ConsciousInvestor® Cloud

Cloud Based Investment Software

User Manual

Version 1.2

Build 9547

ConsciousInvestor® Cloud

by Dr. John Price

ConsciousInvestor Cloud is a sophisticated, yet user-friendly, analysis tool that has been designed to allow all investors to follow a systematic, business-like approach to buying and selling stocks.

Until now, selecting outstanding companies and calculating what price to pay for them has been excessively challenging and time consuming, if not downright impossible.

ConsciousInvestor Cloud completely changes the face of the selection process, and gives you an edge that has never before been available to ordinary investors. You will quickly gain immunity from all the conflicting opinions expressed daily by the talking heads, the gurus, the newsletters, and even your neighbors.

This manual will explain the main features of CI Cloud to help make sure that you get the most from this cutting edge investment tool.

Disclaimer

August 2013; latest update December 2014

Teaminvest

Teaminvest was formed by Howard Coleman, Mark Moreland and John Price. Their idea was simple: They would form a community of experienced and successful investors - people just like themselves. The group would meet regularly to discuss potential investments in a structured and collaborative environment. Teaminvest took its first members in 2009.

All the members are automatically subscribed to Conscious Investor: it plays a core role in the evaluation and discussion of companies. Conscious Investor, by its very nature, focusses on the quantitative side of stock filtering, research and return analysis. This is then augmented by the collective experience, insight and knowledge of Teaminvest members which guides the decisions of individual members. Starting with around 2000 companies on the ASX, the aim is to find genuine Wealth Winners®.

Membership is by invitation only. For further details, visit www.teaminvest.com.au.

Conscious Investor Fund

If you don't have the time to manage your own money, or if you prefer not to have to worry about making investment decisions, in 2013 Howard Coleman, Stephen Harrison and Dr John Price started the Conscious Investor Fund, a wholesale Fund aimed at Australian stocks. The Fund can aslo help you diversify your holdings. It has a unique fee structure based on membership with no fee for funds under management.

The stock selection process in the Fund uses Conscious Investor to filter, research and price companies so that as much as possible all the benefits of being a subscriber of Conscious Investor are transferred to membership of the Fund.

For further details, visit www.consciouscapital.com.au.

Teaminvest Private

Teaminvest Private is the private equity arm of Teaminvest. Through Teaminvest Private, members seek to invest in companies in the size of A$5m to A$50m (though we will consider other investments on a case by case basis). While we predominantly seek control of our investments (i.e. greater than 50% ownership), we are prepared to consider strategic stakes in businesses where a smaller investment is in the company’s long term interest.

For more details about how to become a member of Teaminvest Private and invest in companies through Teaminvest Private, see www.teaminvestprivate.com.au

More details on Teaminvest, the Conscious Investor Fund and Teaminvest Private are given in the last section of the Manual.

Table of Contents

Foreword

The inner value or core of ConsciousInvestor® Cloud is the concept of conscious investing. Putting it simply, this means investing with thoughtful awareness using methods based on evidence and reason. It also means favouring companies with products and services that you support and may even use. Finally, it means recognizing that having money to invest also gives the opportunity to support foundations and causes that you believe in.

There are three steps in ConsciousInvestor Cloud itself for successful investing. The first or outer step is filtering or scanning. It consists of filtering one or more industries, groups of companies you may have tagged or even the whole market to find companies with business excellence and investment potential.

The second or transition step is the analysis or review step. This step provides further analysis of selected companies looking for strong and consistent business performance.

The final or inner step is return or pricing. If looking to invest in a stock, the goal of this step is to determine if it is selling at a price that will give a satisfactory return. If not, then it is important to calculate what would be the appropriate price to offer for it.

If you already own the stock, then this step will help to make the decision whether to keep the stock or to sell it and buy something else.

Everything is set up around these three steps. At different times you may only make use of one or two of the steps. At other times you may modify them by changing the criteria in the filter step, looking at extra charts (including the industry and market charts) in the analysis step, or adjusting the settings in the analysis step to increase the margin of safety. Also you may make use of other features in CI Cloud such as creating reports, or listing companies in the Watch List

The important thing is that these three steps at the core of CI Cloud provide a firm and rational basis to find value in the stock market; in other words, to find Wealth Winners®.

Chapter 1

Menu Bar and Home Page

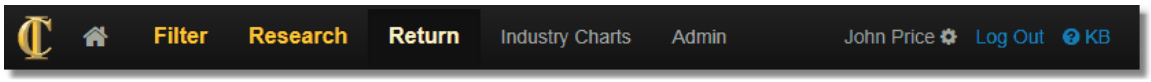
1 Menu Bar and Home Page

This chapter describes the Menu Bar and Home Page of ConsciousInvestor Cloud (Conscious Investor). The Menu Bar runs across the top of each page of Conscious Investor and so can be accessed from any page.

The Home Page is a summary of recent changes in data and Watch List activity. It is the page that displays automatically when you first open Conscious investor.

1.1 Menu Bar

The Menu provides easy access to the key components of Conscious Investor® that help you to select and analyse the market and stocks you are interested in. Notice that the words Filter, Research and Return are displayed in bold. This is to emphasise that the three key steps in Conscious Investor are Filter, Research and Return:



Menu Bar

Items on the Menu Bar

- **Conscious Investor logo**
- **Logo for the Home page** - Clicking on this logo will bring you to the Home Page of Conscious Investor. For more details go to the section Home Page.
- **Filter** - This Filter page allows you search one or more sectors, or even the whole market, to find companies that meet your requirements. You can even filter within preset or "tagged"groups of companies that you might be interested in such as companies in your own portfolio or in a portfolio of companies that you are considering adding to your portfolio. For more details go to the chapter Filter: Stage 1 of Conscious Investor.
- **Research** - The Research page allows to analyse more deeply individual companies using historical charts and internet links. It also allows you to make personal notes about companies, tag them to belong to certain portfolios and to add them to your Watch List. For more details go to the chapter Research: Stage 2 of Conscious Investor.
- **Return** - The Return page gives you information whether to buy, watch or ignore a particular company if you don't already own it, or to hold or sell if you already own it. All this can be done under default historical settings, automatic margins of safety, or your own margins of safety. For more details go to the chapter Return: Stage 3 of Conscious Investor.
- **Industry Charts** - Industry Charts are in two types. First, there are charts that compare different attributes of companies such as return on equity within a specified industry within a given market. Second, there are charts to compare the average over different industries of specified attributes different markets. For more details go to the section Industry Charts.
- **Admin** - You will only see an Admin button of you have administrator privileges.
- **Name** plus Icon - you will see your name or email address in this place followed by a gear "settings" icon. Clicking here will take you to Personal Data,Tag Management, Security and Rollback. For more details on these items go to the sections Personal Data, Tag Management, Security and Rollback. More details are given in the following sub-sections.
- **Log Out** - use Log Out to log out from Conscious Investor, or you can simply close the web page.
- **Help logo** - clicking this logo will take you to an online version of the Conscious Investor manual. For more details go to the section Getting Help.
- **KB** - This is a link to the Knowledge Base, a collection of over 100 brief articles in a

searchable database describing the principles of Conscious Investor. For more details go to the section Getting Help.

1.1.1 Personal Data

Here you will see the personal data we have used as part of your registration including the expiry dates for the different markets. It is accessed by clicking on your name or the gear icon on the main menu bar and selecting Personal Data. Should any of this data be incorrect, please contact us at admin@teaminvest.com.au.

1.1.2 Tag Management

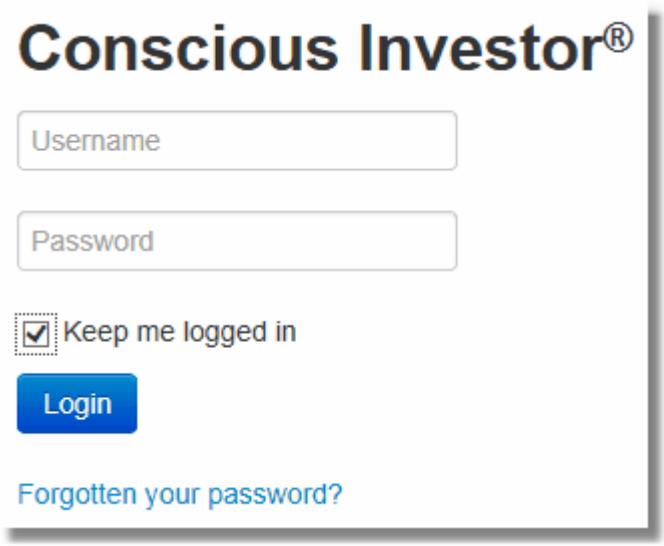
Here you will see details of the names you have given to tag settings and the number of companies with each tag. You can also remove any of the tag settings. It is accessed by clicking on your name or the gear icon on the main menu bar and selecting Tag Management.

1.1.3 Login and Security

Here you can change your password. It is accessed by clicking on your name or the gear icon on the main menu bar and selecting Security.

Please be aware that your password is encrypted within Conscious Investor; we do not keep a copy of your password, nor can we access it. This means that we do not have access to any company reports, notes or personal settings that you may include in Conscious Investor when you log in.

If you forget your password please click on the link "Forgotten your password?" in the login panel in your web browser. This will send an email to your registered email address with instructions how to reset your password.



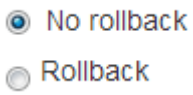
Log In Panel
Web Address: https://online.consciousinvestor.com

Generally your username is your email address.

1.1.4 Rollback

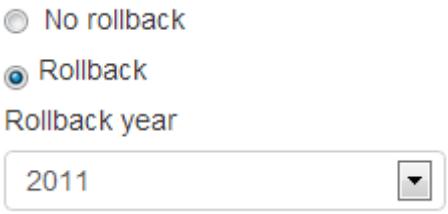
On this page you can reset Conscious Investor so that the Filter stage takes place during an earlier year. It is accessed by clicking on your name or the gear icon on the main menu bar and selecting Rollback. This is a tool in Conscious Investor that helps to give confidence in any filter settings you decide to use because you can see what companies passed the filters in earlier years.

There are two choices: Rollback and No Rollback. The default is No rollback as shown in the next image:



Selection of No rollback

When Rollback is chosen, the opportunity is presented to choose a specific year as shown in the next image:



Selection of Rollback with the Year 2011

Not an exact replication

1. When you rollback to an earlier year, this will not exactly replicate the list of companies that would have passed the filters if they had actually been run at the earlier time. For example, since the system only stores a maximum of ten years of data, if you roll back for five years you are now only using five years of data as part of the analysis. However, if you were actually running Conscious Investor five years ago, you would have access to a full ten years of data.

2. Another reason why this process will not exactly replicate the list of companies is that the rollback analysis uses only average prices for the relevant year; they are not the prices for equities on specific dates such as the first trading day of a calendar year or a financial year.

1.2 Home Page

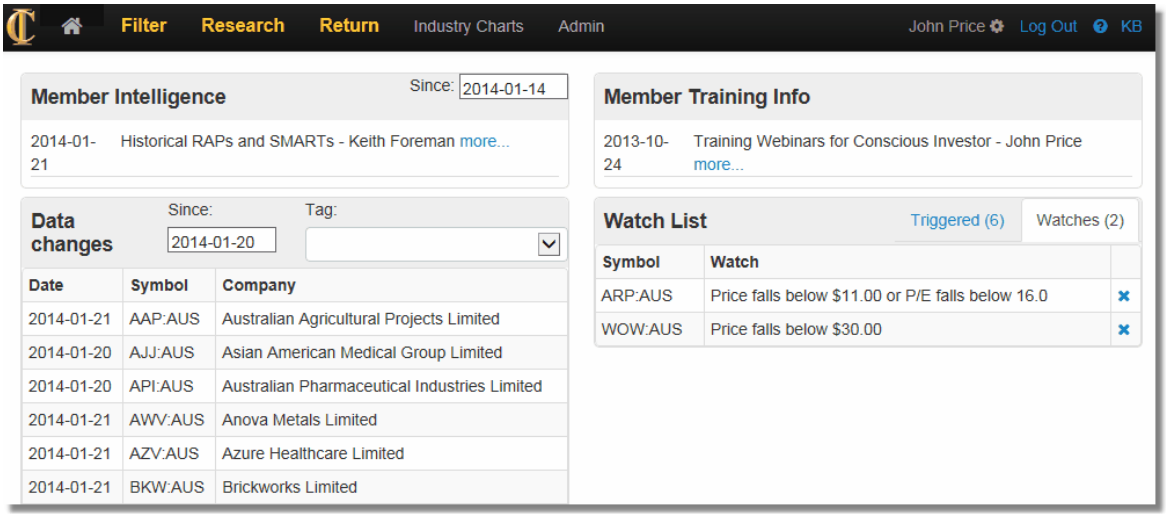
The Home Page is the page in Conscious Investor that displays automatically when you first open Conscious Investor. It is accessed by the logo at the left of the Menu Bar.

Button or logo for the Home Page

The Home Page has four areas:

- Member Intelligence: a list in chronological order of recent additions to information on companies
- Data Changes: a list in chronological order of changes in fundamental data

- Member Training Info: a list of training videos and webinars
- Watch List: a snapshot of your Watch List including any companies with alerts that have been triggered



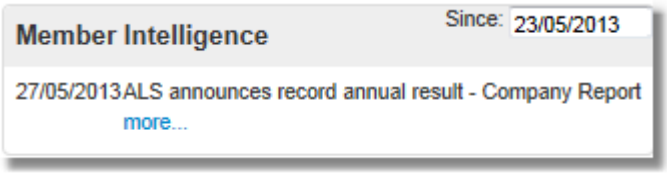
Screen Shot of Home Page

1.2.1 Member Intelligence

The first section on the Home Page is as list of recent entries under the title Member Intelligence. This is information added by administrators that was thought to be of interest or relevance to members.

It automatically lists Member Intelligence since seven days prior to your last login. In other words, if your last login was three days ago, Member Intelligence is listed for the past ten days.

If you wish to see more (or less) Member Intelligence, simply change the date in the calendar box after the word "Since".



Member Intelligence List

1.2.2 Data Changes

The second section in the Home Page is a list of recent data changes in the files containing the fundamental data. For example, if a company has recently published data for a new financial year, then the name of the company may be in this list depending on the actual date of the data change.

Conscious Investor is set up to show the name of the company if the change of data has taken place one day before your last login. In other words, if your last login was four days ago, all companies that have had a change in their fundamental data in the last five days will be listed.

If you wish to see more (or fewer) companies, you can change the calendar box attached to the

word "Since".

Data changes Since: 2013-06-23 Tag:

Date	Symbol	Company
2013-06-23	BOQ:AUS	Bank of Queensland Limited
2013-06-26	CKF:AUS	Collins Foods Limited
2013-06-26	DGR:AUS	DGR Global Limited
2013-06-25	FSA:AUS	FSA Group Limited
2013-06-24	GGE:AUS	Grand Gulf Energy Limited
2013-06-26	MEY:AUS	Marenica Energy Ltd
2013-06-25	MTS:AUS	Metcash Limited
2013-06-26	PNN:AUS	PepinNini Minerals Limited
2013-06-25	BOBE:US	Bob Evans Farms, Inc.
2013-06-25	CRMT:US	America's Car-Mart, Inc.
2013-06-24	DEG:US	Delhaize Group SA
2013-06-24	IXYS:US	IXYS Corporation
2013-06-25	MDT:US	Medtronic, Inc.
2013-06-24	SJM:US	J.M. Smucker Co.
2013-06-24	AGN:CAN	Aegean Metals Group Inc

List of Companies with Data Changes

You may only want to see if there has been any changes in data for companies that you have already tagged. In this case, click the tag box and select the relevant tag name.

Note: Whether there has been a change in fundamental data after any specified date is information supplied to us by our data supplier. Sometimes it may only be a minor change because the company made an adjustment to financial data that was reported in an earlier financial statement. It is often virtually impossible to pick up the actual change. To do this may require looking directly at earlier financial reports by the company and comparing them line by line.

1.2.3 Member Training Info

This section contains descriptions and links to webinars and other sources of training information.

Member Training Info

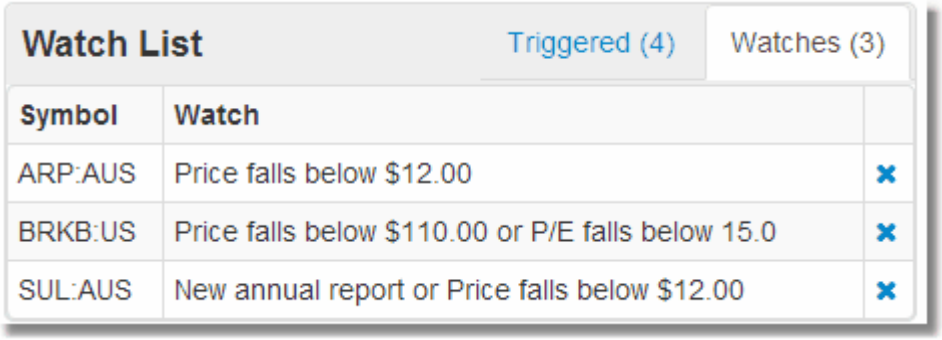
2013-10-24 Training Webinars for Conscious Investor - John Price more...

Member Training Info

1.2.4 Home Page Watch List

The third section in the Home Page is the Watch List. This list is in two part: Triggered and Watches.

- **Watches**: Watches is a list of companies that you are watching to see if their price and or P/E ratio has crossed any thresholds you have set. For example, you may wish to buy shares in a particular company, but only if its price goes below a certain level. Or you may own shares in a company and would like to sell if the P/E ratio exceeds a certain level. You can enter these requirements in the Watch List section of Research. When a new Watch is added it is automatically displayed in alphabetical order. If you set two or more watches on the same company at the same time, the watch will be triggered when any of the thresholds are met. For example, the following image shows that a Watch has been set on Berkshire Hathaway B (BRKB) when the price falls below $110.00 or the P/E ratio falls below 15.0.



