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Value investing in the Indian stock market

I aspire to become a value investor along the lines described by Benjamin Graham in 'The Intelligent Investor'. This blog captures my thoughts and experiences (good and bad) on the way to Intelligent Investorhood, in the context of the Indian stock market. I also plan to publish my stock picks here periodically along with the reasoning behind them, so as to have a record of the way my stock-picking technique evolved over time.

SATURDAY, FEBRUARY 26, 2005

Stocks I bought in January 2005

I picked up two stocks in January 2005. In this note, I explain the value considerations behind these picks.

Stock S1

I bought this stock in the second week of January. The company manufactures machines that process plastic. The main reasons why I felt this was a good buy are :

- The company has been paying dividend consistently, and the dividend yield is good :
    - Dividend data is available for the last four years, and the company has paid a 35% dividend during the last three years.The year before that, it paid a 30% dividend.
    - The 35% dividend corresponds to a dividend yield of around 5.8% at the price I bought. Which is only slightly below par with current Fixed Deposit rates.
- The book value of per share is around one and a half times the price which I paid.
- At the price I bought, the P/E ratio is only slightly above 5.

Stock S2

I bought this stock in the third week of January. The company is one of the largest paper manufacturers in the country. The main reasons why I felt this was a good buy are :

- The company has been paying dividend consistently, and the dividend yield is satisfactory :
    - Dividend data is available for the last three years, and the company has paid a 28% dividend during this period.
    - The 28% dividend corresponds to a dividend yield of around 4.7% at the price I bought. Which is not far below current Fixed Deposit rates.
- The book value is about 10% more than the price which I paid.
- At the price I bought, the P/E ratio is around 7.

I invested Rs.5042/- in S1, and Rs.5119/- in S2.

I have higher hopes for S1 than for S2, both because of its better past performance, and because it has much more room to expand than S2. Also, the promoters of S1 have a much higher stake in it than the promoters of S2 have in it.

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Name:
Value Investor

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Some useful links

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The Basics

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I Power Blogger

posted by Value Investor @ 6:31 AM 1 comments

SUNDAY, JANUARY 23, 2005

Rethink on publishing stock names...

On second thoughts, I have decided *not* to publish the names of the stocks which I buy. Instead, I would be using a notation which will denote the year of purchase and the ordinal number of the purchase. Example : S1-05 for the first stock I bought in year 2005.

Rationale:

1. I don't want run the risk of influencing the price of the stocks I have purchased, especially if the influence results in the price going up.

   Suppose this blog comes to the notice of other people who put their money into the stock market. From what I have seen, an amazingly large proportion of this population firmly believes that following stock recommendations (the source is irrelevant, as long as it is someone else than themselves) is the (only!) way to make money from stock markets. So, if a sufficiently large number from this group happens to come across this blog, it is almost certain that a number of them would start following these recommendations, especially if my past record happens to be good(which I hope it would be!). In other words, publishing a stock in these columns may be a cause for a (probably short-lived) rise in its price. Which would obviously go against my interests.

2. My emphasis is on the methods used to choose a stock, rather than on the specific stock that was chosen

   As such, publishing the stock name doesn't add any value to the blog. Indeed, it might even detract from the little instructional value that it may have for those keen on value investing.

posted by Value Investor @ 6:28 PM 0 comments

On outstanding shares, and a warning about splits

'Outstanding' doesn't have its usual meaning here -- Every share issued (and not subsequently extinguished) by any company is an outstanding share of that company. In short, the phrase 'the number of outstanding shares' has, for all purposes, the same meaning as the phrase 'the number of shares'.

This number is available from the latest Balance Sheet -- look at the schedule for the entry titled 'Share Capital' or some such. Be aware, however, that this number is invalidated by any action of the company, subsequent to the 'As At' date of the Balance Sheet, that changes the number of outstanding shares. *Beware especially of share splits*, since they would skew the numbers in a way which would fool someone depending on the Balance Sheet data to calculate per-share values.

