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Value Investing Made Easy

by Coach Atty. Zigfred M. Diaz, CSS, ReB, ReA, AEPP RFP®

If intelligent investing can be summarized into just 10 words, these are the words that probably best describe it "Investment is most intelligent when it is most business like." Every time I give a stock market investing seminar, I jokingly tell people to recite this mantra before they make a decision to buy a certain stock.

It was almost 70 years ago when the great Benjamin Graham penned those words. In Chapter 20 of his seminal work, The Intelligent Investor, he writes:

"Investment is most intelligent when it is most businesslike. It is amazing to see how many capable businessmen try to operate in Wall Street with complete disregard of all the sound principles through which they have gained success in their own undertakings. Yet every corporate security may best be viewed, in the first instance, as an ownership interest in, or a claim against, a specific business enterprise. And if a person sets out to make profits from security purchases and sales, he is embarking on a business venture of his own, which must be run in accordance with accepted business principles if it is to have a chance of success."

What Graham wrote certainly makes sense considering that when you are buying a stock you are simply buying a portion of a business. Sadly, common sense is not so common when it comes to investing in the stock market. A lot of people buy stocks that have been hyped by by market manipulators.

To determine the value of a business we must look at the figures behind the business. Most people disregard digging into the fundamentals of a company and crunching number because they think it is too complicated to analyze.

However, there is a simple and quick way to determine whether a stock is worth buying or not. Here are 3 value-investing ratios that will give you a quick analysis and will guide you in your investment decision-making.

Price to Book (P/B) ratio – Probably one of the most important among all ratios as it more or less reflects the value of a company based on its books. The ratio is expressed as follows: market price per share ÷ book value per share. Book value is simply a company's total assets less its liabilities. To get book value per share, divide book value by the number of outstanding shares. Generally, any value under 1.0 is considered a potentially undervalued stock. Value investors rarely invest in stocks with P/B of over 3.0 except if it can be justified by other factors. A word of caution, while this ratio can reveal a potentially undervalued stock it could also indicate that a company has some problems; hence it is advisable to use this with other ratios.

Dividend Payout Ratio – The ratio simply expresses how much the company is returning to its stockholders against how much of the net income is being retained. It is computed by dividing yearly dividends per share by earnings per share. Generally companies with stable income and have financially strong balance sheets have a higher ratio as they can afford to give out most of their income to shareholders. However take note that this is not always the case as some stable growing companies may opt not to declare any dividend at all.

Total Liabilities to Current Asset Ratio – The ratio is expressed as total liabilities ÷ current assets. Anything lower than 1 is ideal as this tells you that the company is has very low debt. Use this ratio in tandem with growing earnings per share for the past 5 years and you are most likely to find a very stable and profitable company. Take note that to some extent it is not common to find companies with a ratio below 1. So, do your bargain hunting.

So there you have it! No need for you to do a lot of number crunching. Most of these ratios are even provided by your online broker so no need to even compute! There are other ratios that are used by value investors, and these will be discussed further in the future.

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Three Advantages of Bonds over Real Estate

by PFA

Real estate has been one of the main investments of today's wealthy elite. Property appreciation was accelerated when investing in the Philippine economy came into fashion globally. While foreigners still cannot buy real estate, they could buy condominium units for office space and house their expats in exclusive subdivisions. In the process, property sale and rental prices have shot up.

Unfortunately, investing in property requires huge amounts of money.

Yet, there is an alternative to investing in property. It is an investment that guarantees the payment of rent, the return of the property and sometimes even property value appreciation. This alternative is called bonds.

Bonds are nothing more than debt obligations of either the government or private sector companies that promise the payment of interest, alternatively called coupons, on a periodic basis (i.e. quarterly or semestral) and the return of the principal. You could say that the payment of interest is similar to the payment of rent but this time on the money you lend to borrowers, which could again be either the government or private sector companies).

Just like with property being rented out, the money you lend out through bonds is also promised to be returned. With property, the renter promises to return the premises in good order upon the termination of the rent or lease. With bonds, the full principal is to be repaid upon maturity.

Investing in bonds does not require huge amounts of capital as with real estate. You can buy bonds with just a few hundred thousand Pesos. And bonds are as easy to purchase as other investments like money market instruments and stocks. You just need to talk to a certified fixed income salesperson who may be found in banks, Trust corporations, investment houses and even stock brokerage firms. With a fixed income exchange, just like a stock exchange, the buying and selling of bonds in the Philippines has also never been easier.

Bond investors can also benefit from capital appreciation. This happens when the prevailing interest rate on bonds versus the interest rate or yield at which you were able to buy a bond moves lower. In other words, your bond will be more valuable because it offers a higher interest rate than what is available in the market. And if you decide to sell your bond in such a situation, you will realize a capital gain.

Of course, the reverse can happen where prevailing interest rates are higher than the yield at which you bought your bond. If you decide to sell your bond in such a situation, you will realize a capital loss. But the beauty with bonds is that you do not have to sell. You can simply continue collecting your programmed interest income for the remainder of the term of the bond. The question is, "Are bonds safe?"

Even with property, the guarantee is only as good as the guarantor. The good thing is that both the property owner and investor in bonds can choose with whom to do business. And the added advantage with bonds is that there is a third party that provides credit ratings of bond issuers (i.e. the borrowers) as to: economic risk, industry risk, market position, business diversification, management and strategy, earnings generation, cash flow and liquidity, capital structure, financial flexibility, and asset quality. In the Philippines, the major rating agency is Philratings (www.philratings.com).

Investing in bonds is similar to investing in real estate. The added advantages with bonds are that huge amounts are not needed, there is greater ease in buying and selling, and there is a third party that rates the credit worthiness of the issuer.

So, why not consider bonds as your next investment.

Editor's Note

Efren Ll. Cruz, RFP®
Editor-in-Chief

If you were given Php1 million today, what would you do with it?

We are sure that if we posed that question to 1,000 people, we would get just as many different answers. But allow us to provide not another answer but a framework to answer what to do with money, whether that money is windfall profit or regular income.

Let us first equate your finances to that of a company and let us call it your household finance. The total value of your household finance would be your total assets, which are funded from only two major sources, debt and your retained savings or net worth. And it is said that to have a high return on net worth, you need to be "pala-save" or have a high level of savings relative to your gross income. While you will use those savings to buy more assets, you will need to buy more of earning assets for you to enjoy a brighter future. That means you also need to be "pala-invest". And sometimes your savings alone will not be enough to grow your assets. During such times, you may use to debt to acquire assets and ideally earning assets at that. That is why you also need to be "pala-utang nang tama". Yet all will be for naught if you do not cover your earning capacity with protection against the perils of loss of life and property. That means you also need to be "pala-seguro".

Those are the P^4 of personal finance.

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