The Lore Report

Special Edition

Nine Ways to Choose Your Own Stocks

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In This Edition...

Free Shares?
An introduction to the Lore Report. Discover how we produce our report and find stocks where you really are paying less for more. If you are a first time reader, you are urged to read and understand this section.

Undervalued Stocks in this Report

N/A

Special Report

Nine Ways to Choose Your Own Stocks

Free Shares

A guide to understanding how the Lore Report discovers some of the Best Value stocks on the ASX.

Possibly the only thing better than free ice-cream on a hot summer day is when someone offers you a basket of cut-price shares. Sure, you may prefer rum n' raisin and there is only chocolate available, but they are almost free, right? Even if you do not like them, you can always give them away, or just keep them for the income. You could even keep them until Mister Market wants them back, and then sell them to him for a much higher price…

For the sake of the exercise, we are going to categorize shares as "cut-price" if they have a comparatively high yield, low PE ratio, and/or if they have a comparatively low NTA.

The guide rule of current bank bill rate may be used when comparing yield, so that a share paying 4% dividends which are 100% franked (at the company tax rate of 30%) may be seen as having a more attractive yield than a bank term deposit paying 5% that is fully taxable. Obviously the capital risk and income risk components are different.

Long-running ASX average PE's will be used as a guide, despite being unfair when uniformly applied to some industries. Retailers and banks will often have larger PE's than mining companies, due to their perceived stability. Sometimes these so-called "safer" stocks may have PE's lower than their counter-parts, and this is an anomaly which we wish to exploit when it occurs.

NTA's can also be an unfair comparison when applied across industries and sectors. Remember that we are not trying to be fair to all concerned, we are trying to draw attention to possible opportunities which may have been created by market inefficiencies. If you know what PE's, NTA's and yields are, then you probably are aware of the risks and opportunities which are inherent in investing. Warnings are included anyway.

Realize that it is possible that some shares are priced very low because they are not worth the paper that they are printed on. We hope to uncover some valuable nuggets of gold but be aware that there is also a lot of dirt amongst it! This report is not a recommendation of action to take or investments to make. Always use this report as your first point of reference to identify possible opportunities and then do your own research and/or call a professional. All care is taken and no responsibility accepted.

Lore Report Special Edition: Nine Ways to Choose Your Own Stocks

We are not "advising" this… but…

WARNING: This report is for educational purposes and is NOT a "do-it-yourself" manual. We realize that some people will learn a few tricks and suddenly think that they are experts. This is not necessarily the case but we do know that it does happen. Be forewarned and always check your conclusions with a qualified professional before making any investment decisions.

Some investors use numbers, charts and past analysis to pick winning stocks ("quantitative analysis"). Some other investors rely on feeling, future planning and gut instinct ("qualitative analysis"). If you really want to choose your own investments, you could take a leaf out of both books and do some "quant" and some "qual": use both scientific research and some personal feeling…

Nine ways to choose your own stocks

1. Firstly, ensure that the stock trades on a major exchange. This is for reasons of reputation as well as for liquidity. Look for a listing that is on the ASX, FTSE, AMEX, NASDAQ, NYSE for best protection and for ease of reselling later.

2. Look for a large trading volume, at least 10 000 per day, best if 100 000 or more. If only a few shares are changing hands, it could signal elitism or a difficulty selling later.

3. Medium was good enough for Goldilocks, so aim for a mid-size cap stock. These will generally have more upside potential than large caps with less downside than small caps.

4. Again, medium is safer on price. We are looking for stocks that will increase in value, so do not buy the most expensive stock. Aim for a reasonable price if you want more upside potential.

5. Look for insider buying (not to be confused with insider trading); do the employees and directors of the company hold stocks? Are they buying more? The insiders will know where the company is heading. If they are buying, this is a good sign.

6. Look for a good price to book ratio (NTA). Aim for a ratio of 3 or less and avoid buying companies that are too overvalued… Only one way for them to go!

7. Watch the PE ratio (PER) and aim for the sweet spot of between 10 to 20. If this is lower than ten, it may be an absolute bargain, or just about to

fold. If it is higher than twenty, it will generally not stay there for very long…

8. Look for rising sales (EPS growth). You want a company that is increasing its market share and profits, not one that is flat or falling.

9. Rising profitability (PEG). You will want to make sure that the company is paying out some of the increased profits to shareholders, as well as reinvesting some into growing the company. Retaining all profits can be a slow death or a sign that profits are not exactly "real"...

10. Look for a company with that little extra *'je ne c'est quoi'*, that simple little "I don't know what" quality… The company may have a special niche market, it may have some form of notoriety due to a recent media article, or enjoy familiarity as a "household name". This will often give earnings a boost.

Je ne c'est what?

If earnings are rising from year to year, if profitability is rising, if notoriety is on the increase, then soon the share price may be on the increase.

The "wow" factor may be as simple as a clever marketing name for the product, or an interesting spin on an old idea.

Just a little something extra can make a memorable difference.

Nokia and Windows both had intuitive software which was easier to use than their competitors. Apple made its I-pods white with white coloured headphones instead of straight black. The Apple G3 computers were coloured like fruit instead of black or beige. Hanes made women's stockings packaged in a small plastic egg instead of stretched across flat cardboard.

The list "Nine Ways to Choose Your Own Stocks" included *ten* entries. It is all about the little extra something… Look for companies that under-promise and over deliver…

WARNING: Even if you insist on picking your own stocks, place the deal with someone who cares about you, just in case you're wrong…Or just play it safe and deal with a professional. We take NO responsibility for any action you may take whilst relying on information from us or other sources.

Undervalued stocks are regularly profiled in The Lore Report, using quant data and qual data. The Lore Report is published fortnightly. Past issues are available free of charge at www.lorereport.com

"Nine Ways to Choose Your Own Stocks" is adapted from an article written by Jeremy Britton and published in a new book, "Who's Taking Your Money? (and how to get some of it back!" ($28 in bookstores or $25 online at www.24hourwealthcoach.com)