An easy (but perhaps not foolproof) way of finding if a split has happened after the date of the last Balance Sheet is to see if there has been an abrupt (as in Rs.100 to Rs.5 from one trading day to the next) fall in the price of the share -- a 20:1 split would cause the price to fall to approximately one-twentieth of its pre-split price. And if the researcher overlooks such a split, the post-split per-share ratios would look very attractive, since (s)he would then ascribe to a share the price of one share and the value of twenty!

posted by Value Investor @ 6:05 PM 0 comments

Why a fall in share prices is almost invariably a good thing

When I buy a stock at a certain price, I do so because my research has convinced me that at that price, the portion of the company which the share represents is a good buy.

In other words, when I spend Rs.50 for buying a share of ABC Ltd., I do so because my perusal of the financial records of the company has convinced me that I am getting (say) Rs.75 worth of 'things' when I buy that share. In the simplest (and most unlikely!)case, the company would have that much cash to show for each share, after paying off all its debtors.

For ABC Ltd, that would be the case if, for example, it had 1 Lakh shares outstanding, and as per its Balance Sheet for the latest year,

- *Its Net Current Assets is positive,*
- *Its Fixed Assets are positive(!), and*
- *Share Holder's Funds minus Loan Funds = Rs. 75 Lakh.*

This would mean that by giving Rs.50 for a share of ABC Ltd, I am getting the rights to Rs.75 from the cash reserves of the company. Which certainly seems to be a good bargain.

Now suppose that after I bought the stock, its market price went down, say, by 10%. Is that good or bad for me? Assuming that nothing has happened that would have a significant detrimental effect on the company's current value or its long-term future prospects, I would say the fall in price is a good thing for me. Reason : ***if the share was a good buy at Rs.50, it should be a better buy at Rs.45***. **It is of no consequence that the market thinks badly of the share**, as long as its judgement is not based on what has happened to the company.

So, if the price of a stock which I have bought after due diligence falls due to the market's whims alone, it is a good thing for me. I should be happy, and get ready to buy more of the company at the reduced, and therefore more attractive, price.

The catch here is, of course, that I don't have an infinite amount of money at my disposal to keep buying the stock at every percentage point fall in its market price. So I adopt the second best approach -- keep buying equal-rupee-valued lots of the share after every *n*% fall in its price, compared to the average price at which I hold it. The larger the resources I have to buy the lots, the lesser the value of *n*. At my current state of finances, I would put *n* to be from 10 to 20, depending on the historical price swings of the share -- the more the swings, the greater the value of *n*, but never more than 20.

posted by Value Investor @ 5:48 PM 0 comments

SUNDAY, JANUARY 09, 2005

Some useful links

For preliminary screening of stocks based on their financial performance, I use the (mostly!) excellent database on Indian companies maintained by www.myiris.com.

For getting price information, I use the Yahoo! listings of Indian stocks.

In those cases where the latest information about a company is not available at myiris, or where the available information is patchy/looks shaky, I look up the more dependable, but less user-friendly, EDIFAR database maintained by SEBI.

In those cases where a company which seems to be attractively priced compared to its valuation looks shady (for some reason), I consult the very helpful watchoutinvestors.com site supported by the Investor Education and Protection Fund, for the history of punitive actions/complaints against the company.

posted by Value Investor @ 6:50 PM 0 comments

SATURDAY, JANUARY 08, 2005

DISCLAIMER

1. There are **no guarantees**, implied or otherwise, associated with the stock picks that I publish : they are for my own record, no more and no less.

2. I publish a stock pick *after I have already bought it* at the indicated price.

posted by Value Investor @ 2:30 AM 0 comments

The Basics

- Read Benjamin Graham's The Intelligent Investor for the definitive description of value investing.
- For an inspirational account of how value investing has actually worked, read Warren Buffet's article (available online, adopted from a speech he gave) The Superinvestors of **Graham**-and-**Doddsville**.
- Read on to find how I fare in applying the principles described by the book to the Indian stock market.

posted by Value Investor @ 2:12 AM 0 comments