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ADRs: A Web-Based Approach to Understanding Financial Concepts in a Foreign Language

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American Depository Receipts, ADRs, provide the students of Foreign Languages for Business with the ideal venue to start working with foreign investments, while, at the same time, providing the instructors real life examples for instructional design for teaching a foreign language and, most importantly, cultural context. I initiate this discussion by explaining what ADRs are and demonstrate how they work through the use of different institutional web pages. I have chosen Telefónica’s ADR (a Spanish telecommunications company) as an example in order to illustrate how to manage such a vast amount of information by contextualizing the company in terms of industry. By analyzing different telecom ADRs from Europe (France, Germany, Britain and Italy) and Latin America (Mexico), students will become acquainted with financial concepts and the workings of international investment markets. After the completion of this exercise, students become accustomed to reading about and understanding different companies, industries and/or regions and associated economic events in the target language. In order to do so, students create and track a model portfolio of their investment decisions. Tracking this portfolio forces them to keep up with the news coming from the country they study and with the company(ies) in which they have fictitiously invested. This process provides preliminary and valuable training before venturing into the local foreign stock markets. By having gone through the aforementioned process, once the foreign stock market is approached it will be less intimidating for both student and instructor. The result of this staged approach facilitates the students’ mastering of both the vocabulary
and concepts required for conducting investment transactions in a foreign language, while concurrently developing a basic understanding of financial markets. I have included an example of this exercise in Appendix 1.

An ADR is basically a foreign stock that has been “translated” into the U.S. equity trading exchange system (NYSE or NASDAQ primarily) so it can trade as a regular U.S. stock. According to industry estimates the percentage of investors who have ADRs in their portfolios has been growing at a rapid pace. The reason for this growth is that such an investment entails a safe and easy way to diversify a portfolio while reducing risk exposure.

Before ADRs entered the U.S. market, an investor who wanted to buy offshore equities faced several significant obstacles. Not only did investors feel insecure regarding the lack of control of money overseas but they also had to account for currency risks, dividends in foreign currency, custody fees, and foreign and local taxes. To simplify the purchase of offshore equities, the Morgan Trust Company of New York created ADRs back in 1920.

ADRs are equivalent to buying stock in a foreign company. They are negotiable U.S. securities, and their security status allows them to be traded like any regular stock on U.S. stock exchanges. When investors purchase an ADR from company X, they immediately own equity in that foreign company. Investors can diversify their portfolios internationally without the problems previously attached to buying foreign stock.

From the investor’s point of view, the benefits of an ADR over buying stock in a foreign market are significant. First, there is no worry about currency exchanges or fluctuations because the transaction takes place in U.S. dollars. Second, dividends are also distributed in dollars. Third, it is easy to track foreign stocks since they are listed with regular U.S. stocks.

There are two types of ADRs: sponsored and the rarely used unsponsored. In a sponsored ADR, the issuer of foreign stock, via an investment bank, enters into a deposit agreement with a U.S. bank that agrees to act as the depository. The U.S. bank then sells ADRs while, at the same time, mediating between the foreign company and the shareholder. Specific Securities and Exchange Commission laws govern the dealings between the bank and the stock issuer, which insures additional security. The bank will distribute the dividends and also notify
the shareholder of company meetings and news such as splits or stock revisions, and all other relevant information. The foreign company is required by law to provide the bank with English versions of all corporate communication, which greatly expands the investor’s venture horizons.

It is not surprising that ADRs are already common among the leading mutual funds. Companies like Ericsson (Sweden), Nokia (Finland), BP and Unilever (U.K.), Terra-Lycos and Telefonica (Spain) are some of the top ten ADRs. Ericsson and Terra-Lycos trade on the Nasdaq, while the rest trade on the NYSE. Only companies with large market capitalization and/or potential growth for U.S. investors seek an ADR listing. As a general rule, each (American Depository) receipt represents one offshore share. The price for a company ADR differs from the stock price in the country of origin as a result of the currency exchange, which is already tallied when the stock is traded on U.S. markets.

Currently, there are over 2000 ADRs from more than 50 countries trading in U.S. markets, a figure that probably will rise as the economy becomes more global. Diversification takes on another perspective since now, in order to hedge foreign risk, the investor has to allocate weights among countries and stocks with low correlation. For example, as U.S. productivity slows or its economy weakens, equity investments in Japan and Mexico accrue additional risk due to the high correlation of these economies with that of the United States. European stocks, on the other hand, become more attractive because the contagion effect (correlation with the U.S. economy) might be weaker.

