Investment Tips

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The philosophy of investing has many different viewpoints. Many investors feel that, since they are participating in a fluctuating equity position, there is a need for a gambling attitude. The desire for short-term reward overcomes the patient, value oriented approach that is necessary for long term success.

"Water seeks its own level" is an over-used cliché. Nowhere is it so true as in a proper investment plan. The prospective buyer should search for value that seems to be overlooked, and/or understated, in the current price of a security. Yes, such research will, at times, uncover a security that will move up rapidly after your purchase. More times than not this will not be the case. The value will remain obscured until some announcement, research recommendation or economic development brings it to vast public awareness. Be careful in this value-oriented system that you check forward to be sure that the future earnings forecasts are positive.

Another solid approach is the turnaround situation. Good companies can have earnings problems that greatly diminish the price of the shares. Look for signs of profit rejuvenation. This frequently provides superior market performance as such companies return to favorable market status.

Older investors frequently have a need for stocks with good dividend income. Can you build a portfolio with a 5 percent annual income and still have reasonable growth probability? In my opinion, this can usually be done. My favorite method is to put one third of the money into proven high-income issues, which will insure a good overall return. Then, when you put the other two thirds in a dividend paying growth stocks, you will wind up with the desired income stream and still have good capital gains potential. Your broker can work with you to develop such a portfolio.

Some investors are strictly out for income. Safety of principal is a factor. High grade preferred issues fit well here. Be sure to buy them at a discount from their call price. I would rather have a 6.5% return at a price of 22 than a 7% return at 27. This assumes a call price of 25. Do not overlook the closed end, NYSE listed mutual funds. You can buy them at big discounts from their net asset value to yield over 7.5%.

Another popular area for the income seekers is a tax-exempt bond. There are many different theories on how to purchase them. Many investors emphasize short maturity, such as less than ten years. I do not side with this thinking. My two requirements are safety and the highest current return without paying a premium over the call price. This theory is based on the fact that interest rate swings should give investors the opportunity to get out even or ahead at

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least once in a seven year period. Such thinking leaves you only with the decision on the amount of tax free income that you will accept.

Many of the financial planners emphasize mutual funds almost to the exclusion of other types of investment securities. The argument is made that the professional management and diversification gives a big advantage to this area of securities. It is further stressed that there are mutual funds that cover every investment sector. I can not fault the reasoning here even though my experience is that well selected individual securities will do better than most mutual funds. One of the primary factors here is cost. Don't accept the implied zero cost in no-load funds. While it is true that the "no-loads" are available at the net asset value, you must remember that the annual fees levied against these portfolios average approximately 1.25 percent for the industry. Combine this with a normal annual fee by the financial planner of 1% and you are looking at an annual deduction from your invested assets slightly in excess of 2% per year. Taking this out for ten years and assuming that the funds are doing well, you are looking at a very significant cost versus your initial investment. In short, find out all the expenses before you invest in no load funds through a financial planner.

There is a wide disparity in the true cost factor on conventional "load" mutual funds. Some not only carry an initial charge in the 5% area, but also have high internal fees, many approximating 2% annually. Take a hard look here because there are some excellent management groups whose annual fees are less than ½ %. In short, you may be far better off paying a 5% load on your initial investment if the ongoing annual cost is under ½ %.

Investors often ask about methods for selecting under valued securities. We all know that buying at low price-earning multiple, versus the average is a good measure, providing that the company is showing proper growth trends. The economic climate around various industries also contributes to price vs. earnings considerations. Book value is a very interesting area. It can be very important or quite insignificant. It is quite important on financial issues for instance they average acquisition price in bank takeovers runs in the 3 times book value zone. A recent example of this would be Maryland's Merchantile Bankshares when PNC CORP acquired them. For that reason, a well-run bank situation presents genuine promise to the patient investor who pays under 1½ time book value. Since we are still in a consolidated period in the banking industry this tool should be very useful to the regional bank investor. Incidentally, this designation carries into the "super regionals" because when one of the "giants" moves into a new area, they must acquire an operation that is large enough to justify its presence in the over operation.

Some analysts feel that life insurance companies represent great stories of value and consistent growth. I am a member of this school. The important thing here is not to overlook the "inventory" when computing the book value. After utilizing the conventional method, be sure to adjust upward or downward for the business in force. Based on my long observation, a number of $20 per thousand on whole life and $3 per thousand on term is a reasonable course to follow. You will find that $30 book values turn into $50 adjusted book values. My use of the word "inventory" was deliberate. These policies cause the premiums that grow the companies.

There are different applications used in every industry. I cited the banks and life insurance companies to illustrate this fact. Talk with your broker and use his research material to develop a plan and set of "yardsticks" on other industries.