

SUCCESS BREEDS SUCCESS??

Warren Buffett gives the impression that he favours being very selective and only buying a relatively small number of shares and holding these indefinitely. O'Shaughnessy believed the best performing shares tend to be those that have already started behaving like winners by outperforming the market. As *IfG* in June 1999 observes:- *Many investors tend to avoid buying this sort of share for fear it has already enjoyed its rise.*

If we take the thoughts of these two gurus, add a touch of Dreman's Contraryism (what a mixture!) and follow them to the extreme, a search can be made to find those UK companies that have had an increase in earnings per share every year for ten consecutive years. The result, starting from companies with a PEG, found 19.

Twelve of them beat the index in the bull phase – 1992-99 and seventeen beat the index decisively in the bear phase 2000-March 2003, furthermore seventeen beat FTSE 100 index significantly over the ten-year period. Taking the cycle from December 1995 to March 2003 when the index was the same value the average share price doubled with all nineteen doing better. During the three years of bear market in which the index halved, the average share price was constant. The table below gives the ratios:-

10 consecutive years growth (19 companies)

	10 year 92-02/3	bull phase 92-99	cycle 95-02/03	bear phase 99-02/03
Average				
earnings per share	x 6.4	x 4.7	x 3.5	x 1.63
dividend per share	x 5.5	x 3.3	x 3.1	x 1.70
share price	x 4.8	x 9.9	x 1.94	x 1.0
PER	x 0.89	x 1.91	x 0.67	x 0.63
FTSE100 Index	x 1.27	x 2.69	x 0.98	x 0.47
Average Relative	x 3.7	x 3.7	x 1.97	x 1.90
Companies with Relative > 1.0	17	12	19	17

To achieve 10 consecutive years without faltering may appear unnecessarily harsh, so the exercise was repeated on the basis that there may be a reduction in earnings per share for a year providing it is made up for the following year. Again the number found was nineteen. The results were similar but, on average, not quite as strong.

Ten of them beat the index in the bull phase – 1992-99 and fourteen beat the index decisively in the bear phase 2000-March 2003 and seventeen beat the FTSE 100 index significantly over the ten year period. Taking the cycle from December 1995 to March 2003 when the index was the same value the average share price doubled. Eighteen out of nineteen did better. During the three years of bear market in which the index halved, the average share price dropped only 8%. The table below gives the ratios:-

9 out of 10 consecutive years (19 companies)

Average				
earnings per share	x 7.3	x 5.6	x 3.5	x 1.59
dividend per share	x 4.4	x 3.2	x 2.4	x 1.37
share price	x 3.9	x 6.5	x 2.4	x 0.92
PER	x 0.77	x 1.43	x 0.70	x 0.61
FTSE100 index	x 1.27	x 2.7	x 0.98	x 0.47
Relative Average	x 3.1	x 2.4	x 2.5	x 1.75
Companies with relative > 1.0	17	10	18	14

How did they achieve this performance?

- Are they in the ideal position in their markets?
- Are they the lead companies in their sector?
- Do they have a dominating lead over competitors?
- Have they a culture that enables them to be really efficient?

Have they a product or service balance that provides stability?
Have they had directors who have really foreseen their markets?

What is interesting is that in the 10 years Torex has changed from being a tool hire company to being a software business and South Staffordshire started the period as a water supply company and is now 67% business support services.

In many there has been a significant turnover in directors over the period.

The companies by sectors are:-

Aerospace	Cobham
Banks	Royal Bank of Scotland
Chemicals	<i>Johnson Matthey</i>
Construction	<u>Barratt, Berkeley, Boot H.</u>
	Aggregate Ind., Bellaway, Redrow, Taylor Woodrow, Wolseley
Food & Drug Retailers	<u>Greggs, Morrison Wm., Tesco</u>
Food Producers	<i>Cadbury Sweppes</i> ↓
General Retailers	Clinton Cards, Dixons ↓4
Health	<u>Allied Unichem, Amersham</u> ↓, <i>Smith & Nephew</i>
Leisure & Hotels	Enterprise Inns, Hardys & Hanson, Wetherspoon
Media & Entertainment	<i>Johnston Press</i> Taylor Nelson
Software & Com. Serv	<u>Sage</u> Misys↓
Speciality & Other Fin	<u>Cattles, Provident Financial</u>
Support Services	<u>Capita, MITIE, RPS, South Staffordshire, Bunzl, Torex</u>
Telecommunication Services	<i>Vodafone</i>
Transport	<u>Assoc British Ports</u> ↓, Forth Ports,

Underscored

Bold

Italic

↓

↓4

Ten years consistency, otherwise nine

Median or above for earnings growth over 10 years. Otherwise below the median.

FTSE100

The eps brokers' consensus forecast for 2003 is a fall in eps made up in 2004

An eps brokers' concensus forecast for 2004 indicating a fall in eps

The numbers in the FTSE100 & FTSE250 are roughly proportionate to the index population: 14 and 20. There are 2 Small Cap and 2 non-index.

It is interesting to observe which sectors were not included – Electrical & Electronic, Mining, Oil & Gas and Pharmaceuticals.

Perhaps those selected are rather “dull” but then they are less likely to be over valued.

The question arises:- In a recovering, or a static market how will they perform?

The consensus of brokers' forecasts for earnings per shares averages around 10% for both categories. The average prospective Price Earnings Ratio is 12 for the 10 years consecutive category and 11 for the 9 out of 10 category. The prospective dividend yield is 2.9%-3.0% for both categories with an increase between 2003 and 2004 of 9%-10%. Only two companies had forecasts from a single broker, the rest averaged ten.

In the five months since the 12 March 2003 low, 31 out of 38 have risen more than the FTSE 100.

The companies were found by taking those currently eligible for a PEG value (four years eps growth although two may be forecasts) and therefore exclude property companies. I cannot guarantee the lists are complete.

The consensus of brokers' estimate predicts that four companies will have reduced eps in 2003 or 2004. Other companies may qualify in 2003 and 2004.

These findings should be considered to be just one filter in a multi-filter search, prior to business model analysis.

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