The following websites offer a good start for students to become acquainted with ADRs:

<http://www.adrbny.com>
<http://www.intltrader.com>
<http://www.wordlyinvestor.com>
<http://www.adr.com>

If students have some finance knowledge or a strong business background, it might be more interesting for them to concentrate their investment exercise on only one industry. For example, the website <http://www.adr.com> can facilitate the selection of a class portfolio, which could be based on industry, region or capitalization, depending on
the business background level or personal interest of a student. Regardless of investment approach, each student has to select one or several ADRs at the beginning of the course and then carefully track the performance of the model portfolio over the length of the course. Since ADRs are always companies with important market capitalizations and are, for the most part, key companies in their own countries, this exercise will encourage students to closely follow the overall economic performance of both country and industry.

An activity that always yields excellent results as a follow-up to the previous initial step consists of organizing a group discussion on whether the class portfolio, made up of all the ADRs chosen by the students independently of their classmates, is well diversified. Students are required to present their investment choice to their peers, and convince the rest of the class that the ADR they have chosen offers good economic prospects. As a follow-up to the presentations, the instructor allows the class to choose a portfolio of only five or ten stocks (depending on the number of students). The only requirement that students have is to try to create a portfolio that is well diversified with different stocks that present as little correlation as possible among them (whether correlated by industry, region or even companies).

Once they have chosen their ADR, the first step to accomplish is an in-depth study of the company in the target language. In order to do so, students are required to search for information about the company; usually a quick visit to the company’s website will suffice. Answers to the following questions are expected:

- When was the company created?
- Was it always a private company or has it recently been privatized?
- What does it sell? Where and how?
- Does the company have an extensive product portfolio or is it highly specialized in only one area?
- Has the company diversified its revenue? Does it have an international presence?
- Is the company a leader in its industry or country?
- What are the short and long-term goals of the company?
• How has it been performing lately? Are its later earning reports similar to those of companies in the same industry and region? Why? Why not?

As a preview of what might happen, I also ask the students to carefully track the company’s performance during the previous year. I especially encourage them to look for sharp drops or rises in the stock’s performance, and find out the causes behind such movement (interest rate cut, stock split, overall market/industry/region movement, macroeconomic news…) since this is the main goal of the exercise that they are embarking on1.

For the rest of the semester, the student will be required to keep up with all the information regarding that company. It is of vital importance that the chosen company be of a considerable size in order to facilitate the daily news gathering. The most effective way for students to successfully achieve this activity’s goals is to constantly monitor the economic press, both domestic and international, and the daily press from their ADR country of origin. For non-business trained professors, the leading newspapers from the target country, rather than specialized financial new sources, are the best resource because their non-specialized writing style is aimed at a wider audience and not just limited to the realm of financial analysts or investment bankers. Furthermore, these general newspapers usually include explanations of difficult concepts or terminology. Due to the Internet, there is a wide array of available publications, which students should read daily. Apart from the leading newspapers of each nation, different search engines offer a regional variety, for example, <http://www.yahoo.com> offers specific services in numerous countries, and a growing number of foreign newspapers can be found on <http://www.google.com>. These internet resources make the information gathering process all the more convenient. Students are expected to turn in a weekly report, in journal form, on the main events regarding their company2.

1Since students at the undergraduate level are still unfamiliar with complex financial information, a series of questions like the ones presented in the text should be enough. If students have taken advanced courses in finance, I would encourage them to analyze and report back more specific data such as all the key ratios and a more comprehensive comparison of the ADR against its competition. Again, all this information is readily available in the corporate section of the company’s webpages.

2An easier way for students to track their ADR could be to sign up for a portfolio with any financial website. For instance, <http://www.cnbc.com>, <http://www.nytimes.com>,
To exemplify this process, a student could track Telefónica (TEF, Spain), a leading ADR. First and foremost, s/he should do a competition analysis. For this particular case, students should acquaint themselves with TEF’s international competition in its sector, and evaluate the price at which TEF is selling in comparison with other leaders in the field. A quick snapshot such as Exhibit 1 should suffice.