Watch List: Three Watches have been set. The Watches on BRKB and SUL are multiple Watches.

- **Triggered**: If any of the alerts you have set are triggered, then name of the company and the details that cause the trigger will be transferred to the Triggered List. For example, in the screenshot below we see that an alert for Cochlear (Australia) was placed for the price to drop below $65.00 and that this has taken place with the price being now $63.66. Four other Watches have been triggered including a trigger for TRS (Australia) that new annual data has been released. By clicking on the column heading **Date** the data is ordered chronologically from oldest to newest. Similarly, by clicking on the column heading **Symbol** the data is ordered alphabetically on the symbol.

Triggered List: The Watch on Cochlear (COH) has been triggered as well as four other Watches. and there are two companies being watched.

Note: To add new companies to your Watch List or to make changes to existing watch settings, you need to go to the Watch List tab of the Research stage of Conscious Investor.

1.3 Getting Help

There are two main ways of getting help to get the most from Conscious Investor: the manual and the knowledge base.

Conscious Investor Manual

The Conscious Investor Manual is a page-by-page description of all the features and benefits of Conscious Investor. It is available as an online version by clicking "?" at the right hand end of the main menu bar. You can also download it as a stand-alone pdf file through the link:

https://online.consciousinvestor.com/teaminvest-manual/ConInv.pdf

Many users report that they get maximum benefit by printing the manual so that it is easily available as a reference.

Knowledge Base

The Knowledge Base is a collection of over 100 short articles and reports on all aspects of Conscious Investor and value investing. It can be accessed through the link:

http://knowledge.conscious-investor.com/knowledge/

Chapter 2

Filter: Stage 1 of Conscious Investor

2 Filter: Stage 1 of Conscious Investor

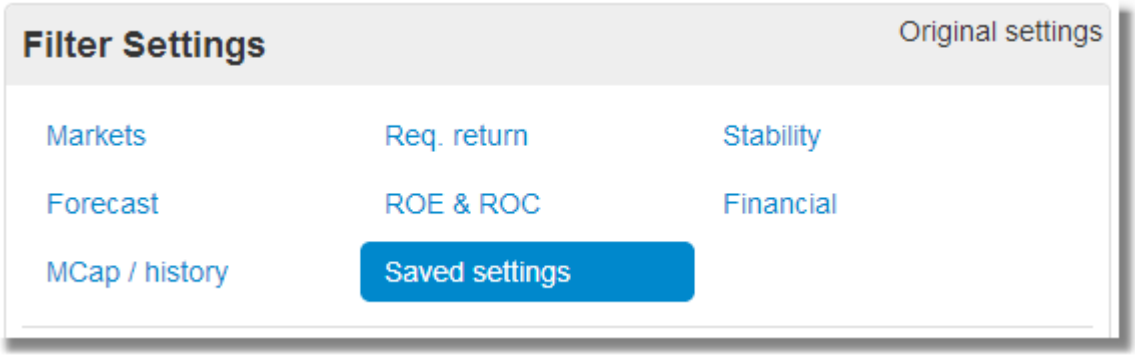
Conscious Investor starts with the filtering or scanning stage. The stage is carried out using the Filtering screen obtained from the Menu bar. Large-scale calculations stage cull thousands of companies to a handful of companies with all the hallmarks of successful businesses and successful investments; in other words, potential Wealth Winners®. The Filter page is in two parts. On the left is the filter panel where the filter settings are viewed and entered. On the right is the display of the companies that have passed the filters. You can also see the reasons why individual companies failed to pass the filters.

2.1 Filter Settings

The filtering starts by choosing a specific market. After that companies are chosen to be part of the filter process via industries, tagged companies or individual companies.

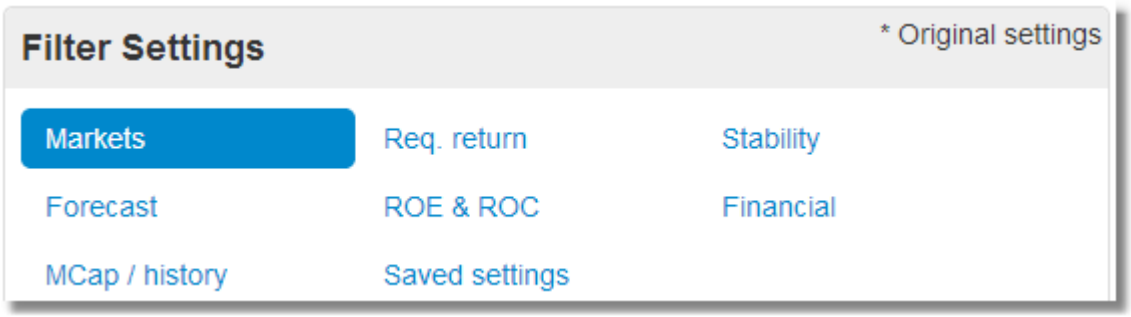
The next step is the actual filtering. This can be done in the areas of Required return, Stability, Forecasts, Return on Equity and Return on Capital, Financial, and Market Cap and History. In each of these areas default levels can be accepted or the threshold levels can be changed.

This filtering can also be carried out using built-in collections of settings. For example, the image below shows that the Original Settings have been selected.



Filter Panel
The top right corner shows that Original Settings have been selected.

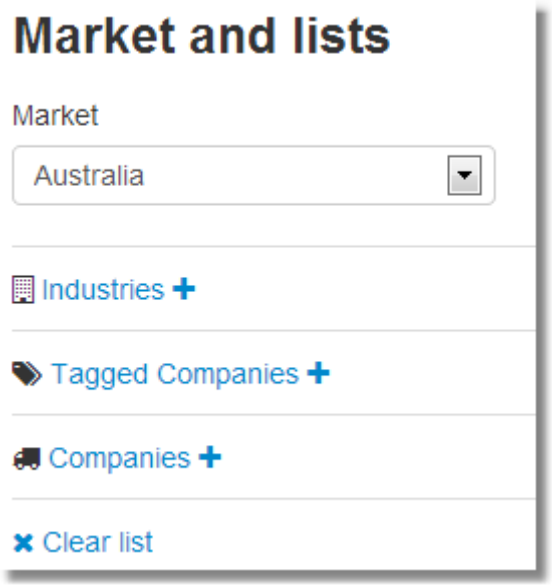
Note: If you change the settings, a "*" will be added to the title of the current collection. This will remain until you save the new collection.



Original Settings changed to *Original settings

2.1.1 Markets

When the Markets button is selected in the Filter Setting you get the option to choose the companies you wish to filter. The selection process includes the market (currently Australia, USA or Canada), the industries within that market (or even the whole market), tagged companies and individual companies.



Selection Panel for Markets, Industries, Tagged Companies and Individual Companies

Step 1: Markets Choose a market (country) by first clicking on the "select" symbol to open the drop-down box and then selecting a market. The following is a list of the markets and the approximate number of stocks available in Conscious Investor for these markets. It is 27 markets with over 63,000 companies.

Note: Depending on your subscription level, you may not have access to all these markets.

Country	Approximate Number of Stocks
Australia	2,000
Canada	4,000
USA	21,000
United Kingdom	2,800
Germany	12,000
France	1,000
Italy	400
Spain	200
Switzerland	300
Turkey	400
Brazil	800
Mexico	600
Chile	400
India	6,300
China	2,700
Japan	300

Country	Approximate Number of Stocks
Hong Kong	1,700
Korea	2,000
Taiwan	1,800
Singapore	800
Malaysia	900
Thailand	1,800
New Zealand	200
Sweden	500
Netherlands	200
Belgium	200
South Africa	400

Step 2: Industries Click on the industries tab. The list of industries is displayed in that market are displayed.In the display list an industry is chosen by highlighting it and clicking on "+ add". After an industry has been chosen it will be marked by "+" as shown in the following screenshot.

Energy Industry Marked with "+"

If you do not want a particular industry to be filtered, select the industry and then click "- Remove".

When you have done this, the filtering takes place automatically. The actual results (depending on the filter settings) are displayed on the right hand side of the page.

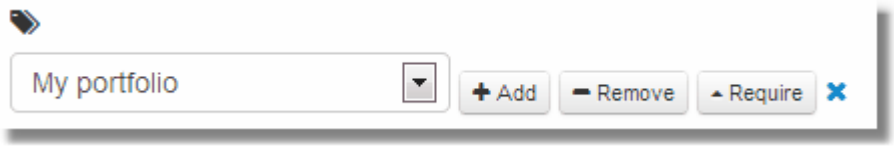
Note: The filtering of a particular industry only takes place when "+ Add" is clicked.

The next two steps, Tagged Companies and Companies, are optional. They are described in the next two sections.

2.1.1.1 Tagged Companies

Instead of filtering on specific industries, it is possible to filter only on those companies that you have already tagged. For example, you can "tag" companies that are in your personal portfolio. Then by filtering on this subset of companies you can quickly see which ones are still passing the filters. Furthermore, by choosing to show all the companies including the failures, colour coding shows why they fail the filters.

You might also tag companies in a test portfolio, companies that you once held but which are no longer in your portfolio, companies that you believe are particularly ethical, and so on.



"My portfolio" Tagged Companies
With the three options: Add, Remove, Require

When you click on "+ Tagged Companies" a drop down box shows a list of tags you have already

made. You are also given three filtering options: Add, Remove or Require

Add Tagged Companies

To select a group of tagged companies, click on the line "Tagged Companies +". This will display the names of groups of companies that you have already tagged such as "My portfolio", "Ethical", and so on. When you select a tag title and click on "+ Add", the companies in this group are subject to the filter process. The result is displayed on the right hand side of the page. In other words, the group of companies are treated as if they were another industry.

Remove Tagged Companies

Suppose you have already filtered a selection of companies by selecting a range of industries. It is possible to remove companies from this selection that you have already tagged. For example, you might have tagged a group of companies with the tag "Unethical". If you select the tag "Unethical" and click "- Remove", these companies will no longer be part of the current filter process.

Require Tagged Companies

Suppose you are already filtering a group of companies. It is possible to filter only those companies and the companies that have a particular tag. For example, you might have companies under the tag "Ethical". Selecting the tag "Ethical" will only filter those companies in your original filter which have the tag "Ethical". Other companies will be removed from the filter process.

Relationship between Add, Remove and Require

Suppose that you are already filtering a set of companies called S and that you have another set of tagged companies called T. The sets that are filtered using the operations of Add, Remove and Require are as follows:

Operation	Description	Symbols
Add	Belongs to S or T	$S \cup T$
Remove	Belongs to S but not T	$S \setminus T$
Require	Belongs to S and T	$S \cap T$

2.1.1.2 Companies

In this optional step you can add individual companies. For example, you want to filter a particular industry. But you are also of the opinion that a certain company should be in this industry even though it is formally in a different industry. Then you can include it by using the tab that says "Companies +".

Note that once you have added the extra company, you can apply a tag to this new group. (Use the Apply Tag link under the Actions button in the top right hand corner of the panel displaying the results of the filter.) This would enable you to filter this group by using Step 3 described above.

Because it is possible to add or remove individual companies, in some cases you may be scanning a partial industry. In this case, provided more than 50 percent of the companies in the industry are subject to the filter process, the name of the partial industry will be marked by "+".

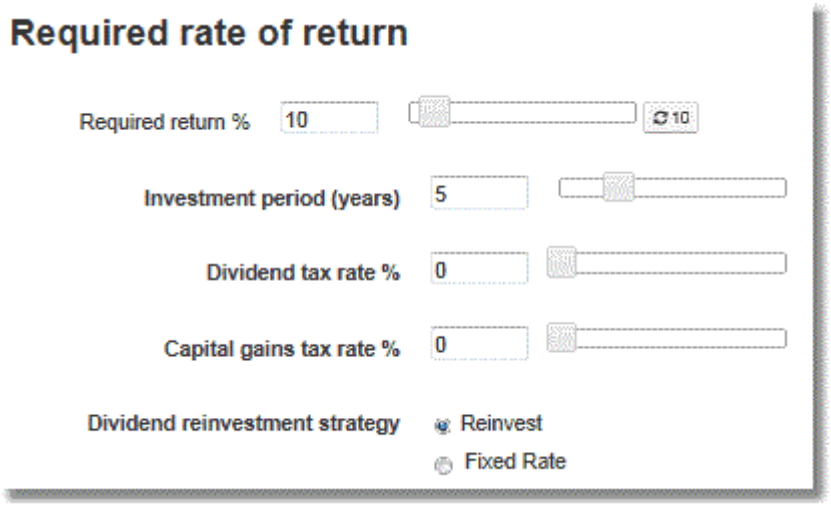
CSL Included in the Filtering

2.1.2 Required Return

Conscious Investor includes proprietary tools that calculates the return you can expect when investing in a company depending on inputs selected by the user. The function that calculates this return is STRET (when dividends are not reinvested but invested separately at a specified rate) and STRETD (when dividends are reinvested).

As a reminder STRET has the derivation STock RETurn and STRETD has the derivation STock RETurn assuming Dividends are reinvested. STRETD is is pronounced STRET-D.

The Required Return button allows you to select the minimum return that you would like for the filtered companies. This is called the required rate of return or RRR. (Sometimes it simply referred to as the required return or RR.)



Required Return Panel

Move the slider to the left or right to select your required rate of return. You can also type it straight into the selection box.

Also select the investment period, dividend tax rate and capital gains tax rate. If you change any of these inputs, they will automatically be changed on the Return page.

Finally, you can decide whether you want the return to be calculated assuming that you reinvest the dividends or you want to reinvest the dividends at a fixed rate. Selecting "Reinvest" does not mean that you have to reinvest your dividends. Merely that this is a standard means of placing all investments on the same footing making it easier to compare them. (When the return of an investment is calculated assuming the dividends are always used to buy new shares, it is usually referred to as total shareholder return or just total return. It is denoted by TSR.)

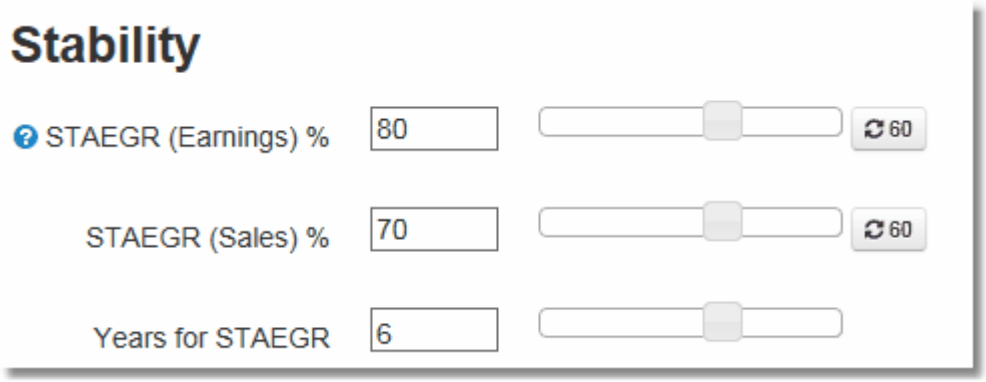
Note that some companies offer a procedure whereby dividends are automatically used to buy further shares at the current price or a small discount to the current price. One of the disadvantages is that it can be difficult to calculate taxes when you sell because you are likely to

have a large number of small parcels of shares. This procedure is commonly referred to by the acronym DRIP (or sometimes simply DRP) meaning "dividend reinvestment plan".

If you choose "Fixed Rate" a slider will appear allowing you to choose the investment rate for the dividends.

2.1.3 Stability

Stability of the growth of earnings and sales is an important part of gaining confidence in the future growth of a business. In Conscious Investor stability is measured by a proprietary tool called STAEGR®. It measures of the stability of the growth of historical data from year to year expressed as a percentage. The maximum figure of 100 percent represents earnings that go up (or down) by the same percentage each year. Consistent year upon year growth gives a high STAEGR. For more details on this vital concept, see the section Stability of Growth: STAEGR.



Screen for Setting Levels of STAEGR

This screen is accessed by clicking the link Stability on the Filter page. It allows you to separately alter the stability requirements. The sliders each individually adjust the particular factor, or the required level can be typed straight into the relevant selection box. Also can can select the number of years used to calculate STAEGR. The default is 6 years. (This is actually 5 full years covering 6 data points.)

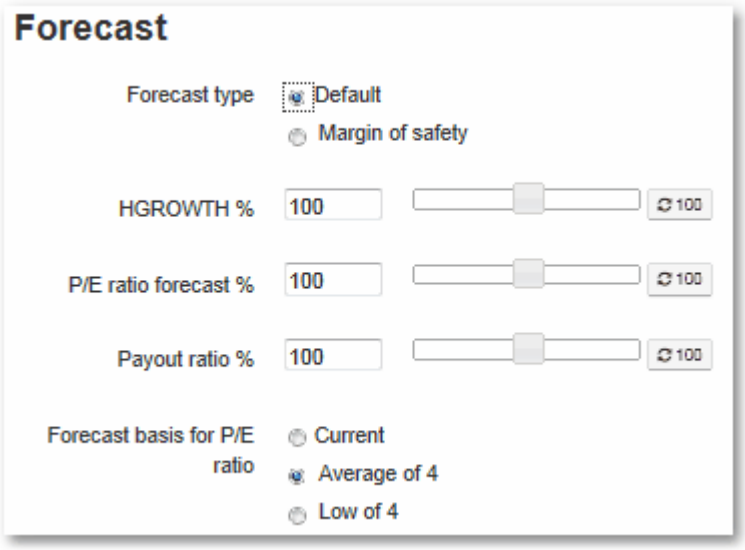
Clicking in the boxes to the right of the sliders return the stability requirement to the default level. In the above image the default is 60 percent for the stability of earnings and sales.

