

CHAPTER 1

INTRODUCTION

Nowadays, investors start looking for alternative to investment for higher returns. Investing in the stock market is an alternative to long-term savings. In the stock exchanges there are several industry groups, therefore if investor decides to invest in securities, investors should be aware of the risk or uncertainty in returns on investment, because each securities have securities yields and risks varies. So it must be analysis factors various related. The factors various are including internal and external. Internal factors are those that are directly a result of a firm's actions, and are often linked to firm profitability. External factors are those that are not in control of the firm, and may include market speculation and investors confidence. The point is, after analyzing a company and deriving an understanding of its strengths and risks, that need to compute the intrinsic value of the firm's stock and compare this to its market value to determine if the company's stock should be purchased (Brown and Reilly, 2009)

This research focuses on fundamental analysis to evaluate intrinsic value and also to forecast risk and return for security investment of EDL-Gen public company in the Laos Stock Exchange. Fundamental analysis is the stock investing method, basing on some basic factors, which have a great impact on the changes of stock value. This method is widely used in order to determine intrinsic value of shares in the market. Hence, there are approximately 90% investors using fundamental analysis

(Khan and Zuberi, 1999). Warrant Edward Buffett, he becomes rich man by invest in the stock exchange; he is an excellent example of successful people of fundamental analysis.

Fundamentals, which should be analyzed involve inside information pertaining to companies, financial statement, business activities, and both international and national economic indicators, especially microeconomics and macroeconomics. The technical used in this study will be use several model combine for analysis such as: the technical to analyze financial statement by using common-size and ratios model. The discount cash flow model (DCF) is used to determine intrinsic value of share. The holding period is used to forecast rate of return on investment, and also to find rate of risk by using standard deviation.

Most investment strategy can be classified into two major categories: technical analysis and fundamental analysis. Each category has distinguishing features that reflect investors' difference in their philosophic view of financial markets, the role of information, and the manner of which data is processed and analyzed. These are two ways that traders analyze the market as researcher also mentioned in that lesson while most people who buy and sell over the short term focus on technical analysis and most people who buy and sell over the long term focus on fundamental analysis, in an opinion of researcher both technical traders, fundamental traders, and investors can all benefit from at least having and understanding of both types of analysis even if they prefer one or the other as their primary tool they use to make

their trading decisions. This study focus only fundamental analysis for analyze risk and return on security investment, by using factors of company's financial statement for determine intrinsic value, and the data daily closing price and data daily closing price index for calculate risk and return. Indeed, there are other methods to analyze but we limit our discussion on this method for means of efficiency in modeling as incorporating many variables result in a lot of degree of freedom.

The result of this study will be help investors can use the data from study to consider as the guidelines when they are making on investment in securities appropriate, also can reduce the risk of investment and to provide a return on investment satisfaction.

1.1 Background of the Study

The stock exchange is an organization that is very important to the economic growth, development of countries and very necessary to domestic capital market. The stock market is a key player of financial sector and provides a platform to the users and suppliers of the financial resources for investment purpose. In addition the stock market is perhaps the most dynamic component of the world market, especially the Foreign Exchange or Forex stock trading market. This is because it's serves as the market for trading of securities issued by companies that registered with the securities market and to increase the liquidity of those securities. The stock exchange will be control over the trading securities to orderly, flexible and fairly as well as the

business segmentation and information services to investors in order to make a correct understanding on investment.

The stock exchange has created the country's economic growth. Country's economic has expanded, the demand of fund from both business sectors public and private increased. Borrowing money from banks is not sufficient for their demands. Funding via a stock exchange as an alternative of business which allow the development of the economy even more due the business that growth and developed must be used a lot of capital to strengthen stable to business and strength to firm, to compete with competitors easily and for develop the nation efficiently, moreover to promote savings in the country.

According to the important role of stock exchange that driven countries economic growth, therefore the Lao government has establish its first Stock Exchange and it was officially open on 10th October 2010. The LSX is a joint venture between the Bank of Lao PDR (BOL) holding the share of 51% and Korea Exchange (KRX) holding the share of 49% (www.lsx.com).

The Lao Securities Exchange (LSX) has begun trading services, creating new investment opportunities for investors in Laos. The LSX is the first capital market in the Lao PDR which will attract the huge capital to develop the nation and raising the long-term funds to companies and also promoting the integrity of Lao financial market. Thus, Lao Government deems it is necessary to establish capital market in order to collect the long-term funds for providing to companies which are required for

developing and expanding their manufacturing and services sustainably. Laos opened a stock exchange also aims to integrate with the global economy and join the World Trade Organization. The **Lao Securities Exchange (LSX)** is the primary stock exchange in Laos, located in the capital, Vientiane.

The establishment of the LSX comes in response to Lao government policy to mobilize funds for the development of the country. The stock market will also help Laos to strengthen its financial system. The government has said it requires funds of about US\$15 billion to secure GDP growth of 8 per cent over the next five years (2010-2015). About 50 to 60 percent of the funds are expected to come from the private sector. The LSX is expected to help companies mobilize long-term investment funds and also ensure more transparent business operations, which will boost the confidence of individuals and businesses considering investing in Laos.

