Column/Investment

# Build your knowledge in shares investment

MOREMI MARWA
moremi@dse.co.tz

How do you pick shares/stocks that are likely to beat the market? In some basic form, when it comes right down to it, the answer should be simple; i.e. invest in stocks that treat you well and let you sleep peacefully at night. And just how do you do that? Well, the answer varies a bit from person to person, but here are some proposed specific criteria and tactics that could help you identify businesses that satisfy your investment objectives. Below, I explain some of these tactics:

You may wish to avoid investing in something you quite do not understand If you do not consider yourself as a risk taker, then it is advisable to try and stick to investment and companies that you do understand or if you try to understand, you will succeed. Or even better, consider investing in shares of companies whose products and services are regularly used.

Banking, cement, transportation, food vending, health related products, telecommunication, etc for example, are somehow straightforward business models; so it is for fast moving consumer goods (FMCG) such as businesses that sells groceries through a large network of supermarkets. Telecom company that sells wireless phone service and operates a popular mobile payment platform, Cement manufacturing and distribution companies, makes ... you guessed it ... well I know what this company does.

Understanding a company's business model and products gives you a clearer view of what factors contribute to its success.

Don't stay far away from established businesses It can be tempting to buy that fast-growing community bank or to participate in that hot IPO that's all over the news. But again if you are not a risk taker, it is better to resist the urge.

Investing in unproven companies can yield higher levels of returns, but they often also come with a high risk of catastrophic loss. Therefore, depending on your risk appetite, it is better that you focus your investment choice on companies that are known quantities, that have proven they can prosper through good economic times and bad. They may not make good conversation material at meetings and parties, but they stand a better chance of building your wealth over time. Remember, investing in shares is lesser of a gamble or speculative business. It is an investment business.

Be Conscious enough to identify scandal, if there is any Have company executives been charged with paying bribes? Has a parent company been caught running a Ponzi scheme? Does it dump toxic sludge into waterways? Does the company mistreat its employee? Malpractice like this is insidious, and it can take years for a company to live it down. Distrust of such companies will weigh on their share prices in a strong way and for a long stretch of time. There are better places to put your hard-earned money to work. You don't need to be associated with businesses that runs into the potential for scandalous.

Remember, sales and revenue growth is crucial for the business If a company isn't selling an increasing amount of products and services to an increasing amount of people, then one may get a sense that there's trouble on the horizon. Yes, there are cases where the company may pursue its smart financial management and accounting treatment and restructuring and hence can boost its earnings for a year or two by cutting costs and becoming more efficient, but if sales are stagnant, in the medium to long term profits will stagnate too.

Look for companies with long-term revenue growth rates that exceed the rate of inflation.

For example if our current inflation rate is 5 per cent, then look to invest in a company where revenue growth and prospect is above the 5 per cent rate.

Consider seriously the issue of profitability, or not Before you invest or consider further investment in a company's stocks, take a look at a company's profitability history. Has it consistently reported negative earnings in the past five years? If so, only consider to invest in the stock if you thoroughly understand the reason for the losses and you are convinced that there are strategies in place that the company is pursuing that will turnaround the situation. That is, if there is a good redemption story and a potential turnaround strategy or plan that will positively impact the profitability of the company, then go for it. Otherwise, for a risk averse investor -- try otherwise.

Look for consistence in dividends payments There is always a push and pull between paying dividends and retaining profits to finance future business growth and expansion. In most cases institutional investors looks for long term returns and would not care much about consistence in dividend payments as long as business growth justifies. But for a retail investor, dividend payment is a big deal. In the overall though, one may say, good companies rarely reduce their dividend, and great companies boost dividends year on year. As an owner, a mature, healthy company should be able to pay you a portion of its earnings in the form of a dividend every year.

If the amount of this dividend is cut, or remains stagnant for several years, there better be a very good explanation for it. If there isn't, then this is a situation worth of serious consideration, especially if there are other better options.

Debts, may be good or bad - consider Companies with heavy debt loads suffer disproportionately during tough economic times and have fewer resources available to them when expansion opportunities arise. What's more, they also have less flexibility to issue dividends or buy back shares.

There, in all consideration, pay attention to the debt to equity ratio for the company and ask questions – why the company carries significant debt obligations.

If there are fair justifications as well as strategies or plans to manage the situation, then it all worth of consideration as you plan to invest or increase investment in a company.

**Mr Marwa is chief executive officer of the Dar es Salaam Stock Exchange**
**Email: moremi@dse.co.tz**

SOLOMON Stockbrokers