Quick-Start Investing – 5 Minute Investing Terms and Analysis

It's easy enough to open an investing account these days but once that's done, the question becomes…how to invest?!?

There's so much information online and on TV, where do you start and how do you know where to put your money? From stock recommendations, predictions of crashes or zooming prices and everything that passes for analysis – *how do you cut through it all and actually get started investing?*

That's what we'll do in this handout, cut through all the jargon and complicated strategies for a simple start to investing that you can do on your own. I'll start with a quick checklist you can use to compare stocks. Then we'll look at a short list of terms for the beginner investor.

Let's Do This!

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Let's Talk Money!

P.S. If you want to see my complete process for picking stocks, **check out the video here!**

5-Minute Stock Analysis Checklist

Take you through the most important measures and ways to compare stocks. Don't worry if don't understand some terms, I'll include them in investing terms below.

- **Sales growth** is the first thing I check on a potential investment, how fast are they growing sales on a year-over-year basis…if at all? If a company isn't making higher sales each year, it's not going to grow profits even if it has a lot of the other measures I'm looking for below. Find sales growth reported at the top of the company's income statement. *(Note: I usually take this on a three-year annualized basis to find longer-term growth)*

  Example: Apple reported $260.17 billion in sales last year and $215.64 billion in sales three years ago. Sales growth (three-year annualized) = $260.17/$215.64 ^ 0.33 = 6.4% annual growth.

- **Operating margin** is the operating income, so sales minus all the costs to run the company, divided by the total sales. It's the best measure of how well management is doing to turn sales into profits. My single favorite measure to compare stocks, you can find this on the ‘Statistics’ page for a stock on Yahoo Finance or by taking the operating income divided by sales.

Example: Apple reported sales of $260.17 billion over the last year and an operating profit of $63.93 billion after all operating expenses. Operating margin = $63.93/$260.17 = 24.6%

Apple Income Statement

▼ **Name** USD in Billion except per share data	TTM	2019	2018	2017	2016	2015
▼ Gross Profit						
► Total Revenue	260.17	260.17	265.60	229.23	215.64	233.72
▼ Cost of Revenue						
Cost of Goods and Services	-161.78	-161.78	-163.76	-141.05	-131.38	-140.09
Total Gross Profit	98.39	98.39	101.84	88.19	84.26	93.63
▼ Operating Income/Expenses						
Selling, General and Administrati…	-18.25	-18.25	-16.71	-15.26	-14.19	-14.33
Research and Development Expe…	-16.22	-16.22	-14.24	-11.58	-10.05	-8.07
Total Operating Income/Expenses	-34.46	-34.46	-30.94	-26.84	-24.24	-22.40
Total Operating Profit/Loss	63.93	63.93	70.90	61.34	60.02	71.23

- **Payout ratio for dividend stocks** is a great measure of how safe a dividend payment is and how much room it has for growth. The payout ratio is the dividend amount divided by earnings made by the company, usually both on an annual basis. Pay out too much and there’s no room for growth or mistakes before the dividend is cut. Pay out too little and it’s not much of a dividend stock!

  Example: Apple pays a dividend of $0.77 each quarter or $3.08 per year and reported earnings per share of $12.50 over the last year. Payout ratio = $3.08/$12.50 = 24.6%

  Check out this video for more about the payout ratio and three risks in using it.

- **Debt-to-Equity ratio** is an important measure of financial flexibility and safety in a stock. Take the amount of Long-term Debt and divide by the Stockholders’ Equity. This not only tells you how much of the company is owned by stockholders and how much is owed to creditors but also the level of risk in the shares.

  Example: On the balance sheet, we see that Apple owes over $91.8 billion in long-term debt against stockholders’ equity of $90.5 billion. Debt-to-Equity ratio = $91.8/$90.5 = 1.01

Apple Balance Sheet

Name USD in Billion except per share data	2019	2018	2017	2016	2015
Long Term Debt and Capital Lease ...					
Long Term Debt	91.81	93.74	97.21	75.43	53.46
Total Long Term Debt and Capital ...	91.81	93.74	97.21	75.43	53.46
Total Paid in Capital	45.17	40.20	35.87	31.25	27.42
Retained Earnings/Accumulated Deficit	45.90	70.40	98.33	96.36	92.28
Reserves/Accumulated Comprehensi...	-0.58	-3.45	-0.15	0.63	-0.35
Total Equity Attributable to Parent Stock...	90.49	107.15	134.05	128.25	119.36

- Price-to-Earnings to growth (PEG) ratio is a twist on the popular P/E ratio because it includes earnings growth as well. It measures how expensive shares are for the level of growth. Take the share price divided by earnings over the last year, then divide this number by earnings growth as a whole number (i.e. growth of 25% would be 25).

  Example: Apple trades at a price of $300 per share on earnings of $12 per share over the last year for a PE ratio of 25-times. Earnings are expected to grow at 12.5% annually over the next three years. PEG ratio = 25/12.5 = 2.0

Taken alone, these measures don’t really tell you much until you compare them against other stocks and against the market. For example, you don’t know if an operating margin of 25% is high or low until you see that the operation margin on another stock is 15%, which would tell you that the first company’s management is more efficient at converting sales to profits.