The Laos Securities Exchange currently has just two listed stocks such as EDL Generation-Public Company (EDL-Gen), which is a subsidiary of the state owned energy company and Banque Pour Le Commerce Exterieur Lao (BCEL). The first day started trading two listed stocks of both companies successfully launched their IPOs. Share offerings have attracted significant international and domestic investor interest with oversubscription for a 25% stake of EDL and 15% of BCEL foreign investors from over 20 countries invested in EDL IPO. After the first day trading, shares of EDL rose 9.3% while BCEL surged 45%. Following its, maiden day, the

LSX Composite index finished up 15%, with Laos becoming the world's best performing market YTD.

EDL-Generation Public Company ("EDL-Gen" or "the Company") was incorporated and registered with the Ministry of Industry and Commerce on 15 December 2010. It was also the date that EDL-Gen commenced its commercial business as it entered into related Assets and Liability transfer arrangement, Concession Agreement(CA), Power Purchase Agreement (PPA) with Electricite Du Laos ("EDL" or "the parents company"). The Company is engaged in the electricity generation business from the transferred assets from EDL in which the electricity generated is sold back to EDL at agreed terms and conditions. Key assets transfer mainly represents 7 hydropower dams under a 30 years concession.

EDL-Gen initial public offering (IPO) in 2010 a number of 217,149,000 shares. It can be funding from domestic and foreign 931,998,330,000 kip (US \$116,136,864). In 2012 EDL-GEN Right Offering (RO) a number of 210,845,938 shares. It can be funding 906,637,533,400 kip (US \$ 112,976,640) and Public Offering (PO) a number of 146,773,777 shares. It can be funding 704,514,129,600 kip (US \$87,798,923). The success of funding from both companies. The LSX can pay trading tax to the Government in 2011 – 2012 amounts of 1,206,210,911 kip (US \$ 150,307) and dividend tax payment 80,660,050,303 kip (US \$ 10,051,097) (www.lsx.com).

LSX operate two years, but numbers of listed stock remain unchanged. It has just two stocks in which to invest and both are state-owned. However, it demonstrates both the extent to which capitalist structures are beginning to penetrate the farthest reaches of Asia and how opportunities are opening up in frontier markets. The first day started trading two listed stocks of both companies successfully share offerings have attracted significant international and domestic investor interest, however if we consider the overview of trading, it is not too much fluctuated base on Figure 1 (yearly closing price index that showing LSX's trading volume since opened start trading).

The reasons that make trading volume not too much volatility may because of domestic investor lack of knowledge on investment in the stock exchange. Stock exchange is a newest trend for internal investors. Moreover, a factor affecting trading in the LSX is also foreign investor's behavior, even though they are interest and confidence to both of companies but trading volume, it is not too much volatility, maybe because of government's policy that opened opportunity to buy both of shares to foreign investors just a bit, for EDL-Gen had 217,149,000 ordinary shares are being offered 25% of its shears for purchase, with 10% of its initial public offering (IPO) going to foreigner investor. Domestic investors snapped up the remaining 15%(www.lsx.com)



Source: www.lsx.com

Figure 1:Yearly closing price index 2011-2012

On January 5, 2012, EDL-Gen has decided to crease foreigner share ownership portion in EDL-Gen to not exceed 20% of the total company's share. For foreign individual investors can hold share not exceed 1% and foreign institution investors (financial institution and non-financial institution) can hold share not exceed 5% of total company's shares.(Securities and Exchange Commission, No. 021/SECO, Date: 05 Jan 2012 "Decision On increasing of foreigner).

There are many ways that traders could analyze the markets which are known as technical analysis, fundamental analysis and behavior analysis. According to Laos Security Investment that has just been emerged, imperfectly and erratically fluctuated, applying technical analysis is likely to lack preciseness and effectiveness. Fundamental analysis can be employed to security investment instead. It is very essential, since it helps the investors to choose the good stocks that result in

minimizing risks and maximizing return. From examine perform of fundamental analysis can provide information for investors to'' buy firm with low P/E ratios and sell firms with high P/E ratios (Penman, 2007). The aim of this study are fundamental analysis of company by focus only EDL-Gen in Laos Stock Exchange, although LSX have two listed companies but we limit our discussion on this company, because Electricite du Laos Generation Company (EDL) is the country's major energy enterprise, it is the main industry that drives Laos' economic growth in few years and also nowadays share of EDL-Gen is fifth of share that attracted significant investors in Asia.

