

94

**NEW YORK INSTITUTE OF TECHNOLOGY**

**FINANCE 610: Financial Policy & Value Creation**

**Final Project**

*Topic : Microsoft*

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## **INDEX**

|                                               |                         |
|-----------------------------------------------|-------------------------|
| <b>1. Executive Summary.....</b>              | <b>Pg. No 3</b>         |
| <b>2. Introduction.....</b>                   | <b>Pg. No 3</b>         |
| <b>3. Interesting facts.....</b>              | <b>Pg. No 3</b>         |
| <b>4. Fluctuations in Stock Price.....</b>    | <b>Pg. No 4</b>         |
| <b>5. The Current Ratio of Microsoft.....</b> | <b>Pg. No 4</b>         |
| <b>6. Return on Assets.....</b>               | <b>Pg. No 4 &amp; 5</b> |
| <b>7. Profit Margin.....</b>                  | <b>Pg. No 5</b>         |
| <b>8. Debit- Equity Ratio.....</b>            | <b>Pg. No 5</b>         |
| <b>9. Cash Flows.....</b>                     | <b>Pg. No 6</b>         |
| <b>10. Dividends.....</b>                     | <b>Pg. No 7</b>         |
| <b>11. Market Value Added (MVA).....</b>      | <b>Pg. No 8 to 9</b>    |
| <b>12. Economic Value Added (EVA).....</b>    | <b>Pg. No 9</b>         |
| <b>13. Analysis.....</b>                      | <b>Pg. No 11</b>        |
| <b>14. Conclusion.....</b>                    | <b>Pg. No 11</b>        |
| <b>15. Suggestions to Microsoft.....</b>      | <b>Pg. No 11 to 13</b>  |
| <b>16. References.....</b>                    | <b>Pg. No 13 to 14</b>  |

# Microsoft

## **Executive Summary:**

I have done my analysis on Microsoft for last five years and also further more as well. I have also concentrated on the fluctuations of its stock price, cash flows, trends, current ratio, debt to equity ratio, return on assets, profit margin, how much are they (Microsoft) paying as a dividend year by year for their stock holders, market value added and economic value added. I have done all this analysis in order to give some suggestions to the customers who are looking to buy the stocks of Microsoft.

## **Introduction:**

Microsoft is an American company (Redmond based located in Washington State, USA) which sells computer software, personal computers, consumer electronics and services. The most popular products of Microsoft were Windows operating system, Internet explorer, Microsoft office etc. It was founded by Bill Gates and Paul Allen in the year 1975. Microsoft is one of the most valuable brands in world; it has employees of 99,000. The most interesting thing is, it helps the government of USA if they have any bugs in their operating systems.

## **Interesting facts:**

- Microsoft had acquired Skype.
- It also acquired Nokia.
- Microsoft is trying hard to tie up with Samsung, where they (Microsoft) are aiming to ask Samsung to produce the windows phones by giving \$1 billion for the support.

- Many companies, come and go but Microsoft remains in the market forever
- Android pays some amount of money to Microsoft

### **Fluctuations in Stock Price:**

If we look at further back in the year 1999 December, Microsoft stock price reached \$58.38. But from there on, the company didn't manage to get that record price (\$58.38). The stock price was very less in the year 2009. But again in the year 2010 it went to \$ 29.29, where it again continued to have ups and downs in its price. It moved from \$25 to \$30 in the years between 2011 and 2012. Finally in the year 2013(e chart finance yahoo) the stock price of Microsoft is \$36.69.

### **The Current Ratio of Microsoft:**

The current ratio is a liquidity ratio which will measure the company's ability to pay short term obligations. If the value is more than 1 then, it is capable of paying the short term obligations (debt & payables). If the value is less than 1 then, we can say that the company is in danger.

The current ratio can be calculated by dividing Current Assets with Current Liabilities. Where in 2013(Finance Yahoo), the Current Assets of Microsoft are \$99,450,000 and Current Liabilities is \$34,623,000.  $\$99,450,000 / \$34,623,000 = 2.872\%$  in 2013. In 2012 it was 2.791%, in 2011 it was 2.92% and finally in 2010 it was 2.80 %. After calculating the current ratio we can say that, the Microsoft has no problem in paying its short term debts. Hence it is strong in the current ratio even though there are fluctuations year by year.

### **Return on Assets:**

Return on assets tells us how profitable is the company when, compared to its total assets. By looking at the return on assets, we can state that how efficient is the company using its assets to

generate earnings. The return on assets can be, calculated by dividing the Net Income with total assets. The net income in 2013 21,863 billion dollars (Market Watch) where the total assets was 142,431 billion dollars, if we divide 21,863 billion dollars/142,431 billion dollars we get a value of 0.153(15.3%). For 2012 it was 0.1400(14%), for 2011 it was 0.212(21%), for 2010 it was 0.217(21.7%).