You also need to remember here to always compare stocks within the same industry or sector when using these measure. You can compare measures across sectors or against the stock market as a whole but it isn’t as useful because of different business types. Comparing these measures for a tech stock against a tech stock though will give you an apples-to-apples comparison and help you pick the better investment.

Ready to Start Investing? Check out this review of the six investing platforms I use and special bonus cash on each.

Terms Every Investor Should Know

- **Price-to-Earnings ratio** is the most popular investing measure and is simple the price per share divided by the earnings (or net income) per share over the last four quarters. This tells you how expensive the stock is relative to another PE ratio like that of another stock, the overall market or the company’s own history of average PE ratios.

- **Debt-to-Equity ratio** shows how much of the company is owned by shareholders and how much is owed to creditors. It's a good measure of the risk in a stock and the financial flexibility the company has if the economy heads into recession.

- **Payout Ratio** is the percentage of the profits paid out to shareholders with the dividend. It's a good measure of how sustainable the dividend is and if there's room for growth. Investors like to see a high dividend but the company also needs to save some profits back to reinvest in growth and stay competitive.

- **Operating Margin** is a measure of how well management can turn sales into profits. Operating income is the money left after paying suppliers and all operational expenses to run the company. This income divided by the total sales is the operating margin, the company's operational efficiency.

Check out this video for seven must-see financial ratios to analyze investments

- **Bear Market** is technically when a stock's price or a market index has fallen 20% or more from its high. Sometimes the high is measured from the 52-week high and sometimes it's just the all-time high.

- **Bull Market** is any sustained increase in a stock's price or the market more than three-months. Sometimes it's also when a stock price or the market has increased 10% off the recent lows but there's really no technical definition.

Watch this video for a history of bear and bull markets plus an investing strategy for each.

- **Market Correction** when a stock's price or a market index falls 10% to 20% from its high. Market corrections happen before a technical bear market but not all corrections turn into a bear market.

- **Dividend Yield** is the dividend amount paid over the last four quarters divided by the stock price. *Example: Apple pays $3.08 a year dividend on a current price of $300 per share for a 1.2% dividend yield.*

- **S&P 500** is the most widely used index to represent 'the stock market'. It's a grouping of the 500 largest companies by market capitalization based in the United States.

- **Net Income (Earnings or Profit)** – also sometimes called 'the bottom line' because it appears at the bottom of the Income Statement. Earnings are the ultimate ownership for stockholders and are after all operating expenses, debt interest and taxes have been taken out.

- **Revenue (Sales)** – also sometimes called 'the top line' because it appears at the top of the Income Statement.

- **Market Capitalization** is the market value of a company, all its shares outstanding multiplied by the price-per-share. Market cap can be broken into groups of company sizes from Micro (from $50 to $300 million), Small (from $300 million to $2 billion), Mid-cap (from $2 to $10 billion), Large (from $10 to $200 billion) and Mega (more than $200 billion).

- **Exchange Traded Fund** is a professionally-managed investment set up to follow a group of stocks. ETFs can hold any asset class (stocks, bonds or real estate companies) and hold anywhere from a few dozen stocks to thousands. They provide instant diversification across companies in the group. ETFs charge an annual fee called an Expense Ratio which is a percentage taken off fund assets each year to cover costs.

- **Assets (also Asset Allocation)** are a broad grouping of investments that share fundamental characteristics. The main asset classes are stocks, bonds, real estate and commodities of which all investors should have some exposure to in their portfolio. Asset allocation is the split of these assets in your portfolio; i.e. 50% in stocks, 20% in bonds and 30% in real estate. Asset allocation depends on your age, tolerance for risk and other factors.

- **Bonds** are debt owed by a company with interest payments made twice a year and the bond amount paid at the end of the investment. Also called Fixed Income because the interest payment is usually a fixed amount. Bonds provide cash flow similar to dividends but are safer than stocks because they are a debt obligation.

- **Expense Ratio** is the percentage charged by exchange traded funds (ETFs) to manage the fund. It's taken out of the fund assets, not out of your account but has the same effect of lowering the ETF value. Always compare expense ratios for ETFs and lower is usually better.

- **Diversification** is the idea of spreading your portfolio across different stocks, bonds and other investments so your overall wealth does not depend on any one in particular. Also applies within asset classes, so spreading your portfolio of stocks across 10+ company's shares so it is not at risk from one single company.

- **IRA (also Roth IRA)** are two types of retirement accounts. Deposits you make into an IRA are tax-free in the year you make them though you pay income taxes on withdrawals in retirement. Deposits into a Roth IRA are taxed as income in the year you make them but then tax-free on withdrawal. Always max out your annual contribution limit to either an IRA or a Roth, every year!

You don’t need to be an financial expert or spend 40+ hours a week analyzing stocks to invest your own money. Nobody will care as much about your money as you do and nobody will be as thoughtful an investor. Keep control of your money and do your own investing.

I’m always here to answer any questions and help out any way I can. Let me know if you have any questions or would like to see a topic in a video.

Thank You for being a part of the Bow-Tie Nation!