Exhibit 1

<table>
<thead>
<tr>
<th>Symbol</th>
<th>Market</th>
<th>Last Sale</th>
<th>Net Change</th>
<th>% Change</th>
<th>Volume</th>
</tr>
</thead>
<tbody>
<tr>
<td>VOD</td>
<td>NYSE</td>
<td>$28.1</td>
<td>1.07▼</td>
<td>3.67%</td>
<td>4,305,300</td>
</tr>
<tr>
<td>TMX</td>
<td>NYSE</td>
<td>$32.95</td>
<td>0.29▲</td>
<td>0.89%</td>
<td>1,817,000</td>
</tr>
<tr>
<td>TEF</td>
<td>NYSE</td>
<td>$48.52</td>
<td>0.38▼</td>
<td>0.78%</td>
<td>693,400</td>
</tr>
<tr>
<td>FTE</td>
<td>NYSE</td>
<td>$56.96</td>
<td>0.94▼</td>
<td>1.62%</td>
<td>35,200</td>
</tr>
<tr>
<td>DTE</td>
<td>NYSE</td>
<td>$23.02</td>
<td>0.36▼</td>
<td>1.54%</td>
<td>3,841,700</td>
</tr>
<tr>
<td>TIA</td>
<td>NYSE</td>
<td>$98</td>
<td>unch</td>
<td>unch</td>
<td>0</td>
</tr>
<tr>
<td>CTC</td>
<td>NYSE</td>
<td>$13.39</td>
<td>0.11▼</td>
<td>0.81%</td>
<td>128,800</td>
</tr>
</tbody>
</table>

The next step is to find out how these companies have been performing in the last three months or so. After having presented an exhibit such as number 2, students should realize that TEF has performed above average, although its price has fallen dramatically since the beginning of March. They should find out the causes behind the drop, and also, determine why Vodafone (Britain), Deutsche Telekom and France Telecom have plunged. A quick glance at some of the local newspapers would easily provide the answer.

<http://www.wsj.com>, among many others, allow you to track an investment, and always include a section of news regarding the performance of a stock. For the class portfolio, <http://www.adr.com> is the easiest way for the instructor to follow the individual performance of the students’ choices. I strongly encourage students to sign up for a portfolio-tracking device in the foreign country. In Spain, for example, <http://www.invertia.es> not only tracks the portfolio and includes news, but also on Fridays, sends emails with all the news of the stocks performance, and the main economic news of the previous week. As mentioned before, <http://www.yahoo.com> offers information for several countries.
Once the students have done a study of the company’s background and its recent stock performance, along with the industry and regional analysis, they undertake the core of the exercise: the daily tracking of the ADR. Students are responsible for tracking the stock’s performance and reporting to the class any significant movement. Again, due to the Internet, finding this type of information is somewhat easy. I would like to emphasize again that the larger the company, the easier the information gathering. Thus, I always encourage students to select the largest ADR from the particular country or specific industry they want to study. For example, it is rare not to find information relating to TEF in almost any Spanish newspaper. Exhibit 3 shows some of the information relating to TEF as it appeared in the Spanish finance section of <http://www.yahoo.com> on March 28th, 2001, a relatively quiet day for TEF.

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3In my university, we created a website just for students looking for business news in Spanish: <http://www.wfu.edu/Academic-departments/Romance-Languages/spanish_for_business/>.  
4Please note that the price quoted is the price on the domestic market (in Euros), thus it is not the ADR. However, news will affect the price in both the domestic market and in its ADR form. Usually, both quotes tend to move in the same direction, unless there is some news that affects the industry/region differently.
Students are expected to read as many daily news sources as possible and decide which news might have had, or will have, an effect on the stock price. As a final step, they write about it in their weekly journal or final paper, depending on its relevance. It has also proven very useful for the students’ written papers and oral reports to create, from the first day of the tracking exercise, a list of vocabulary and distribute it everyday to their classmates.