### **Profit Margin:**

By looking at profit Margin we see how much the company is earning on every dollar of its sales. It is very useful to compare with companies in similar industries. If the profit margin is high then it indicates that, the company has more profits. If the profit margins are high, then we can say that the, company has better control over prices when compared to competitors. It can be calculated by dividing the net profit with sales. The net profit of Microsoft for the year 2013(Market Watch) was \$21,860,000 where the sales amount was \$77,650,000.  $\$21,860,000 / \$77,650,000 = 0.28$  which means, the profit margin is 28%. Similarly, in the year 2012 it was 23%, in 2011 it was 33%, in 2010 it was 30 % and finally in 2009 it was 25%. Though there are, fluctuations in profit margin year by year, nothing seems to be in danger.

### **Debit- Equity Ratio:**

It is a leverage ratio. By looking at this, we can see how suppliers, lenders, creditors and obligors are committed to the company versus what the shareholders have committed. If the leverage ratio is less then it, indicates that company is using less leverage and has a strong equity position. We can calculate the debt- equity ratio by dividing the total liabilities with shareholder's equity. If we look at 2013(Finance Yahoo) the total liabilities was \$60,707,000 where the shareholder's

equity was \$81,641,000.  $\$60,707,000 / \$81,641,000 = 0.74$  which means it was 7.4 % in 2013. In 2012 it was 8.0%, in 2011 it was 7.4 % and finally in the year 2010 it was 7.7%.

### Cash Flows:

Cash flow is the movement into or out of the company. It is used to identify the gauge of the company's financial performances. Companies which have good cash flow can invest the cash back into the business in order to generate more profits.

The Cash Flow is given below:

| Total cash Flow from Operating activities | Total cash Flow from Investing activities | Total cash flow from Financing activities | Change in Cash and Cash Equality |
|-------------------------------------------|-------------------------------------------|-------------------------------------------|----------------------------------|
| 2013- \$28,833,000                        | 2013- \$23,811,000                        | 2013- \$8,148,000                         | 2013- \$3,134,000                |
| 2012- \$31,626,000                        | 2012- \$24,786,000                        | 2012- \$9,408,000                         | 2012- \$2,672,000                |
| 2011- \$26,994,000                        | 2011- \$14,616,000                        | 2013- \$8,376,000                         | 2011- \$4,105,000                |

If we look at the cash flow, it is really huge for Microsoft (Finance Yahoo). But if we look at total from operating activities it has been decreased in 2013 when compared to 2012 it is due the changes in working capital, including increases in inventory and other current assets. Also, if we look at financial activities it is also decreased in 2013, when compared to 2012 because of \$3.5 billion increase in proceeds from issuances of debt. There is also decrease in investing activities and increase in change in cash and cash equality in 2013 when compared to 2012.

**Dividends:**

A dividend is nothing but the distribution of the company earnings, decided by the board of directors. Dividends may be in form of cash, stock or property(Y charts). The companies that provide dividends are considered as more stable companies.

In 2009 they paid 0.13, in 2010 they paid 0.16, in 2011 they paid 0.20, in 2012 they paid 0.23 and finally in now in the year 2013 they paid 0.28. This shows that even though there are ups and downs in other statements but they are always increasing the dividend pay year by year by which company will have credibility.

**Market Value Added (MVA):**

It is the difference between the current market value of a firm and the total capital that is contributed by investors. If the MVA value is higher, then we can state that the, company is in good shape. If the MVA value is negative then we can, state that the company is facing some problems. It can be calculated by subtracting invested capital in company's market value.

Market Value Added (MVA) = Company Market Value – Invested Capital

Company Market Value = (No of common shares\*share price)

+ (No of Preferred shares\*share price)

Invested Capital = Total Assets – Non-interest Bearing Current Liabilities (NIBCL) +Equity

NIBCL = Accounts Payable + Other Current Liabilities

Microsoft Company (MSFT):

End of Fiscal Year -2013:

(Numbers in Thousands (billion\$))

Company's Market Value = 287,316,000

Invested Capital = 142,431,000-34,418,000+78,944,000

= 186,957,000

MVA = 287,316,000-186,957,000

=\$100,359,000

End of Fiscal Year -2012:

(Numbers in Thousands)

Company's Market Value = 256,374,000

Invested Capital = 121,271,000-31,457,000+66,363,000

$$= 156,177,000$$

$$\text{MVA} = 256,374,000 - 156,177,000$$

$$=\$100,197,000$$

End of Fiscal Year -2011:

(Numbers in Thousands)

$$\text{Company's Market Value} = 217,776,000$$

$$\text{Invested Capital} = 108,704,000 - 28,774,000 + 57,083,000$$

$$= \$137,013,000$$

$$\text{MVA} = 217,776,000 - 137,013,000$$

$$=80,763,000$$

### **Economic Value Added (EVA):**

It is a measure of company's financial performance based on its residual wealth. It can be calculated by subtracting cost of capital in net operating profits after taxes. The net operating income of Microsoft after taxes was (For 2013) was \$21,863,000 and weighted cost of capital

was 11.7% (\$2,557,971) (stock analysis). So if we subtract \$2,557,971 in \$ 21, 863,000 we get a value of \$19,305,029 which will be the value of EVA.