2.1.4 Forecast

Calculation of the expected return of an investment in a particular company is based on a few fundamental forecasts: these are the growth rate of the earnings per share, the P/E ratio and the dividend payout ratio.

The Forecast panel allows the user to set different methods for making these forecasts. The two basic forecasts methods are default and margin of safety.

Note: The Forecast panel is for making global forecasts as part of the filter process. Particular forecasts for individual companies can be made in the Return section of Conscious Investor.



Forecast Panel with Default Selected

Forecast Type: Default

When Default is selected, the forecast is based on historical data for each company. The sliders allow the forecasts to be set as percentages of the historical levels. In each case the default is 100 percent. Using lower percentages increases the degree of conservatism of the forecasts. The percentages can be changed by moving the sliders or typing a new percentage into the relevant box. The buttons at the end of each line display the default levels. Clicking a button returns the setting to the default level.

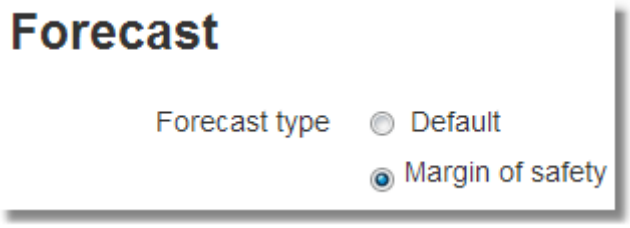
HGROWTH: If the HGROWTH slider is set at 100 percent, the assumption is that future growth of earnings per share (EPS) will continue at the same level as past growth. If it is changed to, for example, 90 percent, the assumption is that future growth is at 90 percent of the past growth.

P/E ratio forecast: This "P/E ratio forecast" slider sets the future P/E ratio as a percentage of the current P/E ratio, the average P/E ratio over the past four years or the lowest annual average P/E ratio over the past four years. Which of these three possibilities is used depends on selecting the relevant radio button. The default is the average of the last four years.

Payout ratio: The "Payout ratio" slider sets the dividend payout ratio as a percentage of the average payout ratio over the past four years.

Forecast Type: Margin of safety

If the "Margin of safety" radio button is selected, Conscious Investor implements automatic margins of safety for the forecasts of growth rate of EPS, the P/E ratio and the dividend payout ratio. In this case, growth rate of the earnings per share, the P/E ratio and the dividend payout ratio are selected automatically based on proprietary algorithms within Conscious Investor.

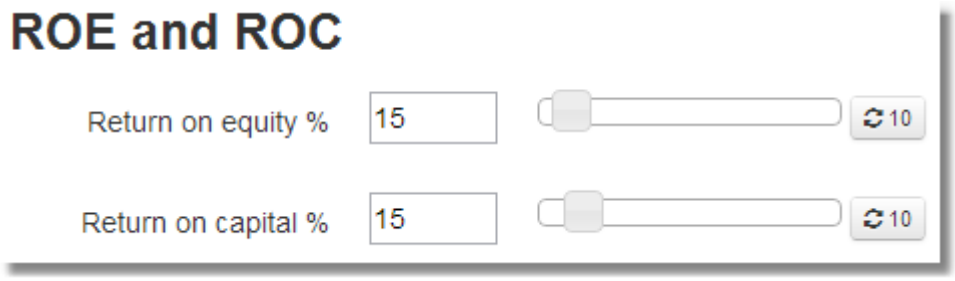


Forecast Panel with Margin of Safety Selected

For more details on the significance of margins of safety, see the section Margin of Safety.

2.1.5 ROE & ROC

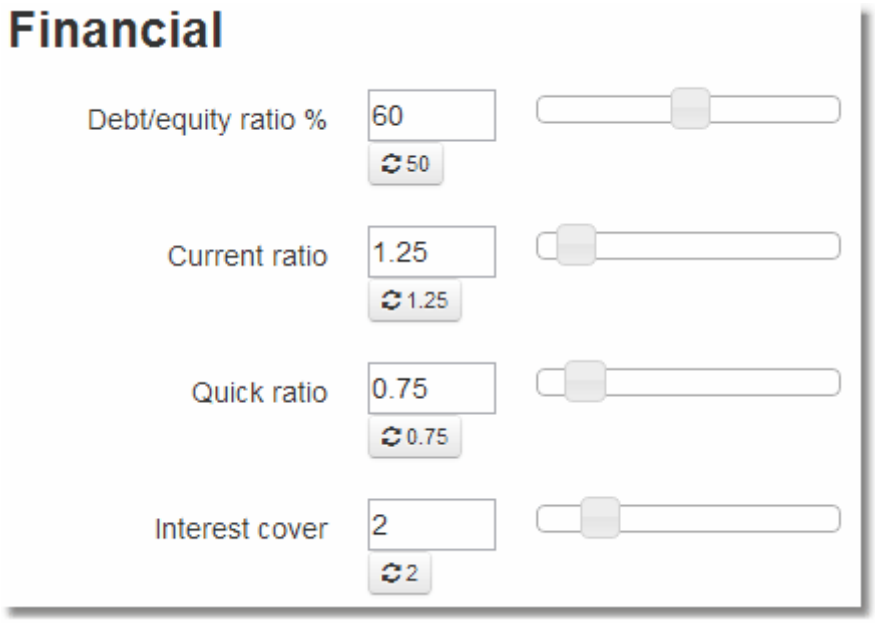
The tab called ROE & ROC allows settings to be made for the minimum levels of return on equity (ROE) and return on capital (ROC). The settings can be made by moving the slider or typing the required value directly into the box. The boxes to the right of the sliders display the default levels. Clicking on them will automatically return the settings to the default levels.



**ROE and ROC Selection Panel:
ROE and ROC are set at 15%,
the default levels are 10%**

2.1.6 Financial

The Financial tab allows you to change the requirements in four areas related to the capital structure of the company: debt to equity ratio, current ratio, quick ratio and interest cover. The required level can be changed by moving the slider or by typing the required level in the appropriate box. The smaller box displays the default settings: clicking on these will return the setting to the default level. For example, in the image below the debt to equity requirement has been changed to 60 percent whereas the default level is 50 percent.



Four Sliders for Changing Financial Requirements

2.1.7 Market Cap and History

The MCap / History tab allows you to change the requirements for the market capitalisation (Market cap) and years of history of the company.

Market Cap: Market cap is the total number of shares outstanding multiplied by the current share price. It is the amount it would cost to purchase all shares on the market at their current price. There are three variations for market cap: only companies with market cap above the specified level, below the specified level, or all companies (meaning independent of the specified level). The variation is selected by clicking the down arrow in the "Selection type" box. The market cap is changed by typing the amount directly into the "Market capitalisation" box. As an example, if you require the amount $200 million, you can type it as 200m or 200000000. In bother case it will rewrite the entry as $200.00M.

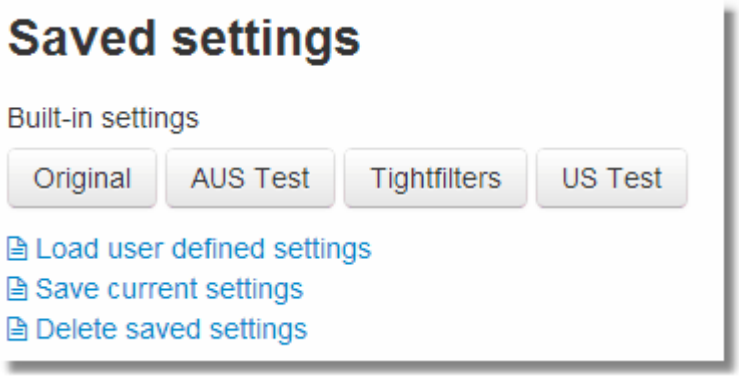
Years of history: When a company becomes a public company and is listed on a stock exchange its financial statements are made available to the general public. (The precise requirements, including auditing requirements, for these financial statements varies between companies and stock exchanges. However, in the main they satisfy what are referred to as GAAP or generally accepted accounting requirements.)

When analysing company data in Conscious Investor, for consistency and reliability we only consider properly reported data. The number of years of properly reported data is controlled by the Years setting. The setting can be changed by moving the slider or typing the requirement directly into the "Years" box.

Market Cap and Years of History Panel
Market cap is set at 100 million dollars or higher;
Years of history is set at 4 years or more.

2.1.8 Saved Settings

Conscious Investor comes with various built-in collections of settings. You can also change the settings. Once you have changed the settings you can save them so that you can easily recall them later. (See the section Saving Settings below.)



Panel for Choosing Settings
You can choose built-in settings, load user defined settings,
or you can save the current settings

To remove user-defined settings, choose the settings and then select "Delete saved settings". This will give you the opportunity to remove the settings.

Built-in Settings

The built-in settings are Original, AUS Test, Tightfilters and US Test. They are briefly described in the next table.

AUS test	Settings used in testing Conscious Investor for the Australian market.
Original	These are the settings of Conscious Investor when it is originally installed.
Tightfilters	These are the filters that correspond to companies appearing in black in the selections window.
US test	Settings used in testing Conscious Investor for the US market.

AUS test and US test

The preloaded settings AUS test and US test were chosen as reasonable settings to test the performance of Conscious Investor on a year by year basis. In no sense are they supposed to be the "best" settings. The main reason for choosing these settings was that they seemed to give rise to a number of stocks that approximated the number of stocks in portfolios commonly held by individual investors. In individual cases you might want to change the filters to increase or decrease the number of stocks that passed. Also the settings were chosen before the automatic margin of safety was incorporated in Conscious Investor. So you may want to consider switching on the automatic margin of safety.

Another disadvantage of the settings AUS test and US test is that many excellent companies such as Wal-Mart in the US and Woolworths in Australia are immediately excluded because of low current ratios and quick ratios no matter how they score on the other filters. To see why this is the case it is necessary to understand that the filter levels for the current ratio and quick ratio are set at levels that make sense when looking at most industrial companies where payables and receivables are approximately equal. However, cash based companies such as Wal-Mart and Woolworths have payables far higher than receivables. This knocks them out because of very low current ratios and quick ratios.

The table below describes the actual levels for the preceding preloaded settings.

Data Item	Settings			
	AUS Test	Original	Tightfilters	US Test
Debt to Equity Ratio	50%	75%	50%	50%
Current Ratio	1.0	0.0	1.25	1.0
Quick Ratio	0.75	0.0	0.75	0.75
Interest Cover	2.0	5.0	5.0	2.0
STAEGR (Earnings)	85%	60%	85%	85%
STAEGR (Sales)	85%	60%	85%	85%
Required Return	15%	10%	10%	15%
HGROWTH Forecast	100%	100%	100%	100%
P/E Forecast	100%	100%	100%	100%
Payout Forecast	100%	100%	100%	100%
Reinvestment Rate	10%	10%	10%	10%
Reinvestment Period (Yrs)	5.0	5.0	5.0	5.0
ROC Hurdle	10%	10%	10%	10%
ROE Hurdle	10%	10%	10%	10%
Required Return	15%	10%	10%	15%
Stability (Years)	6	6	6	6

Saving Settings

If you change the settings, it is possible to save them for use at a later time. Simply click the link "Save current settings" and type in a name of your own choosing. Then click the check mark to save the settings. Clicking "Load user defined settings" allows past saved settings to be loaded. Click "X" to remove settings.

Panel for Saving or Loading Settings

2.1.9 Testing and Backtesting: Test or Research Portfolios

For each calendar year since 2000 test or research portfolios have been constructed using Conscious Investor® and their performance measured over the corresponding full calendar year. This is an outline of testing and backtesting procedures used to construct these theoretical portfolios.

Most of the tools in Conscious Investor were developed and tested before the actual design and build stage in 2000. (Some tools were added later such as the automatic margin of safety and the automatic descriptions of two of the key charts.) Three years after Conscious Investor was up and running, a procedure was set up to re-test the results to make sure that they lived up to expectations.

For the testing the settings were based on the settings AUS_test and US_test. As explained in the previous section, the main reason for choosing these settings was that they seemed to give rise to a number of stocks that approximated the number of stocks in portfolios commonly held by individual investors. Roughly between 15 and 30.

The plan was to run Conscious Investor towards the start of each calendar year and form a theoretical portfolio consisting of the stocks that passed the filters. The portfolios were to be formed with equal dollar values for all the stocks. The idea was to hold them until the first trading day of the next calendar year with no trading or rebalancing during the year. In other words, once a stock was in the portfolio it stayed there for the full 12 months.

To get as many years of data as possible for the study I used the rollback feature with AUS_test and US_test settings for the calendar years for the early years.

After that the stocks were usually chosen by actually running Conscious Investor during the calendar year and not using the rollback feature. One exception was if the portfolio was considered to be "too" small (less that 12 stocks). Then the STRETD-criterion for AUS_test or US_test was lowered to 10 percent from 15 percent to allow more companies to pass.

The return for each of the companies was calculated using the percentage growth from closing price on the first trading day of the calendar year to the closing price on the first trading day of the next calendar year. The average of these returns was used to calculate the average return for the respective portfolios. For the Australian portfolios calculations were also carried out with the inclusion of dividends.

Over the first 12 years of testing the theoretical Conscious Investor portfolios have performed well usually outperforming the corresponding index.

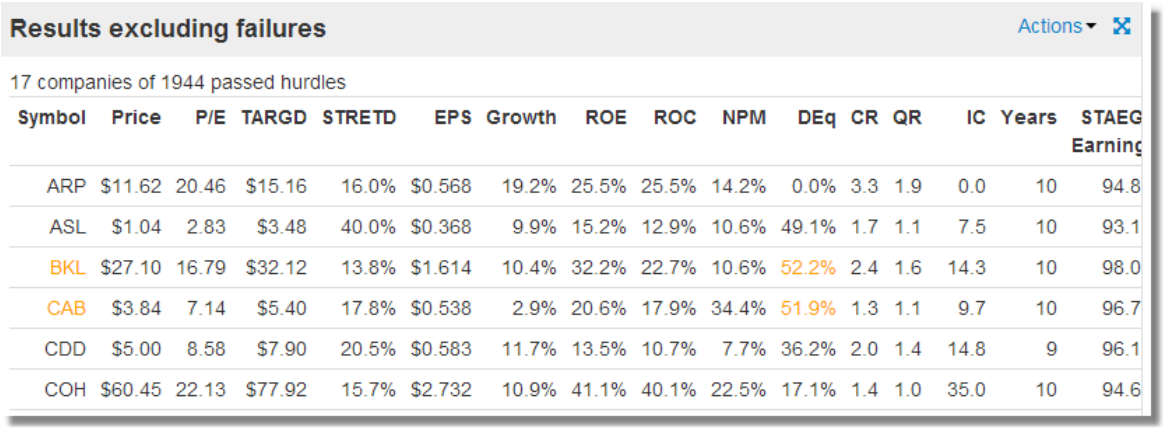
Comments
1. These are test or research portfolios: it is unlikely that they could be achieved in practice.
2. No transaction costs or other fees were included.

3. It may not be possible to fulfill the orders at the prices used in the study.
4. In some cases the portfolios were chosen using the rollback feature and not actually on the first trading day of the year. (Because of survival bias, this could lead to a higher performing portfolio.)
5. In some cases the filters were modified to get a larger portfolio by changing the STRETD requirements.
6. Although the settings AUS_test and US_test were chosen using the general principles of Conscious Investor (such as stocks with high STAEGR), in no way should they be taken as optimal.

Important Disclaimer: no guarantee is given or implied that these methods or any variations of them, will give any particular performance for portfolios chosen using the methods.

2.2 Selection Results

The selections screen on the far right of the Filter page represents the stocks that have passed all of the hurdles you have set using the Filter Settings. Each row displays the data for a single company. For discussions of the colours, see the sections Selections in Black, Selections in Orange and Selections in Red.



Results excluding failures Actions

17 companies of 1944 passed hurdles

Symbol	Price	P/E	TARGD	STRETD	EPS	Growth	ROE	ROC	NPM	DEq	CR	QR	IC	Years	STAEG Earning
ARP	$11.62	20.46	$15.16	16.0%	$0.568	19.2%	25.5%	25.5%	14.2%	0.0%	3.3	1.9	0.0	10	94.8
ASL	$1.04	2.83	$3.48	40.0%	$0.368	9.9%	15.2%	12.9%	10.6%	49.1%	1.7	1.1	7.5	10	93.1
BKL	$27.10	16.79	$32.12	13.8%	$1.614	10.4%	32.2%	22.7%	10.6%	52.2%	2.4	1.6	14.3	10	98.0
CAB	$3.84	7.14	$5.40	17.8%	$0.538	2.9%	20.6%	17.9%	34.4%	51.9%	1.3	1.1	9.7	10	96.7
CDD	$5.00	8.58	$7.90	20.5%	$0.583	11.7%	13.5%	10.7%	7.7%	36.2%	2.0	1.4	14.8	9	96.1
COH	$60.45	22.13	$77.92	15.7%	$2.732	10.9%	41.1%	40.1%	22.5%	17.1%	1.4	1.0	35.0	10	94.6

Typical Selections Display Showing Companies in Black and Orange
The companies are shown in Orange because at least one of the cells is in orange.
A cell is in orange because the data fails to meet the level specified in the "tight filters" setting.

The following table shows the headings of the columns. Note that only one of STRETD or STRET will appear at the same time depending on the settings in the Dividend reinvestment strategy in the Required rate of return panel. The same applies to TARGD and TARG.