At the end of the tracking period, the student will have gained an understanding of a series of key business issues: what company reports trigger stock price changes, how macroeconomic news and monetary policy affect markets, how country politics can shape financial performance for a specific stock, depending on the activity level of the tracking period. It is, however, the amount of new vocabulary and real economic material that students encounter, interpret, read and write for the reports in the target language that is the ultimate goal of the exercise and the core of any Foreign Language for Business course. In my experience, after having completed this semester-long exercise, students become skillful at quickly digesting and interpreting fundamental economic news, and consequently can proficiently convey in the target language, both orally and in written form, financial information about their ADR, region and industry. And it is a rather successful exercise since students seem to enjoy it.
Appendix

Mock write-up of TEF (ADR). Students are expected to convey in the target language all italicized words/expressions:

Telefónica (TEF) is the largest supplier of telecommunications services in the Spanish-speaking world, with a market of over 300 million clients. A growing network of domestic and international investments makes TEF one of the few telecom companies in Europe with a diversified revenue base. At present, more than 16% of the group’s annual revenues come from outside Spain. TEF is one of the world’s top ten telecommunications companies, with 2000 sales reaching $23.8 billion (net profit margin of 9.8%) (<http://www.adr.com>). TEF has invested heavily in Argentina, Perú, Brazil and Chile, among others. And, as of last week, talks about investing in Mexico’s emerging mobile phones industry were widely discussed in the press (<http://www.adr.com>).

The 7-week tracking of TEF (ADR) shows how, at the beginning of the period, the ADR performed above both the Nasdaq composite and the S+P 500. It also tracked the ups and downs of both indices very closely (for example, an uptick of more than $3.00 occurred when the Fed lowered rates). As of the end of April, however, TEF has performed substantially lower (to be discussed later).

The Telecommunications sector is still recovering from the Nasdaq’s winter plunge. Caution seems to be the underlying word when approaching this industry. The same bearish attitude permeates analysts’ opinions for European Telecommunications (ADRs). By focusing its interest elsewhere, TEF escaped the mobile licensing downfall that seriously affected British Telecom (BTY), France Telecom (FTE), Deutsche Telecom (DT) and Telecom Italia (TI). However, some contagion occurred since investors walked away in droves from the Spanish Telecom as well. As Exhibit 1 shows, they all have rebounded nicely, yet they all are still far from their 52-week highs. To make matters worse, European ADRs are, as of this last week, suffering from the gloomy reports about its economy, which irrefutably point towards slower growth and faster inflation. Furthermore, the global telecommunications ADR industry has posted a 6-month return of —
13.83% (YTD of –10%), which indicates a wait-and-see attitude. YTD returns for BT (-28.41%), FT (-28.05%), DT (-23.21%), ItaliaT (-3.42%), and TEF (-6.92%) are consistent with the bearish attitude towards European Stocks, and telecommunications in general.

TEF, when analyzed alone, has performed rather well given the less-than-encouraging economic background. Before the tracking period began, TEF successfully spun off its TEF Media branch, and its Terra Lycos division. Earnings for 2001/1Q yielded optimistic results for investors: EBITDA rose 10.9%, with revenues increasing 17.9% to 7,603 billion euros vs. last year’s results from the same period. Most importantly, its customer base increased 21.8% in its fixed and mobile telephony (8.4 million new customers) and pay-TV business, which gave TEF a net profit rise of 24.8% vs. the same period last year. At an annual rate of growth in sales of 14.26%, 11.28% average annual increase in earnings, and ROE of 12.50% over the last year, TEF seems a solid growth company in which to invest. Moreover, with a 60-month Beta of .97, TEF ADR price movements are highly correlated to that of the S&P, as Exhibit 2 shows.

However, the TEF stock price dropped significantly at the end of April. In the IBEX-35 (domestic market), TEF lost 1.8 billion euros in one day (April 22nd), a performance that was closely followed for its ADR counterpart in the U.S. market, plummeting from $53 to $47 approximately. The reason behind the fall has to do with Argentina’s struggling economy, an important source of TEF revenues. Once news about Argentina’s perennial crisis hit a new low, investors rapidly sold TEF stock. Since Argentina and Brazil amount to 50% of TEF’s EBITDA, economic and political instability will have an immediate translation on TEF’s stock performance, via a depreciation of the local currencies. As of last week, TEF’s performance has not improved due, in my opinion, to the overall uncertainty that the market in general is currently experiencing and the dismal prospects coming from Latin America.

Exhibit 1 (Top European Telecommunications ADRs)
Exhibit 2 (TEF vs. Nasdaq and S&P500)