Stock Selection Guide (SSG)

Guidelines for Beginners

This reference sheet presents basic guidelines for beginners when completing your own Stock Selection Guide.

Step 1: Perform a Quality Check on Your Selected Stock

Historical Sales and EPS Growth	Increasing sales and EPS (UP)
	Sales and EPS are growing at a steady, consistent rate (STRAIGHT)
	Sales and EPS are growing at about the same rate (PARALLEL) • Sales growing faster than EPS may be a red flag
	Is there sufficient growth for the size or the company? • Small (< $1 Billion in sales) expected growth rate > 12% • Medium expected growth rate between 7% - 12% • Large (> $10 B in sales) expected growth rate between 5% - 7%
	Has growth been slowing over recent years? • As a company gets larger, growth will slow, but check that it is not slowing down too much.
	Is recent quarterly growth in line with historical growth? • Large changes warrant investigation.
% Pre-tax Profit on Sales (Profit Margin)	Historical profit margins should be steady (even) or increasing.
	Profit margins should be as good as or better than competitors' profit margins.
% Earned on Equity (ROE)	Historical Return on Equity (ROE) should be steady (even) or slightly increasing. Significant changes, either up or down, should be investigated.
	Look for companies with at least 15% ROE. Great companies achieve return on equity of 20%.
Debt	In general, look for debt levels to be less than 33% of capitalization. • Compare to others in the industry • Consider industry averages

*** Continue the study only for companies that pass the Quality Check ***

BetterInvesting™
Empowering Investors Since 1951

Step 2: Add Judgment to Complete Your SSG

Judgment Guidelines to Keep New Investors Out of Trouble

Sales and EPS Growth Projections	Understand what the company does to make money.
	Identify items that drive and/or challenge future growth.
	The most recent trends in growth are generally considered to be the most relevant.
	Understand that growth will generally slow as a company gets larger.
	Check analyst estimates, but use these estimates as additional information rather than as a final judgment. • finance.yahoo.com • www.valueline.com • www.morningstar.com *TIP: Check your library and/or brokerage for FREE online access to Value Line, Morningstar and/or S&P.*
	A good rule of thumb is to limit growth projections to 15-20%. Use extreme caution if you estimate above 15%.
	Use extreme caution if you project EPS to grow faster than sales.
Future P/E Projections	Remove any P/Es that do not seem to fit (significantly higher or lower) from the historical average.
	Use extreme caution if you estimate future P/Es higher than the historical averages.
	In general, set future high P/E to no more than 30.
Low Price Projection	In most cases, your forecast low price should be at least 20% below the current price.
	If the upside-downside ratio is 9 to 1 or higher, then you probably need to lower your forecast low price.
Buy Criteria	Buy only when the SSG says the stock is in the BUY zone.
	Buy only when the upside-downside ratio is 3 to 1 or higher.
	Buy only when the total compound annualized return is sufficient for your portfolio. A portfolio that grows at 15% compounded annually would double your money in five years.