1.2 Problem Identification

The Lao stock exchange is the newest and smallest stock markets in Asia with just two listed companies. It will probably be too small for alternative invest in LSX . EDL-Gen is one of the listed company trading in stock exchange which be a newly formed entity, in depth information of business available for investors are limited, combination with too much protection of the government's policy (the government give a green light to foreign investors to buy or owned shares of the company quite small volume) hence level of trading remained quiet. Most of Lao people or local investors lack of knowledge about stock exchange; don't know how to invest in the stock exchange. It can be said that most of their behavior of saving would be deposit in the bank; they scare to invest in a new business (capital market). For current local stakeholders mostly they are employees in both companies, they own the shares just waiting for dividend yield. In addition, concerning of the foreign investors, the

percentages of their investment is too much restricted by the government policy. Regarding to these concerns, the main question could be the following: **Why an investor should invest in the EDL-Gen share?** Million of shares of business firms are traded every day on the world's stock markets. The investors who buy and sell these shares ask themselves: Am I trading at the right price? What are the shares really worth? **Can the performance of fundamental analysis provide the best answer for these questions?**

1.3 Objective of the Study

- a. The objective of this study is to perform fundamental analysis, evaluate intrinsic value and analysis of risk and return for securities Investment in EDL-Gen in the Stock Exchange of Laos.

1.4 Significance of the Research

- a. The result of this study will be helpful investors in their planning and investment decisions.
- b. The results provide the guideline for rational investment and efficient development of the stock market in Laos.
- c. The results will be a reference for the government or related institution to improve LSX performance and related regulations appropriate to enhance more investors investing in LSX in the future.

1.5 Scope of the Study

The data use in this study is daily closing price and daily closing price index, which obtained from LSX market analysis and the financial statements of EDL-Gen, which collected since January 2011 to December 2012.

1.6 Limitations of the Study

- a. LSX is a new capital market in Laos which has been running for two years, so, business data and its services are remains imperfect.
- b. EDL-Gen is new listed companies in LSX, 75% of its share belong to the Government, data and market analysis regarding to this company also limited in the public sources.
- c. The information available on the internet, journals, magazines, news paper and any institution of Laos was limited.

1.7 Conceptual Frameworks

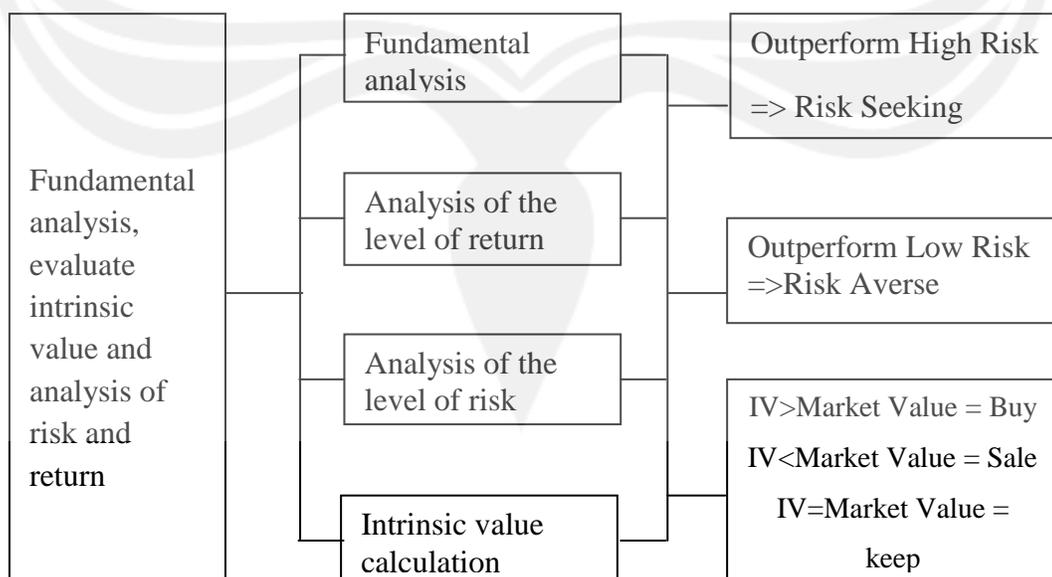


Figure 2: Conceptual Framework

1.8 Data Collection

The researchers use several sources of secondary data, including:

- a. The data from Laos Stock Exchange include, daily closing price, daily closing price index and company annual report.
- b. The data from the institutions that related to this study such as Bank of Laos, LSX, EDL-Gen, EDL du Laos, etc.
- c. The data used from published books and periodicals, government publications, annual reports of government or international organizations, academic journals & articles and previous researches and websites.

1.9 Reporting System

Chapter I: Introduction.

This chapter the contains description of the background, statement of the problem, objective of study, significance of the research, scope of the study, limitations of study, conceptual frameworks and data collection.

Chapter II: Theories and Literature Review.

In this chapter describes the literature review and theories that discusses the concepts underlying the research. There are theoretical basis, which are the review of the literature and review on related studies. The literature review wrote about the theory used in the research study to analyze the problem. The review on related studies provided overview of Laos socio-economic and some related research.

Chapter III: Research Method.

This chapter contains describes the research method with conceptual framework, data collecting method, research instrumentation and research data.

Chapter IV: Data Analysis.

This chapter includes all observations, inferences, analysis and conclusions that will be made out of the data analysis during the course of study.

Chapter V: Conclusion and Recommendation.

This chapter contains description conclusion, recommendation, research limitations and problem that will be encountered during the study will be discussed in this chapter, and also provide some suggestions for further research.