Relative Value





Mini Investment Class by the OKI Tri-State Chapter

Presented at OKI Annual Meeting 2011 by Marge Daniels, Director, OKI Tri-State Chapter



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It's All Relative

Definition of Relative Value

Definition of Projected Relative Value

Choosing a good time to buy or sell

Warnings and Watch Outs



Many Definitions

Fund managers compare price/earnings, price/book, or price/sales with a benchmark and then make a decision.

Relative Strength is dividing the performance of one stock by the performance of an index or of another stock.



P/E's are part of RV

Think about the company's P/E

The Average P/E is a sort of signature P/E – a measure of the normal enthusiasm that investors have for this company.

Stock prices are driven over the long term by earnings.

Deviations in P/E, not caused by earnings, will tend to seek its normal or signature level.

Historically, P/E's have ranged from 6-25



There are Many RV Definitions

INSIG SECTION 3

Current P/E Ratio divided by the co's historical 5-year average P/E Ratio

VALUE LINE

- Basic P/E = price divided by last 6 mo earnings plus next 6 mo estimated earnings.
- Relative P/E compares the P/E of a co with the median of estimated P/Es of all other co in VL



SSG Section 3

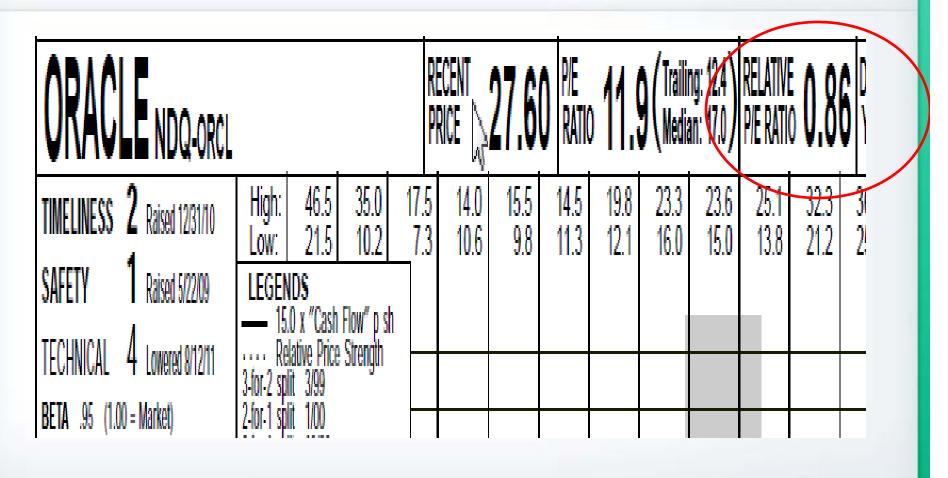
3 PRICE, PRICE/EARNINGS RATIO and DIVIDEND ANALYSIS

	CURRENT PRICE				31.850 52-WEEK HIGH		36.5	
	Fiscal Year	High Price	Low Price		EPS	High P/E	Low P/E	
1	2006	19.8	13.1		0.81	24.4	16.2	
2	2007	23.3	18.2		1.06	22.0	17.2	
3	2008	23.6	13.8		1.09	21.7	12.7	
4	2009	26.6	19.5		1.21	22.0	16.1	
5	2010	36.5	21.3		1.67	21.9	12.8	
6	AVERAGE		17.2			22.4	15.0	
	AVERAGE P/E RATIO		18.7		PROJECTED P/E RATIO		16.2	
	CURRENT P/E RATIO		18.0		PEG RATIO		1.5	
	RELATIVE VALUE		96.3		PROJ. RELATIVE VALUE		86.7	

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How to Use Relative Value

Buy company whose
Sell if RV is less than RV is less than 110%

85%

Use the whole SSG to make your decision.

Check financial news, the company web site, investor relations.



Projected Relative Value

Projected P/E Ratio divided by the 5 year average P/E Ratio

- SSG uses the future earnings which YOU estimated at the bottom of page 1.
- Don't buy a co with Projected RV above 100%

Get suspicious if it's below 80%.



What does RV Mean?

If less than 100%, the stock would be undervalued.

We strive to purchase stocks whose current P/E is not much above the average or better yet is somewhat below it.



Cautions and Watch Outs

- Interest rates
- Inflation
- Competition
- Industry Trends
- Cyclical companies
- Emerging companies
- Irrational Market
- Dividing an unrealistic current P/E by an equally unrealistic Average P/E gives a useless Relative Value



Two Cycles to Keep in Mind

Life cycle of the business

P/Es are higher when estimated growth rates are high Growth rates decline as a company matures

The business cycle of the economy Average P/Es are highly correlated with inflation rates.





Red Flags

Disappointing Qtr Results

Actual loss or not meet analysts expectations

Sales Growth

Flattening?

Pretax Profit Margins

Down for 2-3 quarters?

EPS growth

Is growth rate for last 4 quarters above industry avg?