Heading	Description
Symbol	Ticker or symbol of the company.
Price	Current closing price of company.
P/E	The P/E ratio used in the calculation of TARGD/TARG and STRETD/STRET
STRETD	Forecast of stock return per year assuming dividends are

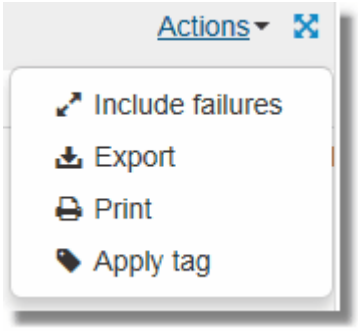
	reinvested.
STRET	Forecast of stock return per year assuming dividends are invested at the specified rate.
TARGD	Target price assuming dividends are reinvested.
TARG	Target price assuming dividends are invested at the specified rate.
EPS	Earnings per share over the trailing 12 months
Growth	Average annual growth rate calculated using HGROWTH.
ROE	Return on equity for last financial year.
ROC	Return on capital for last financial year.
NPM	Net profit margin for last financial year.
DEq	Debt to equity ratio at end of last financial year.
CR	Current ratio at end of last financial year.
QR	Quick ratio at end of last financial year.
IC	Interest cover
Yrs	Years the company has been listed as a public company
STAEGR Earnings	Stability of earnings per share calculated using STAEGR
STAEGR Sales	Stability of sales per share calculated using STAEGR
Yield	Dividend yield
MCap	Market cap
Name	Name of the company

Time Periods

The time periods for the calculations for STRET, STRETD, TARG or TARGD are set in the Required Rate of Return panel in the Filter settings page.

Actions

In the top right hand corner there is a drop down box called Actions. Links in the box allow you to include (or exclude) failures in the display and to export, print or apply tags to the displayed companies.



Contents of Action Box

Include or exclude failures: When *Include failures* is selected, the companies in the search category that failed the filters are included in the display. To distinguish them from the compnaies that pass the filters, they are displayed with a light red background. See the section Selections in Red.

Export: When the *Export* option is selected, the data is exported to a CSV file. This can be opened

as a spreadsheet.

Print: When the *Print* option is selected, the data is exported as a pdf file. This file can be printed or saved to your computer.

Apply tag: When the *Apply tag* option is selected, a tag can be applied to all the companies passing the current filters.

The icon  expands the data on the selected companies to full screen; the icon  returns the display to the original format.

Change Order of Columns

If you left click and hold in the heading of a column, the column can be dragged to the left or the right. This allows to to change the order of the columns.

Sorting on the Order in a Column

If you left click in the heading of a column, all the data on the page will be sorted so that the data in the selected column is sorted from the highest to the lowest. Clicking a second time will change the sorting from the lowest to the highest.

2.2.1 Selections in Black

If the data entry of a company shown in the Selections Screen is in black, this means that the data satisfies the current and the settings contained in the collection of filters called Tightfilters. If all the data entries are shown in black, then the name and symbol of the company will also be shown in black.

2.2.2 Selections in Orange

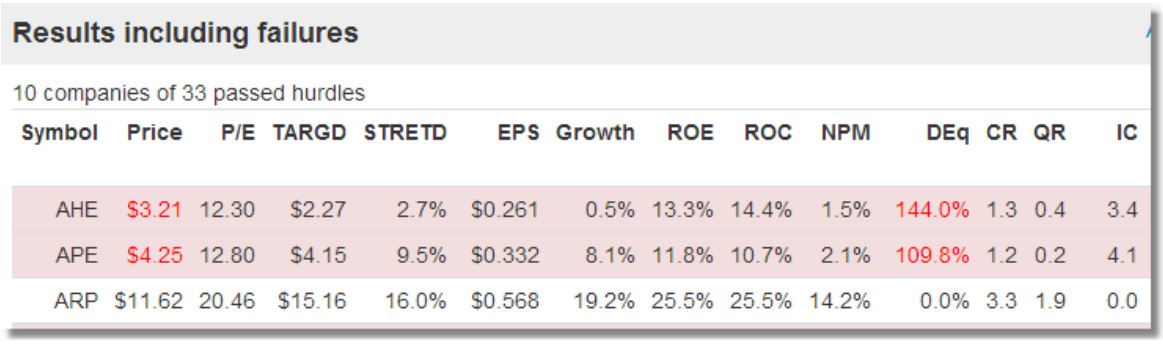
If the data entry of a company shown in the Selections is in orange, this means that the data satisfies the current settings but does not satisfy the set of filters called Tightfilters. If one of the data entries is shown in orange, then the name and symbol of the company will also be shown in orange.

2.2.3 Selections in Red

The default is that only the companies that pass the settings of the filters are displayed on the right hand side of the Filter page. However, by selecting "Include failures" in the Action box, all companies in the chosen sectors or with the selected tags will be displayed.

To distinguish between those that pass the settings, the companies that fail will be displayed with a pale red background. Also the entry (or entries) where the company fails the specific filter will be displayed in red.

In the image below AHE and APE have shaded backgrounds because they fail the filters. First they fail to meet the required STRETD meaning that their prices are too low. Hence in both cases their prices are shown in red. Second, their debt to equity ratios fail to meet the required level and so the DEq entries are shown in red.



Results including failures

10 companies of 33 passed hurdles

Symbol	Price	P/E	TARGD	STRETD	EPS	Growth	ROE	ROC	NPM	DEq	CR	QR	IC
AHE	$3.21	12.30	$2.27	2.7%	$0.261	0.5%	13.3%	14.4%	1.5%	144.0%	1.3	0.4	3.4
APE	$4.25	12.80	$4.15	9.5%	$0.332	8.1%	11.8%	10.7%	2.1%	109.8%	1.2	0.2	4.1
ARP	$11.62	20.46	$15.16	16.0%	$0.568	19.2%	25.5%	25.5%	14.2%	0.0%	3.3	1.9	0.0

Display of Companies including Failures
Only the first three companies are shown.

Chapter 3

Research: Stage 2 of Conscious Investor

3 Research: Stage 2 of Conscious Investor

Once companies have been chosen using the Filters of Stage 1, this stage consists of research on chosen companies. The companies may be chosen using the filters of stage 1 or they may be chosen from other sources. Either way, it is important that they are thoroughly analysed and researched. The research in Conscious Investor is quantitative. It is up to individuals to supplement this with qualitative research on the companies. In Conscious Investor this step is carried out using the Research link obtained from the Menu bar.

The Research stage has the components:
- Details
- Analysis
- Charts
- Data
- Watch List

These components are accessed via tabs below the main Menu bar at the top right of the page.

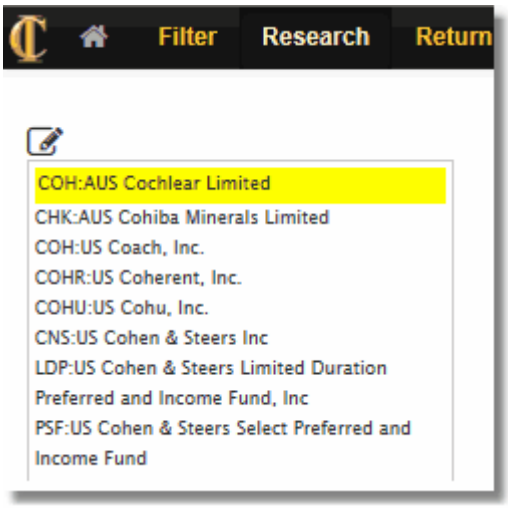
Tabs for the Research Stage

3.1 Company Name or Symbol

The first step in the Research stage is to select a company. This is started by clicking on the pencil icon at the top of the page. This causes a text box to be displayed.

Pencil Icon:
Click to Enter Company Name or Symbol

Next slowly type the name of the company or its symbol in the text box.. As each new letter is typed, the list contracts down to the companies with these letters as part of their name or part of their symbol. The screenshot below is a result of typing the letters C O H and then selecting the first entry which is COH:AUS Cochlear Limited. As an entry is selected it is highlighted in yellow. Once a company is highlighted in yellow, left clicking on it introduces it into the Company Details page, the first page of the Research Section..



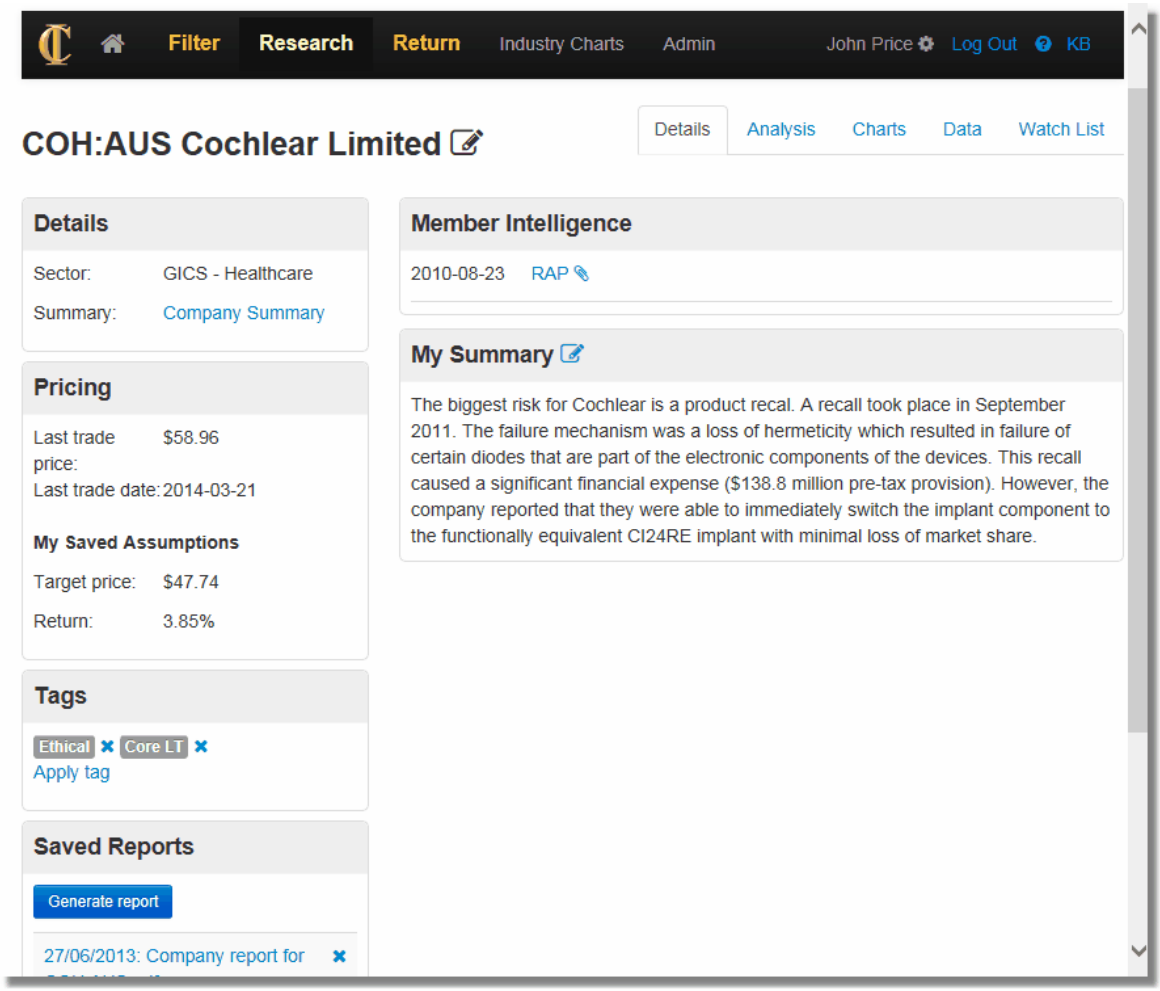
The result of typing C O H

Note: Each time a new letter is typed, this information is sent to the server at our data centre where a sorting process is started. The result of this sort is returned to your computer. For this reason it is important that the letters are typed slowly so that this interchange process has time to be completed at each stage.

3.2 Company Details

Once a company has been selected in the Details page of the Research step, a summary of the company information is displayed. The summary is in the sections:

- Company symbol
- Details
- Pricing
- My Saved Assumptions
- Tags
- Saved Reports
- Member Intelligence
- My Summary



Details Page

Company Symbol: The company symbol (or ticker) is shown followed by the country of the company and its full name. Clicking on the pencil icon after the company name allows the company to be changed.

Details: The Details section starts with the sector of the company. The words Company Summary are a link to an internet finance site containing more information on the company.

Pricing: This section contains the last trade price for the previous trading day and the date of this day.

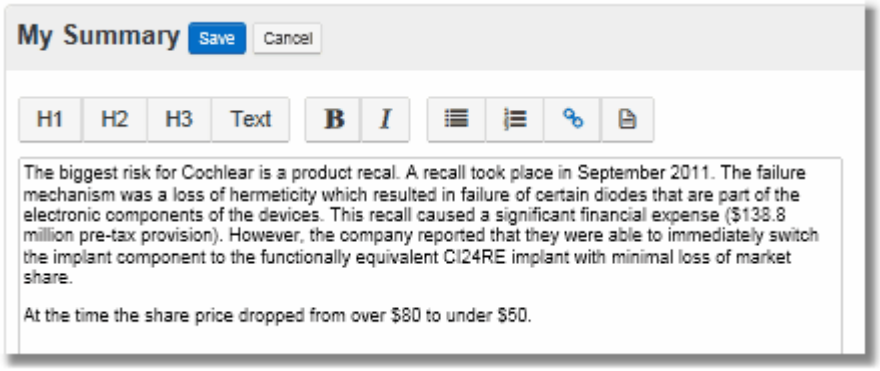
My Saved Assumptions: On the Return Page you can make changes to the inputs for the calculation of STRET/STRETD and TARG/TARGD. These inputs and the results of the calculations can be saved in the line called "Saved". When this is done the results of TARG/TARGD are saved as "Target price" and the results of STRET/STRETD are saved as "Return" in the section My Saved Assumptions. If you did not make save any changes or do not make any changes, the entries will be "None set".

Tags: Companies can be singled out for membership in special groups by labeling or "tagging" with the name of the group. The names of these groups are shown in this section. Clicking on "Apply tag" gives the opportunity to add a new tag.

Saved Reports: Clicking on "Generate report" generates a report containing any text you have entered in "My Summary", a display of all the data and calculations on the Return page, and key fundamental charts relating to the company.

Member Intelligence: This section contains a list of articles, notes and reports related to the company that have been added by on of the Conscious Investor administrators. You can also see a list of earlier reports that you have generated and saved.

My Summary: In this section you can add your own summary or notes on a company. Click on the pencil icon to open the editor. The buttons labeled H1, H2 and so on allow for basic formatting and the addition of internet links. To save the text, click on the button "Save".



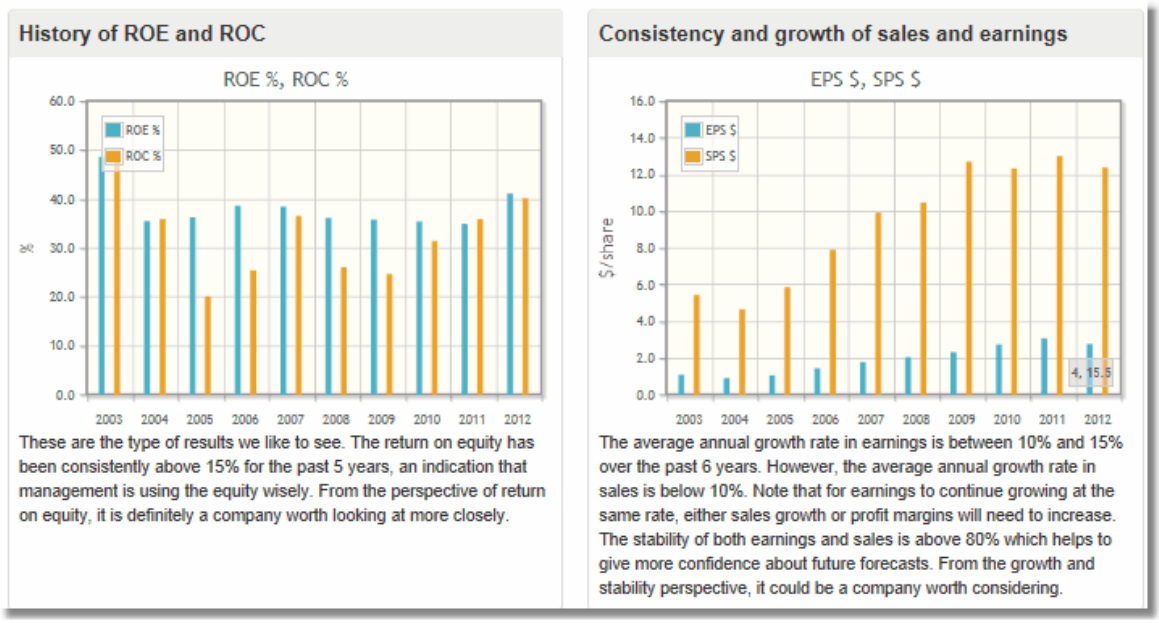
Text Entered by User

3.3 Analysis

The core of the Analysis page is two key charts followed by descriptions of their content and significance.

The first chart has the title "History of ROE and ROC". It displays the Return on Equity and Return on Capital for up to ten years.

The second chart has the title "Consistency and growth of sales and earnings". It displays earnings per share and sales per share for up to ten years.



Key Charts and Summaries

Below the charts is a description in plain English describing their content and their significance in considering the company as a future investment. Comments on the significance of the data in the first chart range from "From the perspective of return on equity, it is definitely a company worth looking at more closely." to "Unless investors have very good reason to believe that the company will turn around, from the perspective of return on equity it is probably best that they look elsewhere."

For the second chart they range from "From the growth and stability perspective it is definitely a company worth considering." to "As the average annual growth rate in both sales and earnings for the past 5 years is negative, you would need strong evidence of a turnaround to consider this company. A high reliable dividend yield would also help."

This "expert system" or Wizard within Conscious Investor is a remarkable tool to help you evaluate the investment potential of thousands of companies. For more details see the section Automatic Company Analysis.

3.4 Charts

It is often said that a picture is worth a thousand words. The historical charts in Conscious Investor are a powerful and effective way of quickly displaying and examining large amounts of data. This helps to spot any trends or anomalous data that needs to be examined in more detail. This section contains the company charts: industry and market charts are obtained by clicking on "Industry Charts" on the Menu Bar. For more details on industry and market charts, see the section Industry Charts.

