

## Consideration of Stock Sale

### Basic Data

Company	Symbol/Market	Current Price	Date
Pre-Tax Profit on Sales	ROE	Debt/Equity	Last 4Q EPS
Upside/Downside Ratio	PE	5 yr Ave EPS	RV

### Signs of Change

Consideration	Good	Bad	Comments/Notes
<b>Is there a declining growth rates for sales and/or earnings?</b> These almost always lead to declining Price to Earnings (P/E) ratios and lower market prices. A gradually-declining growth rate for sales and earnings may be the result of a company transforming from a high growth to a maturing company. Watch the research and development spending rate and the company's introduction of new products and services. These can affect the company's future growth rate.	No	Yes	
<b>Has there been a management change?</b> If old management was good (e.g., Iacoca), it will take 3 years for new management to screw it up, if at all; likewise, if good management replaces bad, it will take them 3 years to turn it around.			
<b>Is the dividend payout ratio is too high</b> (above 50%, except for special situations like utilities) and/or the percent earned on equity is too low? (Look for negative changes too.)	No	Yes	

### Fundamentals

Consideration	Good	Bad	Comments/Notes
<b>Are the profit margins declining?</b> Declining profit margins are probably the best indicator of a downturn.	No	Yes	
<b>Is the company's financial condition is deteriorating?</b> Watch the amount of debt taken on and whether the company can meet payments if the economy slows.	No	Yes	
<b>Are fundamentals good?</b> Do not sell because of a paper loss if the company fundamentals are good.	Yes	No	
<b>Is growth is satisfactory?</b> It is very difficult to achieve bottom line (earnings) growth without top line (sales) growth. Use PERT and the SSG graph to judge this growth.	Yes	No	
<b>Is this a growth stock?</b> Do not sell just because the price has not moved. Growth stocks often grow in spurts.	Yes	No	
<b>Are profit margins eroding?</b> Use PERT to check the Pre-tax Income growth and the growth as a percent of sales.	No	Yes	
<b>Are fundamentals good?</b> If quarterly earnings lag expectation by a few cents and fundamentals are good ignore the panic selling but check the reason. If they are profitable with good fundamentals, you may want to consider buying more.	Yes	No	
<b>Is the stock is grossly overpriced?</b> Use the SSG to check the P/E ratio against the 5-year average, using a 12 month leading P/E. If the P/E is one and a half times the average, and the upside-downside ratio is less than 1, it is time to consider selling. Consider selling if the PE rises to 1.5 times the 5 year average. Sell if the PE ratio is too high unless for a quality company, e.g., Coco Cola. If contemplating selling consider taxes and sell/buy commissions. Use Challenge Tree. (STB SA has an excellent one)	No	Yes	

Fundamentals (continued)

Consideration	Good	Bad	Comments/Notes
If the <b>earnings are going up and the profit margins are trending down</b> , a decline will probably follow within a few years; follow closely.	No	Yes	
<b>Is the stock price declining for no apparent reason?</b> Institutional investors may know something you don't know. You can see the price history graphically if you have filled in the PMG stock prices several times a year.	No	Yes	
<b>Is this a quality stock?</b> In a Bear or Bull market it is the quality stocks that are the first to recover from the bear and the last to go down at the top of a bull run.	Yes	No	
<b>Is growth satisfactory?</b> The management's competence is under question. Examine PERT to note the growth in the various categories.	Yes	No	

Management and Market Considerations

Consideration	Good	Bad	Comments/Notes
<b>Does this company have a good product mix?</b> Do not buy a company that just has a single product.	Yes	No	
<b>Does this company contribute to our diversification?</b> To balance your portfolio. Avoid overweighting by company size, industry, or company.	Yes	No	
<b>Is the investment climate for the company or the industry deteriorating and no improvement is seen on the horizon?</b>	No	Yes	
<b>Are insiders selling?</b> Watch insider information if stock is declining in a rising market.	No	Yes	
<b>Is institutional ownership reasonable?</b> Do not buy if institutional ownership is greater than 65%. Volatility is usually caused by institutional trades.	Yes	No	
<b>Is this stock in a competitive market?</b> Watch highly competitive markets, e.g., TVs, computers.	No	Yes	
<b>Is this a cyclical stock with a high PE?</b> Metals, autos, and retails are most cyclical. Buy when PE ratios are high and sell when PE ratios are low. The SSG process is best with growth stocks; poor with cyclicals.	Yes	No	
<b>Are we considering selling short?</b> Leave selling short to the professionals.	No	Yes	

Wrong reasons for selling

- Selling because the price hasn't moved
- Selling because of a Paper Loss or a Paper Profit
- Selling because of Temporary Bad News
- Selling just to Take Action
- If you've kept a stock while it plummeted, don't sell it when it has fallen so far that any remaining downside risk is minimal compared to its upside potential
- Selling by using Price Targets, eg: automatically selling when stock has doubled or when it has dropped by a certain percentage
  - Any drop in price should flag the stock for further analysis; it should not, however, cause an automatic sell ...understand why things happen
  - If a stock has doubled, hold it to triple or quadruple

Wrong reasons for NOT selling

- You're emotionally attached to a company
- You hate to admit that you made a mistake
- You hate to take a loss, and you want to wait until the price rises back to the purchase price
- You don't know how to take advantage of a loss for tax purposes

Conclusion

- Selling, like buying, is not an easy decision
- You must look at the whole picture, not just at one or two numbers
- If 4 out of 5 selling decisions are correct, you should do well