### **Analysis:**

It is very common to have fluctuations in stock price of the company but the variation is not too much in the case of Microsoft. The 2013 current ratio of Microsoft which is 2.87% shows that, it is a very strong company also by seeing its current ratio year by year we can say that, they can always pay their short term obligations very easily. If we look at the return on assets, even though it is low when compared to 2009 & 10 but still we can clearly say that company is in safer side (doesn't have any danger). Profit margin is very good where it was 28% in 2013, even though it is less when compared to 2012, but still 28 % is a good profit margin. The debit- equity ratio of Microsoft is very less which is around 7.4 percent in 2013, which is also less when compared to 2012. So we can say that, they are using lesser leverage which is very safe. The cash flow of Microsoft is very strong in 2013 even it is decreased when, compared to 2012. The most successful aspect in Microsoft is their dividend payment. Even though, are lot of fluctuations in other statements, they were always increasing the dividend pay year after year which is 0.28 in 2013. They never decreased the dividend payments, this shows their credibility and proper planning. If we look at their MVA in 2013, it was around \$100,359,000 which means it has been increased from 2012 100,197,000 even though the increase is not much but still it is positive. Actually in 2012 the MVA value was decreased when compared to 2011 which was around \$137,013,000. But still those fluctuations occur in almost every company but Microsoft has improved from 2012 which is really good for the company, also EVA value shows that, the company is very strong.

**Conclusion:**

To sum up, after looking all the above aspects we can say that Microsoft is a really safe for investment. They were not able to capture a high market share in tablets but now they are trying seriously with their powerful surface which will become a substitute for laptop in future. Also they have acquired Nokia which will help them to increase the market share in mobile phones. They are also trying to collaborate with Samsung, which will really boost the company. Other than all this they have Windows which is always required now and as well as in future. **So, by doing all this analysis I would suggest to buy the stocks of Microsoft.**

**Since, I have done my analysis on Microsoft I have written a report on why Apple is succeeding over Microsoft in recent times.**

**Why do the Market leaders (Monopolies) fail at one time?****Summary:**

We all know that how Microsoft was leading the market in the industry of computer software. Also it was one of the biggest monopolists in that particular (Computer Software) industry. But today, majority of the people are thinking that Microsoft as “the Creative Spark Burning Out”.

Even though Microsoft announced Windows 8 and did a big promotion, PC sales declined to three percent when it is compared to 2011. The Statistics of the Microsoft will show us that,

customers are not interested in upgrading because still, Windows XP has 40 percent of the windows market where the Vista is having 5.7 percent more than that of Windows 8, which has a market share of just 1.75 percent.

After that, Microsoft failed miserably where once Microsoft's market domination was more than 95 percent in 2005, where now it decreased to 20 percent in 2012. Now Microsoft is no longer considered as a leader because it is losing the market rapidly year by year. Microsoft tried really hard with its team in order to compete with the Apple and Android products by releasing Surface and Windows 8, even though practically the product was good but it failed to capture the market where Surface sales were just 5 percent of I pads shipped. Also the future market would be in tablets where Microsoft failed. So that, now the people are looking at Apple, Google, Amazon, Samsung and Face book which are quite successful in analyzing the customers. The domination of Apple / Android with also the decline of PC sales is really a bad news for Microsoft. Also according to the reports there won't be a rebound in the sales of PC, because in future there won't be more than 1 PC in a house due to the strong penetration of mobile devices. Today there is a situation where, now people are really scared to invest in the stocks of Microsoft which is a bad signal for the company.

### **Analysis:**

It is really important for the companies to be able to adopt the external environment which is one of the important aspects to succeed, where lit rely Microsoft failed when compared to its competitors. (Forbes) We all know that in the present terms, PC sales are declining where the majority of the consumers are switching to smart phones and tablets but here, Microsoft failed to capture(phone and tablet market) because the Surface and Windows 8 sales were not impressive.

Also Microsoft failed to analyze the customer needs so, now a day's majority of the customers are interested in I-OS and Android because these companies are quite successful in analyzing the customer's needs.

The main failure of Microsoft was, because it failed to shift its market to mobile industry and as well as tablets which would record double volume sales by 2016. This makes Microsoft in tougher conditions. The world's richest company and as well as the leader in software development is burning out, because they are mainly concentrating on their products (Vista, Windows 8, Surface) instead of customers.

**Verdict:** Customer Orientation and the ability to adopt according to the external environment will help the company to succeed, where Microsoft should concentrate

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