3.4.1 Chart Panel

The types of charts are chosen via the Chart Panel. The top of the panel allows the selection of default charts. Below that are settings for two-dimensional (2D) or three-dimensional (3D) charts, normalised or regular data, and charts with or without labels.

Single measures or attributes can be displayed or combinations of companies and/or attributes.

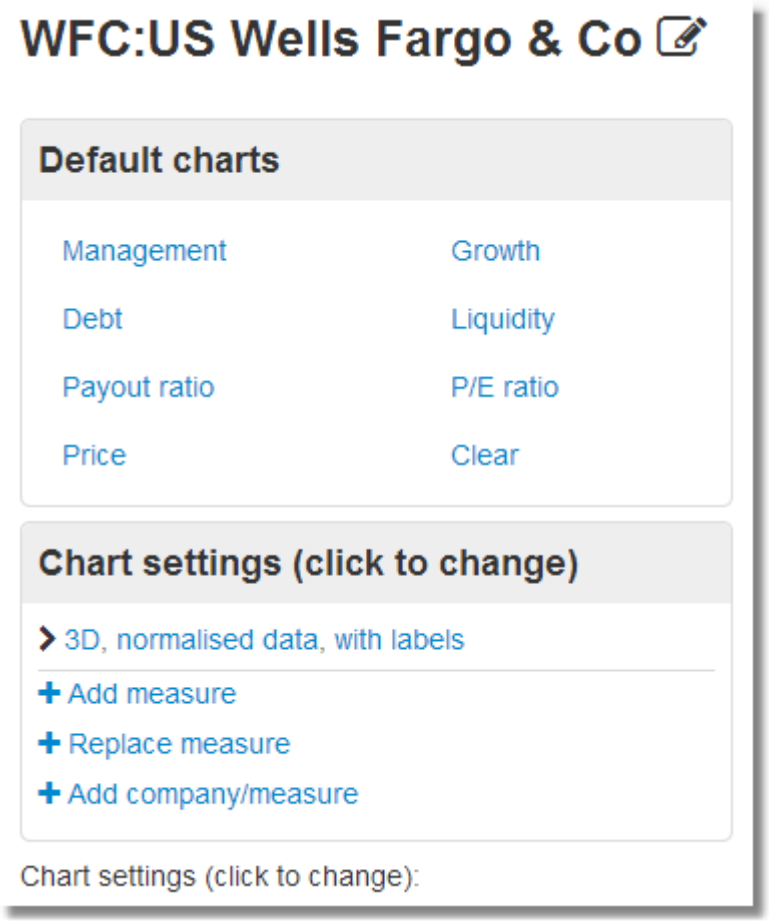


Chart Panel

Once a company is selected, different charts and combinations of charts can be displayed using the Chart panel. There are two sections of the panel for choosing charts, Default charts and Chart settings. There is also a section with toggle switches to change the appearance of the charts.

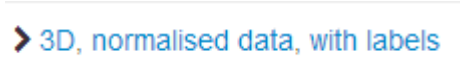
Default Charts: The section of the Chart panel called "Default charts" permits the display of key combination charts that have already been preset. See the section Default Historical Charts for more details.

Chart Settings: The next section called Chart settings permits the display of individual and combined measures for single companies and multiple companies. See the section Company Historical Charts for more details

Toggle Switches: The links 3D / 2D, normalised data / raw data and with labels / no labels allow charts to be toggled back and forwards between different formats as shown in the next table.

Toggle	Effect
2D / 3D	Switches between the charts being displayed in 2-dimensional and 3-dimensional formats.
normalised data / raw data	Switches between the data being displayed as normalised data (meaning the percentage deviation for the mean) and the stadard or raw data
with labels / no labels	Switches between the data displayed with labels and without labels.

The following image shows an example of the toggle switches. Since, for example, 3D is shown, the chart would be shown in 2-dimensional format and clicking on 3D would convert the chart to 3-dimensional format.



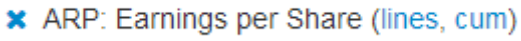
Example of Settings Panel for Toggle Switches

It is also possible to toggle between displaying the data as bars or lines, and as non-cumulative (that is, raw data) or cumulative as shown in the next table:

Toggle	Effect
lines / bars	Switches between displaying the data as bars or columns and as lines. It can be useful when displaying a number of measures to show some as bars and some as lines.
cum / non-cum	Switches between the data being displayed as raw data (non-cumulative) and as cumulative data which means adding the data for each year to the previous data. This would allow, for example, to see the total earnings per share accumulated over the period of the chart.

The following image shows an example of the chart display panel. Since, for example, "lines" is shown, the chart would be displayed as bars and clicking on "lines" would convert it to a line chart.

Example of the forat panel



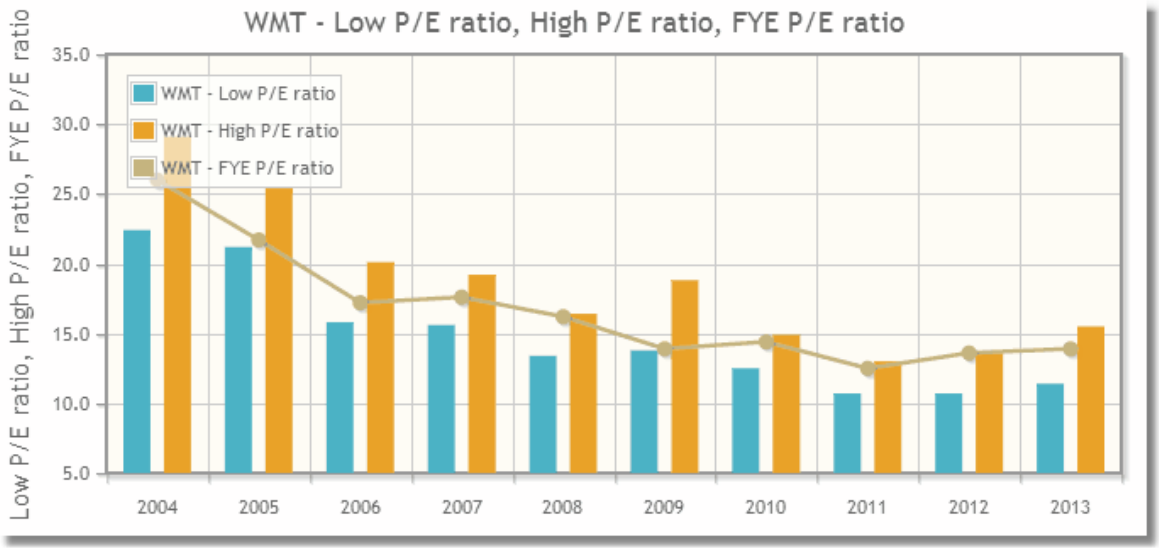
Example of Format Panel

3.4.2 Default Historical Charts

To get quickly to main features of companies there are a collection of default charts. They are accessed by the Links at the top of the Chart Panel.

These six charts combine key attributes of companies into six charts. These charts are:

- Management: Return on Equity and Return on Capital
- Growth: Sales per Share and Earnings per Share
- Debt: Debt to Equity Ratio and Interest Cover
- Liquidity: Current Ratio and Quick Ratio
- Payout: Payout Ratio
- P/E Ratio: Low P/E Ratio, High P/E Ratio and Average P/E Ratio



Default P/E Ratio Chart for Wal-Mart

The final combined chart is Price:

- Price: Low Price, High Price and Average Price

3.4.3 Company Historical Charts

The links in the Chart panel in the section called Chart settings allows you to build charts that combine different companies and different measures or attributes.

A basic historical chart consists of a company (such as Cochlear) and an attribute (such as Earnings per Chart). Chart 1 is an example of a basic chart. The company is the Commonwealth Bank of Australia (CBA). It is selected by choosing the company at the top of the page. Then click on "+ Add measure":

Button to Add Further Measures

This will give a list of available measures: Current Ratio, Debt to Equity ratio, and so on.

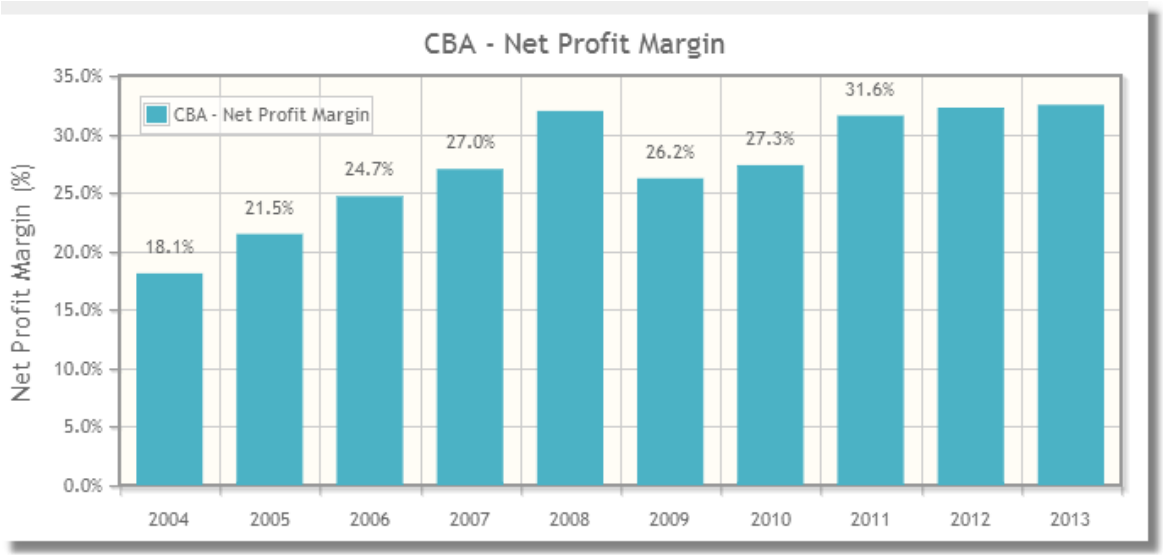


Chart 1: Net Profit Margin for CBA

The basic measures that can be displayed for the companies are: Current Ratio, Debt to Equity ratio, Debt to Market Cap ratio, Earnings, Earnings per Share, FYE (financial year end) P/E Ratio, High P/E Ratio, High Price, Interest Coverage, Low P/E Ratio, Low Price, Net Profit Margin, Payout Ratio, Price, Price/Earnings Ratio, Quick Ratio, ROC, ROE, Sales, Sales, Sales per Share, and Shares Outstanding.

More details of these financial terms and ratios can be found in the Glossary. Data points such as High Price are calculated as the high price for each financial year.

If you want to run through the charts for the measures for a company one after another, click Replace measure. This will remove all the measures for the current chart and all the companies except the default company. It will also provide a drop down box to choose a new measure or attribute.

Several basic charts for different companies can be combined in a single display. This is done using the link "+ Add company/measure".

For example, Chart 2 below shows the same attribute (Return on Equity) for multiple companies (the four major Australian banks: ANZ, CBA, NAB and WBC). The collection of charts are displayed in line format.

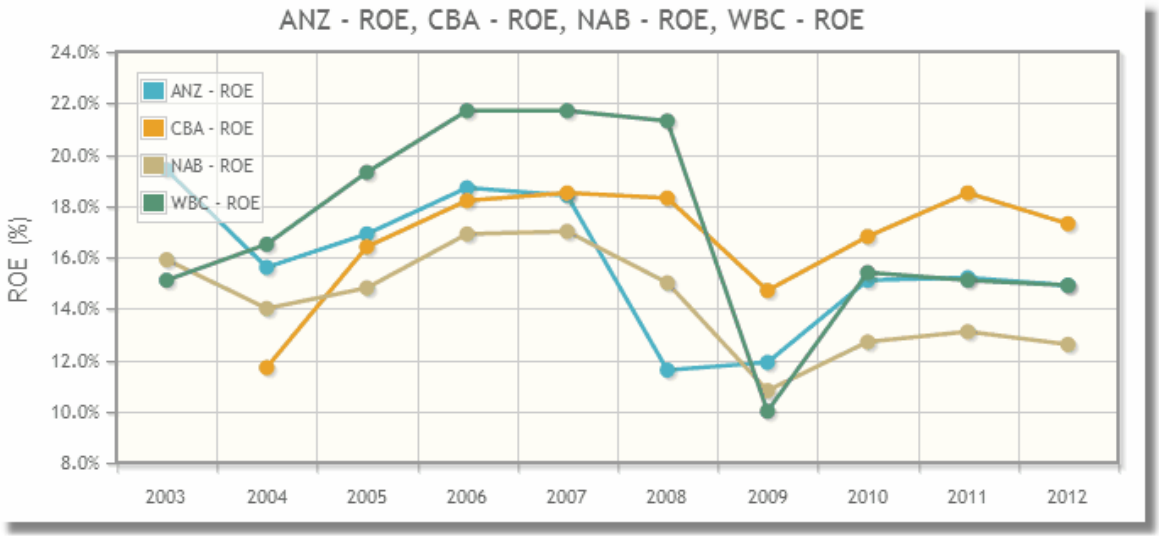


Chart 2: Return on Equity for the Four Major Australian Banks

In contrast, Chart 3 shows different attributes (Earnings per share and Sales per Share) for the same company (Cochlear). The collection of charts are shown in the default column format.

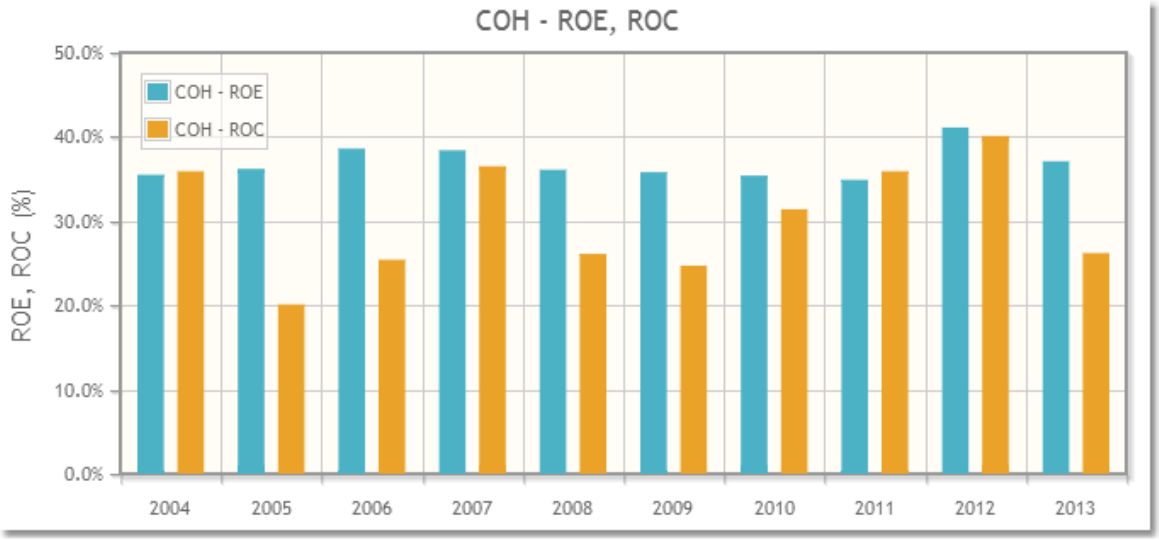


Chart 3: Earnings per Share and Sales per Share for Cochlear

EPS Charts: When EPS data is displayed in a chart on it own, EPSttm is automatically added as an extra data point. If no interim data has been released, EPSttm will have the same value as the EPS for the previous year. Otherwise, depending on the most recent data, EPSttm will differ from the EPS for the previous year. In both cases, the column for EPSttm is shown in a different colour. (See Chart 4 below.) If an extra data series is added, the data point for EPSttm is removed.

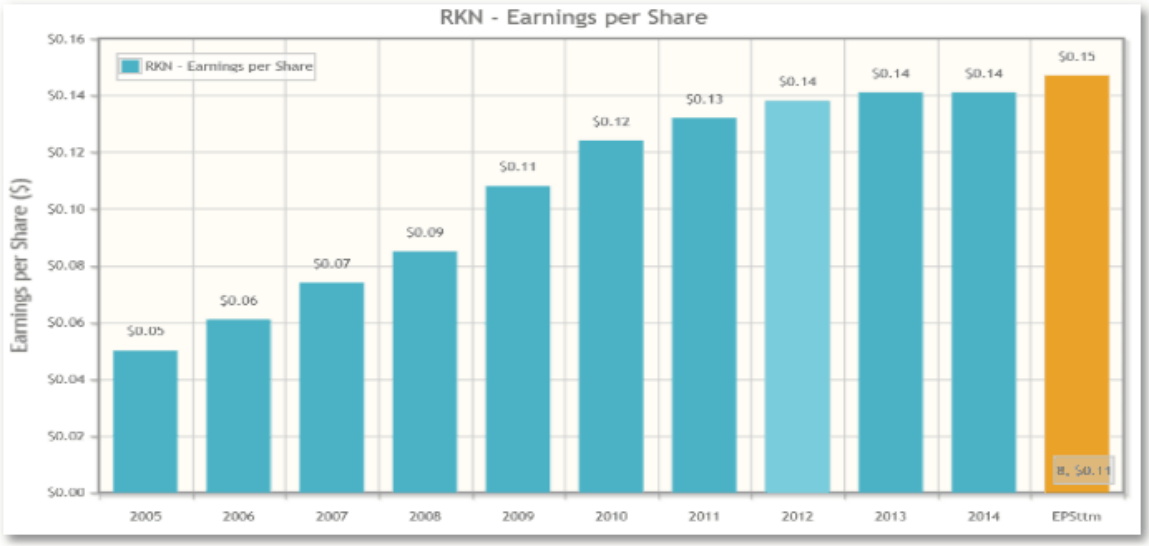


Chart 4: Earnings per Share Chart with the extra column showing EPSttm (labels are turned on)

3.5 Data

The Data page has two types of data: Current Price Data and Historical Data.

