in all platforms of credit markets including overseas buyers and municipal-bond investors and portfolio managers who are in search of super safe government debt. The scramble was also joined by insurance companies, pension funds, and hedge funds.

## ASSIGNMENT 1: WHAT IS IT WORTH? 7

Taking advantage of a steep decline in Treasury interest rates, the technology giant borrowed the money in six portions at low costs. This was Apple's first bond in nearly two decades. Apple borrowed \$5.5 billion for 10 years at an annual yield of 2.415%. Apple also issued a 3-year debt at 0.511%, 5-year debt at 1.076% and 30-year debt at 3.883%.

Time Cook and his BOD suggested that Apple will borrow money to return \$100 billion to investors by December 2015. Despite celebrating a \$730 billion fortune, Apple's cash is at overseas banks. Wiring money back to the US would see the firm paying exorbitant taxes to the government, so acquiring cash in the bond market significantly helps in "calculated-tax evasion" (Burne and Cherney, 2013).

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