The Current Price data consists of the fields:

- **Last trade date:** the date of the latest closing price
- **Latest close price:** closing price on the previous trading day
- **Latest daily volume:** total trading volume over the last trading day
- **Latest updated date:** the date of the last change for the historical data
- **52 week high price:** the highest price the stock traded at over the previous 52 weeks
- **52 week low price:** the lowest price the stock traded at over the previous 52 weeks
- **EPSttm:** earnings per share over the trailing 12 month; for countries such as the US where companies report quarterly, EPStm will be the sum of the EPS over the previous four quarters; for countries such as Australia where they report biannually, this will be the sum overt the previous two six month periods.

The historical data consists of the fields:

- **Date of latest update:** the date of the last change for the historical data
- **Annual Report Month**: the month that the company makes its official annual report: for the US this is usually December, for Australia it is usually June.
- **Annual Report Year:** the year of the data
- **Debt to Equity:** debt to equity ratio at the end of the financial year
- **Debt to Market Cap**: debt to market cap at the end of the financial year
- **Quick Ratio:** quick ratio at the end of the financial year
- **Current Ratio:** current ratio at the end of the financial year
- **Interest Coverage:** interest coverage at the end of the financial year
- **P/E at Fiscal Yr Close:** P/E ratio at the end of the financial year
- **Return on Equity:** return on equity at the end of the financial year

- **Return on Capital:** return on capital at the end of the financial year
- **Earnings per Share:** earnings per share for the financial year
- **Payout Ratio:** dividend payout ratio for the financial year
- **Net Income:** net income or earnings for the financial year
- **Sales:** total sales or revenue for the financial year
- **Shares Outstanding:** number of ordinary shares outstanding at the end of the financial year
- **Fiscal Yr High Price:** the highest price the stock traded over the financial year
- **Fiscal Yr Low Price:** the lowest price the stock traded over the financial year
- **Fiscal Yr High P/E Ratio:** the highest P/E ratio over the financial year
- **Fiscal Yr High P/E Ratio:** the lowest P/E ratio over the financial year

Data Symbols NA and NC

In some cases, symbols such as NA, NC, NE and NM are displayed in the data fields in various parts of Conscious Investor.

NA: signifies that the data is not available. For example, the current ratio and quick ratio is not available for banks and will be displayed as NA.
NC: signifies that the no calculation is possible for this data field. For example, if EPS is negative, then the P/E ratio will be displayed as NC.
NE: signifies that earnings are negative.
NM: signifies that the results are not meaningful.

Why Do Different Websites and Data Suppliers Sometimes Show Different Figures for EPS?

First, a few technicalities and acronyms. Each country has its own accounting principles that public companies must adhere to before their auditor will approve their financial statements. These are generally referred to as Generally Accepted Accounting Principles or GAAP. In the US, the main organisation for setting GAAP are the Financial Accounting Standards Board and the Accounting Principles Board. In Australia GAAP is determined by the Australian Accounting Standards Board (AASB). In general most countries state that they are moving towards the standards described in the International Financial Reporting Standards (IFRS).

The outcome is that, even though somewhere in each (audited) report, the official GAAP earnings per share is quoted, the company itself may state a different figure or the data supplier may quote a different figure. These adjusted numbers are often referred to as normalised or underlying earnings. Here is what I wrote in The Conscious Investor:

> On some financial web sites you might see a reference to normalized earnings or normalized income. These are the net income of a company, adjusted for nonrecurring or unusual items. They are an attempt to provide information that is more representative of the performance of the company rather than include items that are likely to be one-off. One difficulty is that since they are not GAAP quantities, there may be differences between different providers of the data due to different protocols for extracting them from the financial statements. Another less common use of the term normalized earnings refers to the earnings that have been smoothed to allow for the effect of economic cycles. (Page 96)

Company quotes a different EPS

When a company quotes a different EPS it generally, but not always, to make itself look better.

3.6 Watch List

The Watch List is the area where you can "watch" price and P/E movements of stocks that interest you and be alerted when they meet thresholds that you set. You can even choose to be alerted when new company data has been released.

The alerts are set using the fields on the left hand side of the page. The Watches that you set can be viewed on the right hand side along with any alerts that have been triggered.

Once you choose a company, there are five possible alerts. You can receive an alert when:

1. there has been a change in the historical data of the company
2. the share price exceeds a specified price
3. the share price falls below a specified price
4. the P/E ratio exceeds a specified level
5. the P/E ratio falls below a specified level

Note that the watches can be set as multiple thresholds. For example, you might want to be alerted when the price drops below a specified level or the P/E ratio drops below a specified level.

On the right hand side the Watch List is in two parts:

1. Watches: this a list of watches that you have set but which have not yet been triggered.
2. Triggered: this is a list of those watches that have already been triggered.

When companies are added to the Watch List they are automatically displayed in alphabetical order based on their symbol. Companies in the Triggered list can be ranked according to the date they were triggered and on their alphabetical order based on their symbol. This is done by clicking in the column headings **Date** and **Symbol**.

The Watch List and Triggered List are automatically displayed when you first open Conscious Investor and view the Home page. For more details, including setting multiple thresholds, see the section Home Page Watch List.

Chapter 4

Return: Stage 3 of Conscious Investor

4 Return: Stage 3 of Conscious Investor

Stage 3 is where all the previous activity comes together in Conscious Investor. It is where you can calculate the expected return of any investment based on expectations of the growth of the company, market opinion and board dividend policy. The third step is carried out using the Return page or Scenario Analysis obtained from the Main Menu bar.

Other names for the Return page are the Scenario Analysis or What If Analysis. It allows the expected return to be calculated under different scenarios. The default scenario is based on historical data. However, most importantly, you can also carry out these calculations under an automatic margin of safety or your own inputs.

The screen also allows an analysis of HGROWTH, STAEGR, Net Profit margin, P/E Ratio (High and Low), Price (High and Low), Payout Ratio, STRET/STRETD and TARG/TARGD for a stock. At the top of the screen is a drop down box which lets you select a company. This can be selected using company name or symbol. Once selected the data for that company will populate all of the fields in the screen using the default data and default calculations, automatic margins of safety, or user-defined data that you may have entered previously.

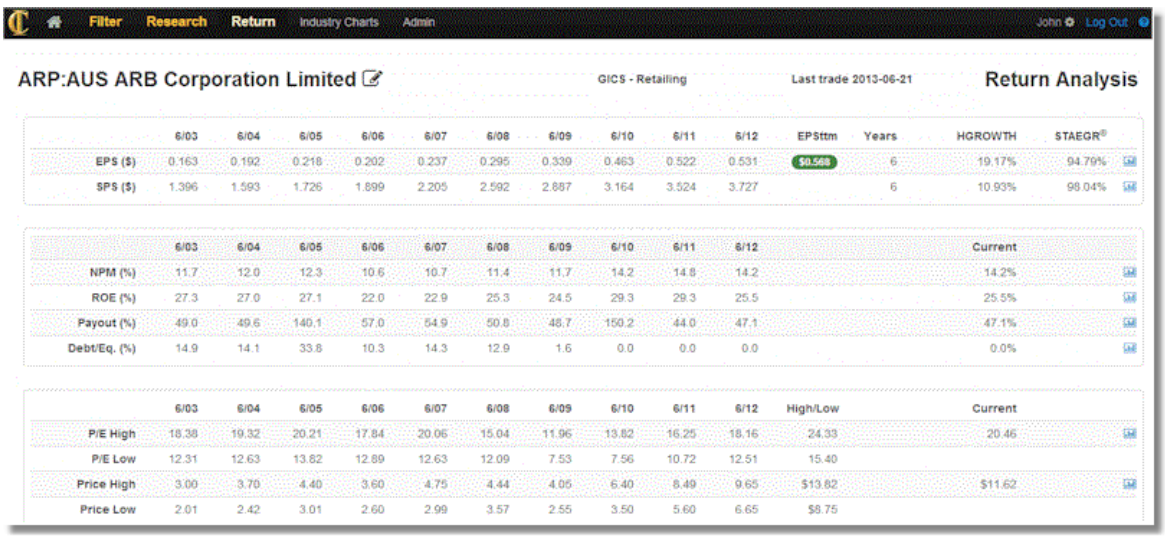
The Return or Scenario Screen is in two parts:

- Historical Data: Shows up to 10 years of historical data for the selected company.
- Return and Target Calculations: Estimates the likely return under different scenarios and margins of safety using STRET and STRETD. It also calculates the target price for the maximum price to pay to obtain your desired return under different scenarios and margins of safety using TARG and TARGD.

We describe these parts in the next two sections.

4.1 Historical Data

After choosing the company, the Historical Data section of the Return page shows up to 10 years of historical data for the selected company.



Company Data in the Scenario of What If Analysis Screen

Earnings Per Share (EPS): The first row shows Earnings per Share for each financial year. For example, 6/12 means the financial year ending June (month 6) in the year 2012.

EPSttm: This is followed by EPSttm which means earnings per share for the trailing 12 months. In the case of the U.S. and Canada which report quarterly this is the sum of the earnings per share for the four most recent quarters. Australia reports six-monthly so EPSttm is the sum of the earnings per share for the two most recent semi-annual company reports.If EPSttm is greater than equal to all the earlier EPS levels, it is shown in green. Otherwise it is shown in red. See the section Triple Green Stocks for more details about the significance of the colors.

Sales Per Share (SPS): The second row shows Sales per Share for each financial year.

For both rows the rate of growth HGROWTH and stability of growth STAEGR is calculated over the number of years displayed under the heading Years.

- **HGROWTH** - Measures the average annual percentage growth in either sales other that time period
- **STAEGR** - Measures the stability of the growth in either sales other that time period

Data can be changed: any of the data points for can be changed including the number of years. The HGROWTH and STAEGR will be automatically recalculated.

Net Profit Margin: The third row displays net profit margin or NPM which is the percentage of earnings per share divided by sales per share for each financial year.

Return on Equity (ROE): The fourth row displays the percentage return on equity for the company for each financial year.

Payout: The fifth row displays the percentage payout ratio for each financial year.

Debt/Eq: The sixth row displays the percentage debt over equity for each financial year.

The next four rows of data all concern price

Price Earnings Ratio (P/E Ratio): The next two rows display the high and low P/E ratios for each financial year. The two boxes under the word Current are the high and low P/E ratios over the 12 months up until the date of the last data download. In other words, it is the highest and lowest P/E ratio over the previous 12 months. It also displays the current P/E ratio.

Price: The next two rows display the high and low prices for each financial year. The two boxes under the word Current are the high and low prices over the 12 months up until the date of the last data download. In other words, it is the highest and lowest price over the previous 12 months. It also displays the current price.

Charts: To the right of the rows of data are small boxes with a chart icon...  Clicking on these boxes displays the company charts associated with the relevant row or rows.

4.2 Return and Target Price Calculations

The next section in the Return Page or Scenario Analysis contains the calculations of the expected return and the target prices. The calculations are carried out using the default settings, automatic margins of safety and your own settings. There are two input panels. The main input panel is for the input of Price, EPSttm, P/E Ratio, HGROWTH, Payout and Required Return.

Main Input Data Panel with Calculation of Return and Target Price
The entries for these calculations change when the company is changed.

The second input panel is for the input of the investment period, the tax rates on dividends and capital gains and the type of dividend strategy, reinvestment or fixed interest.

Input Panel for Extra Data
The entries in this panel do not change when the company is changed

4.2.1 Default Settings

The main entries for the default calculations are described in the next table. These entries change as the company is changed.

Price	Closing price
EPSttm	Earnings per Share Trailing Twelve Months
P/E Ratio	Price Earnings Ratio: The default is the average P/E ratio over the past 4 financial years with more emphasis given for recent years.
HGROWTH	Historical growth rate of earnings per share. The default is the average per year over the past 6 financial years.
Payout	Dividend Payout Ratio - Proportion of earnings paid as dividends. The default is the average payout ratio for the past 4 financial years with more emphasis given for recent years.
Req Return	The return you require to invest in the company
Investment Period	Period of investment to see your returns. The default is 5 years.
Tax rate on dividends	Tax rate on any dividends you receive as a percentage. The default is 0 percent.
Tax rate on capital gains	Tax rate on capital gains on sale of stock as a percentage. The default is 0 percent.
Dividend Investment Strategy	There are two choices: reinvest (which means dividends are reinvested) or fixed rate (which means that dividends are invested at a specified fixed rate).

Table 1: Description of the Fields for the Main Entries
These entries change as the company is changed.

The secondary entries are described in the next table. This entries are valid for the default and safety calculations.

Investment period (years)	The number of years used in the calculations. The default is 5 years.
Dividend tax rate %	The tax rate assumed to be paid on dividends. The default is 0 meaning that the calculations are carried out before tax on dividends.
Capital gains tax rate %	The tax rate assumed to be paid on capital gains. The default is 0 meaning that the calculations are carried out before tax on capital gains.
Dividend reinvestment strategy	This give the option between assuming that dividends are being reinvested or invested elsewhere at a specified fixed rate of interest.

Table 2: Description of the Fields for the Secondary Entries
These entries do not change when the company is changed.

More Emphasis on Recent Years

This data is automatically completed when a new company is selected in the selection box at the top left corner of the page. The inputs for the P/E Ratio and the Payout Ratio assume that this will be the average levels over the period of the calculation.

The default investment period is five years. The reason that five years is used is that it is reasonable compromise between two opposing market trends. First, the time span is long enough

that the market has had time for the price to move beyond short term fluctuations and be a better reflection of the underlying "value" of the company. Second, it is short enough that it is still possible to make reasonable forecasts for the key parameters involved in the calculations which are growth, the P/E ratio and the payout ratio.

The length of the investment period can be changed using the panel at the bottom of the Return page.

The assumptions in the calculations of STRET/STRETD and TARG/TARGD is that the P/E ratio and the dividend payout ratio will remain at the input levels over the investment period. Similarly, the calculations assume that the growth will be at the input level.

Default P/E Ratio and Payout Ratio The default inputs for the P/E ratio and the dividend payout ratio are based on their values over the previous four financial years with more emphasis given for recent years. The reason that we do not simply use the most recent P/E ratio or payout ratio is that sometimes they can be one-off situations and not be a reasonable guide for the future. For example, there might be a special dividend that distorts the payout ratio. Or there might be a write down causing a temporary spike in the P/E ratio.

Four years was deemed to give sufficient data to smooth out any years when the data is "unusual" in some way. More emphasis is placed on recent data because, despite any unusual situations, this is the data that most likely the best indicator of the future.

Default Growth Rate The default input for the growth rate in the calculations is the growth rate over the past six years calculated using HGROWTH shown at the top of the Research page. HGROWTH calculates the average rate of growth while automatically giving more emphasis on recent years. For more details see the section Rate of Growth: HGROWTH.

Tax Rates

The default is to calculate STRET/STRETD and TARG/TARGD before the effect of taxes on dividends and capital gains. However, by changing the values in the panel at the bottom of the return page it is possible to perform the calculation allowing for specified tax rates.

Reinvestment or Fixed Rate

It is possible to choose between performing the calculations assuming that dividends are reinvested or that they invested elsewhere at a fixed rate.

Reinvestment: The first dividend investment strategy assumes that dividends are reinvested in the stock being considered during the period of the investment. This bases the calculations on the assumption that you will use the dividends (if any) to buy additional shares. Even though you might not do this in practice, it is a standard way of being able to compare investments in different companies if you assume that you will reinvest the dividends. (Many companies offer this is as an option when you invest in them automatically crediting extra shares in lieu of paying a cash dividend. It is usually referred to as a DRIP or Dividend Reinvestment Plan.)

The estimated return is displayed as STRETD. (Think of this as STock RETurn assuming Dividends are reinvested.) This is the total return per year provided that the assumptions about the growth and other input variables are satisfied.

Related to STRETD is TARGD. This is the minimum price to pay to get your required return assuming that dividends are reinvested in the stock being considered during the period of the investment.

Fixed Rate: The second dividend investment strategy assumes that dividends (if any) are invested

separately in a fixed interest investment (such as a bank deposit) at a specified interest rate.

The estimated return is displayed as STRET. (Think of this as STock RETurn.) This is the total return per year provided that the assumptions about the growth and other input variables are satisfied.

Related to STRET is TARG. This is the minimum price to pay to get your required return assuming that dividends are reinvested in the stock being considered during the period of the investment.

Further Details

For more details on STRET/STRETD see the section Stock Return: STRET and STRETD. For more details on TARG/TARGD see the section Target Price: TARG and TARGD. The Return page also uses the colours green, black and red as a guide whether a company is likely to be a Wealth Winner®. For more details see the section Triple Green Stocks.

4.2.2 Safety Settings

Automatic Margins of Safety

When calculating STRETD/STRET and TARGD/TARG, Conscious Investor also modifies the key input variables to include an automatic margin of safety. This is akin to stress testing the outputs for STRETD/STRET and TARGD/TARG to ensure that the return results meet your investment requirements using inputs that you are confident will be achieved.

The results are displayed in the second row of the calculation panel and is labeled Safety. The margin of safety applies to HGROWTH, the P/E ratio and the Payout ratio. The margins of safety are calculated using built-in functions called ESAFETY (for the earnings growth), PESAFETY (for the P/E ratio), and PRSAFETY (for the payout ratio).

User-defined Margins of Safety

In case you want to modify the inputs even further than the default inputs or automatic margin of safety inputs, it is easy to introduce your own inputs.
This can be done in two ways: direct and modified data.
1. Direct input: Simply type your own inputs directly into the cells in the row marked **My Assumptions** and then click the **Recalc** button. This will enter results into STRETD and TARGD or STRET and TARG.
2. Modified data: At the right hand end of the rows marked **Default**, **Safety** and **Saved** are buttons marked **Copy**. Clicking on the **Copy** button will transfer the data for the corresponding row into row marked **My Assumptions**. Now you can modify the data to meet your forecasts or requirements.

Saving Your Assumptions

At any time you can save the entries in the line called **My Assumptions**. Simply click the button at the right hand end called **Save**. This will transfer the data to the line called **Saved**. Any data in the line called **Saved** will be saved. This means that when you close Conscious Investor and open it again, if you select the same company in the return page, the data will be automatically entered in the **Saved** row. Furthermore, the results for STRETD and TARG in the **Saved** row will automatically be transferred to the Details page of the Research step and displayed as My TARGD and My STRETD.

Updating the current price: The Saved row displays the price that was current when the data was saved. If you want to update the price to the current price, click the logo consisting of two circular arrows at the left of the line.

Significance of Margins of Safety

For more details on the significance of margins of safety and the algorithms PESAFETY, ESAFETY and PRSAFETY used to calculate them see the section Margin of Safety. Also see the section Triple Green Stocks.

4.3 Appendix: Franking Credits

Australian has a dividend imputation system. This means that when investors receive dividends, they also receive a credit for the tax paid by companies on the corporate profits related to the dividends. (Even further, if an investor is in the pension phase for superannuation, he or she will receive a direct payment from the taxation office covering this credit.)

For example, suppose a company with a tax rate of 30% earns $100 before tax. Also suppose it pays $35 as a dividend. Since the tax rate is 30%, this is equivalent to 35 / 70% = $50 before tax. Hence, it wasn't for corporate taxes, the investor would have received an extra $15 (assuming that the dividends are fully franked).

Hence, under Australian law, the investor receives a dividend of $35 plus a franking credit of $15.

In this case the total assessable income or grossed up dividend is said to be $50.

These tax credits can be included in the STRETD/TARGD and STRET/TARG calculation in Conscious Investor® resulting in an increase in the result for STRETD and STRET. However, don't feel obliged to do so. Since one of the aims of Conscious Investor is to estimate returns under a strong margin of safety, you may not want to do this. Just treat the tax credits as a bonus. In this way it is like an extra margin of safety. But if you do want to include the effect, or just want to see how it is done, the following describes how to accomplish this by modifying the payout ratio.

Payout Ratio

The effect of the tax credits on the return calculations is done by modifying the dividend payout ratio. In the previous example, the payout ratio is 35 / 70 = 50%. But the grossed up payout ratio is 50 / 70 = 71.43%. We need a method of converting the original payout ratio to a new payout ratio that makes allowance for the franking credits.

Method 1: Use a formula Suppose p is the stated payout ratio and P is the payout ratio allowing for franking credit. Denote the ratio of P / p by m and call it the payout ratio multiplier. For those who want to make exact calculations, the formula is

$$m = 1 + t \times f / (1 - t),$$

where t is the corporate tax rate and f is the franking level. In the previous example, m = 1 + 30% x 1 / 70% = 1.43. Since the old payout ratio is 50%, this means that, as we saw, the new payout ratio is 50% x 1.43 = 71.43%.

Method 2: Use a table The following table contains the gross up multipliers for the payout ratios for a range of franking levels and corporate income tax rates. They range from 1.00 when the franking level is 0 percent to 1.43 when the franking level is 100 percent and the corporate income tax rate 30 percent. (This latter case corresponds to the previous example.)

Franking Level	Corporate Income Tax Rate					
	25%	26%	27%	28%	29%	30%
0%	1.00	1.00	1.00	1.00	1.00	1.00
10%	1.03	1.04	1.04	1.04	1.04	1.04
20%	1.07	1.07	1.07	1.08	1.08	1.09
30%	1.10	1.11	1.11	1.12	1.12	1.13
40%	1.13	1.14	1.15	1.16	1.16	1.17
50%	1.17	1.18	1.18	1.19	1.20	1.21
60%	1.20	1.21	1.22	1.23	1.25	1.26
70%	1.23	1.25	1.26	1.27	1.29	1.30
80%	1.27	1.28	1.30	1.31	1.33	1.34
90%	1.30	1.32	1.33	1.35	1.37	1.39
100%	1.33	1.35	1.37	1.39	1.41	1.43

Chapter 5

Special Features of Conscious Investor

5 Special Features of Conscious Investor

Conscious Investor contains many proprietary features that make it unique in the area of stock market screening tools. In this section we list some of these special features. They include:

- Three steps of Conscious Investor
- Automatic company analysis
- Margin of safety
- Rate of growth: HGROWTH
- Stability of growth: STAEGR
- Stock return: STRET and STRETD
- Target price: TARG and TARGD
- Triple green stocks
- Industry charts

5.1 Three Steps of Conscious Investor

There are three stages or steps in Conscious Investor® for successful investing: Filtering or Scanning, Researching or Reviewing, and Return calculations or Pricing. These steps provide a clear path from all the companies traded on various world exchanges to the decision process for identifying and investing in potential Wealth Winners®.

Step 1: Filter

The first step is the most objective stage dealing with 1000s of companies in the Australian, Canadian and US markets. Using large-scale broad calculations based on fundamental and price data, it filters these companies down to between one and five percent of the original number. These are companies that have displayed business excellence and performance with hallmarks of this continuing in the future. The filters operate by user-friendly sliders to change the requirement levels. Some of the areas include return on equity and capital, debt levels, growth stability and anticipated future performance. Filtering can be done based on historical settings, an automatic margin of safety or on user-defined margins of safety. The stage is carried out using the Filtering screen obtained from the Menu bar.

Step 2: Research

The second step is the transition stage between step one and step three. By ensuring that the companies arising from the filter process have stable and consistent business records, this step provides a bridge between the large-scale calculations of the first step with the detailed calculations of the third step. Of particular importance is the Analysis page and the Charts page within the Research step. You can also write and save reports on any companies that interest you. In Conscious Investor this step is carried out using the Research link obtained from the Menu bar.

Step 3: Return

The third and final step is the most subjective stage since it brings into the picture the intelligence and experience of the investor to make final investment decisions. Building on steps one and two, it involves detailed calculations for each company being examined. If looking to invest in a stock, the goal of this step is to determine if it is selling at a price that will give a satisfactory return based on the specific characteristics of the business and the requirements of the investor. If not, then it is important to calculate what would be the appropriate price to offer for it. If you already own the stock, then this step will help to make the decision whether to keep the stock or to sell it and buy something else. The calculations can be carried out using default historical settings, an automatic margin of safety, or your own settings. The automatic margins of safety or stress testing operate in the areas of: (1) growth of the business, (2) market recognition of the business, and (3) board policy regarding dividends. The third step is carried out using the Return page or Scenario Analysis obtained from the Main Menu bar.

5.2 Automatic Company Analysis

The Research stage has a page called Analysis. On this page two charts are displayed and automatically interpreted in terms of what they infer about the quality of the company and whether it should be followed up as a potential investment. A key feature of this interpretation is that it is expressed in plain English. In computer language, such systems are sometimes referred to as Wizards. The addition of this Wizard makes Conscious Investor fourth generation investment software.

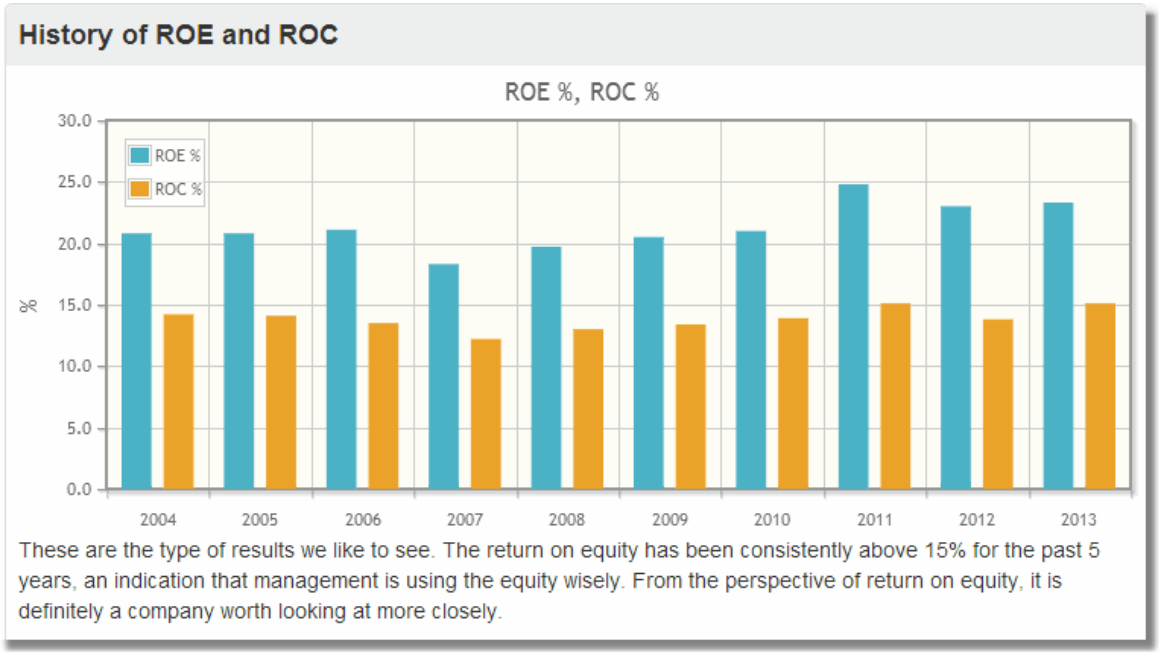
The Evolution of Investment Software

1st Generation: The first applications of computers to the stock market were to calculate standard well-known functions involved with the analysis and evaluation of equities. There was no associated database with the functions often working in a spreadsheet setting.
2nd Generation: This was the phase where databases involving fundamental and price data were integrated with calculation systems. This enabled the filtering or screening of thousands of stocks leading to an output of a small number of companies. The screening was done using various combinations of functions and measurements from the first level. Weighting to combine the measures into a single overall statistic for ranking purposes may be used.
3rd Generation: A thorough analysis of the functions in the first level showed their inadequacies and weaknesses. This third phase added completely new research-proven functions specifically designed to identify quality investments such as stability of growth and to introduce automatic safety settings for increased security.
4th Generation: Conscious Investor This starts with all the best features from the previous three levels including valuation methods that are theoretically sound and thoroughly back-tested. Then it integrates in a seamless way an expert system that

- describes and interprets key charts in plain English, and
- thoroughly analyzes whether it is best to buy, sell or do nothing under historical, safety and user-defined settings.

One user described it as "like having your own personal investment expert in your computer."

The following is an example of the chart "History of ROE and ROC" followed by its automatic description and interpretation.

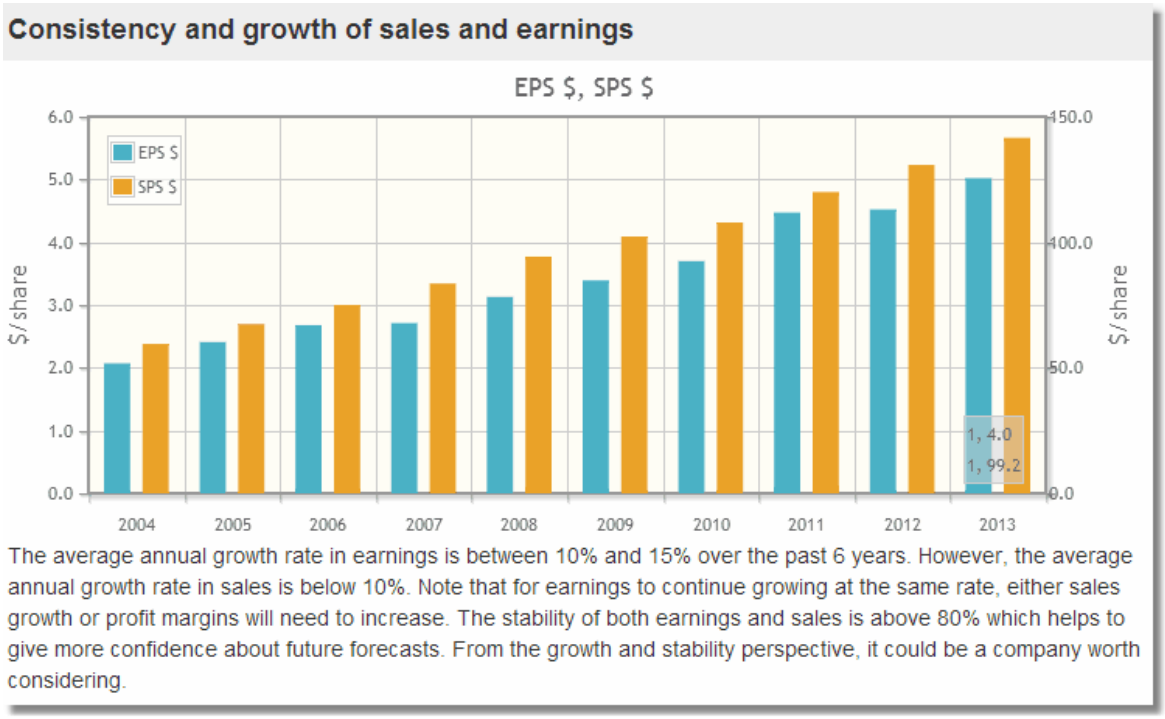


"History of ROE and ROC" Chart followed by its automatic description and interpretation

The reason that a chart showing the history of Return on Equity (ROE) is shown is that it is an important measure of the economic success of a business. Return on equity (ROE) is defined as the earnings of a company divided by its equity. The same applies to return on capital (ROC) if it is available. (Return on capital takes into account the debt of a company. It is defined as the earnings of a company plus interest paid divided by its capital.) To help evaluate the likelihood of a reasonable ROE in the future we look at historical levels as shown in this chart.

The narrative below the chart describes some of the main features of the historical levels of ROE. It also describes whether they are levels that indicate that this is a company worth considering from the perspective of ROE.

The following is an example of the chart "Consistency and growth of sales and earnings" followed by its automatic description and interpretation.



"Consistency and growth of sales and earnings" Chart followed by its automatic description and interpretation

Sales (or revenue) describes the money coming into a company from its usual activities. After paying for the cost of sales, operating expenses and taxes, the remainder is referred to as earnings. After dividing by the number of shares outstanding, we get sales per share and earnings per share. It is helpful to think of these as the sales and earnings generated on behalf of a shareholder for each unit of stock that is owned.

Current earnings per share and their anticipated future growth are the most important determining factors for the price of the stock of a company. Successful investments usually require their consistent and strong future growth. However, when looking at earnings growth, it is prudent also to look at sales growth since it is a foundation for earnings growth.

To help evaluate the likelihood of consistent and strong future growth of earnings we look at the historical levels of sales per share and earnings per share as shown in this chart.

The narrative below the chart goes a step further by describing results of calculations on this raw data regarding both its average growth per year and stability. It also provides a guide to whether or not they are at levels that indicate that the company is worth looking at more closely from the perspective of growth and stability.

5.3 Margin of Safety

In 1949 Benjamin Graham, the mentor of Warren Buffett, wrote a famous book called *The Intelligent Investor*. In it Graham wrote that the three most important words in investing are “margin of safety.” But up to now the idea of a margin of safety has been a vague idea with no clear steps to implement it. Extensive research and back testing at Conscious Investor has changed this. A carefully calculated margin of safety is an exciting addition to Conscious Investor. With the introduction of an automatic margin of safety, subscribers can have even more security and confidence in the search for great companies selling at profitable prices.

Although it is referred to under the general name of margin of safety, it is more akin to the idea of stress testing. When an architectural engineer gives approval for the construction of a new building, he or she must give assurances that, not only will the building meet the requirements of the new owner, it will also pass a range of safety requirements. Before a single shovel-full of dirt is removed for the foundations, the design has to be stress tested for everything from the ability of the floors to carry specified loads to the building being able to withstand extreme winds.

Stress testing in the share market is designed to do something similar. Before a purchase is made the investment needs to be stress tested in an objective systematic manner. In this way stress testing goes far beyond the general idea of asking that an investment has a margin of safety. Precise stress testing is the key to ensuring that a purchase meets the needs of a successful investment ranging from preservation of capital through to a healthy secure return.

There are three areas for stress testing any potential investment: (1) growth of the business, (2) market recognition of the business, and (3) board policy regarding dividends. In each of these areas I have developed computer models to apply stress tests which are built into Conscious Investor.

Stress testing or margin of safety is like analyzing the stock under a worst case scenario. This is particularly important at the current time.

Users of Conscious Investor know that it is easy to modify the input variables in the Price page and to incorporate a margin of safety. Now it is even easier since there is an automatic margin of safety. It is implemented every time a new company is selected in the Price page. The first row of the calculations uses the default data based on historical data, the second row introduces the automatic margin of safety for the forecast of the P/E ratio and the forecast of the growth rate of the earnings per share.

The implementation is a carefully constructed stress test. The potential investment is tested under extreme conditions. If after this test it is still has all the signs of an attractive investment, then we can more confident about making the purchase.

The goal is the same whether you use the automatic margin of safety built in to Conscious Investor or your own settings. It is to find investments that will give a satisfactory return even allowing for a downturn in performance of the business (as seen by the earnings not growing as fast as expected), a decrease in market perception or confidence (as seen by the P/E Ratio being lower than expected), or revision by the board of the level of dividends to be paid. In all cases it is now even easier to implement these “safety first” criteria into your investing decisions.

The actual calculations behind the Safety button are based on careful logic. They have also been tested and refined using thousands of examples. The resulting calculations are complex, but so that you have a general idea of what is involved in the calculations, below is a broad outline of the key steps. The calculations are in two parts: safety calculations for the P/E ratio and safety calculations for the forecast of earnings.

More details about margins of safety are contained in *The Conscious Investor*, particularly Chapter 13.

Safety P/E Ratio Forecasts

The safety level for the P/E ratio uses the current P/E ratio and the average of the P/E ratios over the previous four financial years.

The calculation starts by setting the safety P/E ratio equal to the current P/E ratio. If the average P/

E ratio over the past four years is lower than the current P/E ratio, then we want to allow for the case that the P/E ratio may only be at this level for a short period of time and could drop once again. The calculations lower the safety P/E ratio in a specified way using both the average P/E ratio and the current P/E ratio. In the opposite case where the average P/E ratio is higher than the current P/E ratio, no change is made to the safety P/E ratio.

Once this is done, a mean reversion is used in the downward direction as an extra margin of safety.

Note: Generally the MOS P/E ratio is lower than the default and current P/E ratio. However, in some cases the current P/E ratio far exceeds the default P/E ratio thus distorting the history of P/E ratios – in these cases the MOS P/E ratio may exceed the default P/E ratio.

The actual function used in the calculation is called PESAFETY and is pronounced "P E safety".

Safety Earnings Forecasts

As an investor, it is less important to make an accurate estimate of growth rate than it is to make an estimate about which we can be confident that the actual growth will equal or exceed it. In other words, we are looking for a worst case scenario or something close to it.

The safety level for the forecast for earnings per share is calculated using a function called ESAFETY and is pronounced "E safety". The input variables in this function include:

- the historical growth rate of earnings per share,
- the historical growth rate of sales per share,
- the stability of earnings per share,
- the recent growth rate in earnings per share including EPSttm, and
- the debt to equity ratio of the company.

It uses these inputs in an integrated way to make a conservative estimate of the future growth rate of earnings per share.

Regarding the five input variables, it is clear why historical growth rate of earnings per share is used since a simple future forecast is that it is the same as the past. The calculations start by setting the safety growth rate equal to the historical growth rate of earnings.

There are two options for the historical growth rate of sales per share; either it exceeds the growth rate of earnings per share or it does not. If sales per share growth is lower than earnings per share growth, then this can act as a restriction on earnings to continue growing at the same rate since for this to happen either the net profit margin would have to increase or the growth rate of sales would need to increase. In this case we use the growth rate of sales to lower the safety estimate of the growth rate of earnings.

In the opposite case where the growth rate of sales exceeds the growth rate of earnings we give less importance to the sales component.

Regarding the third input, namely the stability of the growth rate of earnings, the higher the stability, the more confidence we can have in the historical rate of growth acting as a forecast for future growth rates. To integrate this finding into the safety forecast, the lower the stability of the historical earnings, the lower we make the forecast. (The stability of earnings is measured by the proprietary tool STAEGR.)

For the fourth input, if there is a drop in the recent growth rate in earnings per share including EPSttm, then an even more conservative forecast of earnings growth is calculated in case this drop is the start of lower growth in the future.

The reason that debt to equity is included is because higher levels of debt generally adds risk to the continuing performance of the business. This is because the company is vulnerable to any requirements by the creditors to reduce the level of debt or increase the interest rate. It also makes it harder to raise capital to take advantage of any opportunities for particularly attractive acquisitions. When the debt to equity is below a threshold, then it has no impact on the forecast. When debt to equity grows above this threshold, the forecast of earnings per share using ESAFETY decreases

Finally, over and above the what was just described, we incorporate an overall margin of safety. This is in two parts: mean reversion in the downward direction and an absolute reduction.

Safety Payout Ratio Forecasts

The safety level for the forecasts for the payout ratio compares the current payout ratio and the average payout ratio over the past four financial years. If the current payout is lower, then it is used as the forecast of future payout ratios. If the current payout is higher, then this is taken as a sign that management could lower the payout ratio in the future from its current level. To incorporate this into the calculations a combination of current and the average past payout ratios is used as the forecast of future payout ratios. Adjustments are also made for special dividends which might otherwise distort the results.

Finally, high levels of debt can lead to the board lowering the dividend payout ratio. For this reason, if the debt to equity is above a threshold, then a more conservative forecast of the payout ratio is calculated.

Note: Generally the MOS payout ratio is lower than the default and current payout ratios. However, in some cases the current payout ratio far exceeds the default payout ratio thus distorting the history of payout ratios – in these cases the MOS payout ratio may exceed the default payout ratio.

The actual function used in the calculation is called PRSAFETY and is pronounced "P R safety".

5.4 Rate of Growth: HGROWTH

The function HGROWTH works in partnership with the function STAEGR. HGROWTH is the name of the function that calculates the average annualized growth rate of a sequence of data and STAEGR measures the stability of this growth. The data could be sales per share or earnings per share.

For example, the HGROWTH of the earnings per share figures
1.0, 1.1, 1.2, 1.4, 1.6
is 12.75 percent.

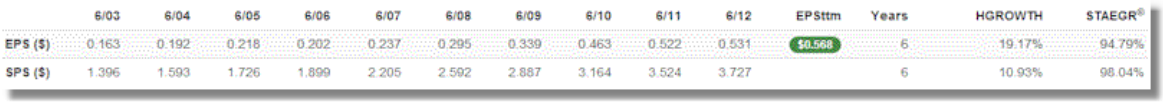
This means that on average the earnings per share are growing by 12.75 percent each year.

In contrast to the conventional method of calculating average growth rate, all the numbers in the sequence are included in the calculation. In the conventional method only the first and last numbers are used.

For example, if we replace the second number 1.1 in the sequence with 0.9 to get the sequence
1.0, 0.9, 1.2, 1.4, 1.6
then the HGROWTH becomes 15.26 percent. The higher figure is because the numbers are growing from a lower base. However, if we use the standard method for calculating growth there would be no difference between the growths for the two sequences.

You can remember the name by thinking Historical Growth.

The main place where you see HGROWTH is in the top two lines of the Return page



	6/03	6/04	6/05	6/06	6/07	6/08	6/09	6/10	6/11	6/12	EPSttm	Years	HGROWTH	STAEGR®
EPS ($)	0.163	0.192	0.218	0.202	0.237	0.295	0.339	0.463	0.522	0.531	$0.568	6	19.17%	94.79%
SPS ($)	1.396	1.593	1.726	1.899	2.205	2.592	2.887	3.164	3.524	3.727		6	10.93%	98.04%

Top Two Lines of the Scenario Analysis HGROWTH and STAEGR are shown for Earnings per Share and Sales per Share.

Benefits of HGROWTH

Starting with the fact that it uses all the data points, there a number of benefits of HGROWTH compared to the standard method of using only the first and last points.

1. All the data points are used.
2. More emphasis is given to more recent data.
3. Adjustments are made to allow the incorporation of negative data points.
4. Adjustments are made for extreme outliers and data points near 0. Without this, in both cases such points can overly influence the rate of return.

5.5 Stability of Growth: STAEGR

The function STAEGR® is arguably the most powerful analytical tool for assessing the potential of a company to continue its pattern of earnings growth into the future far exceeding the reliability of standard analyst forecasts.

Companies with high STAEGR have been proven to have more reliable future earnings growth. Extensive historical testing shows that when the earnings of companies have high STAEGR, past growth rates of earnings can be used as extremely reliable forecasts of future growth rates.

Primarily the function STAEGR measures the stability or consistency of the growth of historical earnings per share from year to year expressed as a percentage.

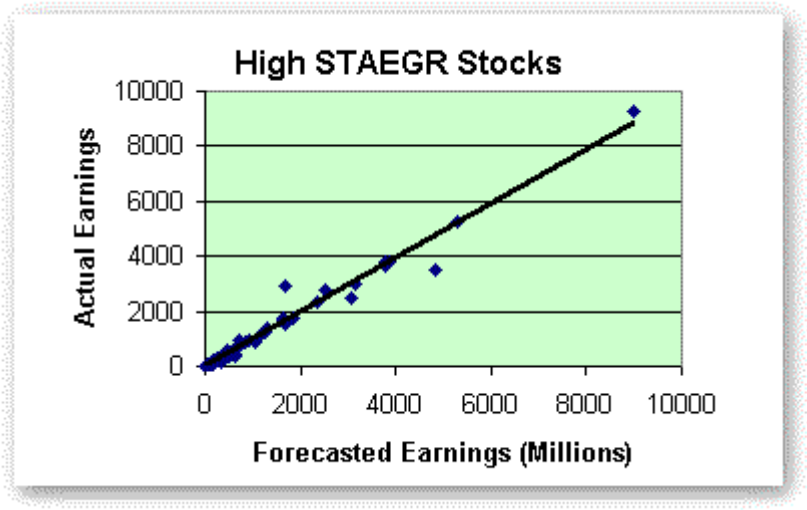
However the STAEGR function is much more versatile than this. It can be used to assess any sequence of financial data ranging from earnings per share to total revenue.

For investors and analysts, the function is fundamental in meaningfully assessing the strength, and therefore the attractiveness, of a business by measuring the stability of the growth of its earnings and sales.

Measuring stability through STAEGR is particularly important whenever there is extra turbulence of the markets. Focusing on companies with stable growth is vital for reducing investment risk and fear in the market place.

STAEGR measures the stability of the growth of historical data from year to year expressed as a percentage. It works as the partner to HGROWTH. HGROWTH measures the average annual rate of growth of a sequence of data and STAEGR measures the stability of this growth. The maximum figure of 100 percent for STAEGR represents earnings that go up and down by the same percentage each year. The calculations are based on fitting an exponential curve to the historical data with more emphasis on the stability of the growth of recent earnings. As for HGROWTH, special adjustments are made for recent data, negative earnings, for extreme outliers, and for earnings near zero.

For the technically minded, the forecasted earnings explained 85 percent of the variation of the actual earnings in the following group of companies. This can be seen in the following chart for U.S. companies. (Similar results were found for Australian companies.)



Comparison of Forecast and Actual Earnings For Companies with High STAEGR

The points represent the earnings figures, forecast and actual, of the companies in the group. The straight line is the best fit to the data. Its slope is almost exactly 1 and it passes through 0. Most of the points are either on the line or very close to it which means that actual earnings were very close to the forecasted earnings. The STAEGR of this group of 115 companies was 93% and up.

The main place where you see STAEGR is in the top two lines of the Return page.

Note: STAEGR is an automatic measure and cannot account for every situation. For example, a company might have very stable growth for the past four years but previous years might be very unstable. In this case, the STAEGR figure would be quite low even though, based on the past four years, the stability might make it an attractive company.

To ensure that a company is not ruled out because of situations such as just described, stability data for companies that pass the filters are shown in black and in orange.

Suppose a company is shown on the Selections Screen. If it has STAEGR for earnings per share above 85 percent, the entry in the STAEGR (Earnings) column will be shown in black. If it is above 60 percent, the entry will be shown in orange. The same applies to stability of sales with the column STAEGR (Sales).

Features and Benefits of STAEGR

1. The function STAEGR clarifies and formalizes the key attribute of stability for any series of financial data such as earnings or sales as well as performance ratios such as return on equity or return on capital.
2. STAEGR is comprehensive since it can measure the stability of financial data over any time period.
3. STAEGR is highly intuitive to use and the results easy to interpret since it provides a measure in the range 0 - 100 percent with high STAEGR corresponding to high stability and low STAEGR corresponding to low stability. A measure of 100 percent signifies complete stability.

4. The function STAEGR has high accuracy since it has the key property sought by analysts and investors of putting more emphasis on recent data and less emphasis on older data. This means that the final measure has more weight on the stability of recent data.
5. STAEGR results are reliable since the function has the important feature of adjusting for data that could overly distort the result such as one-off extreme data points, negative data and data near zero.
6. The calculation of STAEGR measures stability in a quantitative and consistent form so that it can be included with confidence as a screening parameter within any existing set of stock screening functions.
7. The calculation of STAEGR puts in reliable form something that investors and analysts have been estimating in a qualitative and ad hoc way through observing charts, namely the stability of financial data. This means that it naturally occupies a central role in the analysis of companies either on a one-by-one basis or as an inclusion in any set of company screening functions.
8. The function STAEGR is flexible and adaptable in that it can be used on its own or as part of any set of stock analysis functions or methods.
9. The function STAEGR works particularly well in partnership with HGROWTH which measures the growth rate of historical data by taking into account all the data and not just the endpoints as is customarily done.
10. The partnership between STAEGR and HGROWTH is that STAEGR measures the stability of the growth and HGROWTH measures the rate of this growth and so the two functions work together to quickly provide an effective and comprehensive understanding of any set of historical financial data.
11. The output of STAEGR is part of the input of another function called ESAFETY which provides an automatic conservative forecast of earnings based on a unique analysis of the historical earnings and historical sales. ESAFETY provides investors with a margin of safety when making earnings forecasts.

Further discussion on STAEGR is contained in Chapter 13 of *The Conscious Investor*. Also included is a discussion of the low level of accuracy of earnings forecasts provided by the analysts.

5.6 Stock Return: STRET and STRETD

The functions STRET and STRETD® are proprietary tools within Conscious Investor. They provide the answer to the most important question for every investor: "What returns can I expect on a stock purchase under reasonable assumptions?" You can even calculate the expected return under different margins of safety.

The output of STRET and STRETD is an estimate of the annualized percentage profit return or rate of return from owning the stock. For example, if the output was 10 percent, then it is expected that over the prescribed holding period the average total return would be 10 percent per annum.

It is calculated in a compounding manner. This means that the value of your holding would rise by 10 percent in the first year, and then by 10 percent of the new total value in the second year, and so on.

The difference between STRET and STRETD is that STRET assumes that the dividends are invested at a specified rate while STRETD assumes that the dividends are reinvested in the stock.

The calculation of STRET or STRETD proceeds in a number of steps. In broad terms, if you estimate the future P/E of a stock and its future EPS (via the growth rate), then you have an estimate of its price. Next you need to make adjustments for the proceeds that come from dividends either through investing them or reinvesting them in the stock itself.

Now you have an estimate of the total wealth from your investment at the specified time in the future. (Adjustments are also made to allow for tax on the capital gains and the dividends.) Finally,

you can calculate the average return that this represents based on the current price. Of course, the actual code to implement this is quite complicated. This is why we registered STRET/STRETD and TARGD as trademarks.

The functions STRET and STRETD represent a major breakthrough in evaluating stock profitability. They far surpass the traditional discount cash flow methods for determining value which are imprecise and impractical. (Problems with standard valuation methods are detailed in *The Conscious Investor*.)

The main place where you see STRET and STRETD in action is the screen at the bottom of the Return page.

STRETD Screen
The screen shows an example of a STRETD screen. The estimated average annual total return is 16.01% under the default assumptions and 9.75% under the automatic margin of safety.

When you select "Dividend reinvestment strategy: Fixed Rate" a slider appears in order to input a rate at which you will invest the dividends and the calculations switch from STRETD to STRET.

5.7 Target Price: TARG and TARGD

The functions TARG and TARGD® are proprietary tools within Conscious Investor and work in partnership with STRET and STRETD. The outputs of STRET and STRETD are an estimate of the annualized percentage profit return or rate of return from owning the stock. TARG and TARGD calculate what price you would need to pay to achieve a particular return. This puts you in a powerful position since you are less likely to be swayed by analysts' reports and media publicity. You can do as Buffett says: wait until you can buy the stock you want at the price that you are willing to pay.

The difference between TARG and TARGD is that TARG assumes that the dividends are invested at a specified rate while TARGD assumes that the dividends are reinvested in the stock.

The main place where you see TARG and TARGD in action is the screen at the bottom of the Return page.

When you select "Invest at the rate below" a slider appears in order to input a rate at which you will invest the dividends and the calculations switch from TARGD to TARG.

5.8 Triple Green Stocks

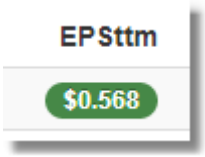
Triple Green Stocks

There are three places in the Return page or Scenario Analysis where are colors are used to give guidance whether a company is a Wealth Winner®. These colors are for the data EPSttm, Price in the STRET/STRETD panel which is calculated from the Fear-Greed Index, and the result of the TARG/TARGD calculations. If the color is green in those three areas the company is referred to as a *triple green stock*.

In summary, a stock is triple green if its EPSttm has grown, its current P/E ratio is at the lower end of its historical range, and its target price exceeds the current price.

5.8.1 EPSttm

Depending on the frequency that the companies are required to report, Earnings Per Share Trailing 12 Months (EPSttm) is the sum of the earnings per share over the four most recent quarters or the two most recent semi-annual reporting periods. In the Return Page it is shown in a green box or a red box. If EPSttm is greater than equal to all the earlier EPS levels, it is shown in green. Otherwise it is shown in red.



EPSttm shown in Green

It is quick way of checking that earnings per share is higher than all previous levels. In this case it would be in a green box. If it is red, it is a warning to look back of the annual EPS figures to see where it has been higher and by how much.

5.8.2 Market Fear-Greed Index

In 1987 Warren Buffett described two investor diseases: fear and greed:

> What we do know, however, is that occasional outbreaks of those two super-contagious diseases, fear and greed, will forever occur in the investment community. The timing of these epidemics will be unpredictable. And the market aberrations produced by them will be equally unpredictable, both as to duration and degree. Therefore, we never try to anticipate the arrival or departure of either disease. Our goal is more modest: we simply attempt to be fearful when others are greedy and to be greedy only when others are fearful.

Or again, in 2005:

> Investors should remember that excitement and expenses are their enemies. And if they insist on trying to time their participation in equities, they should try to be fearful when others are greedy and greedy only when others are fearful.

Buffett makes it clear what you should do to combat these diseases: be fearful when others are greedy and greedy when others are fearful. In other words, buy only when others are fearful.

How do we measure fear and greed for an individual stock? One way is by the level of the current P/E ratio compared to historical levels. For example, if the P/E ratio has been in the range 10 to 15 over the past four years and currently it is above 14, say, we could interpret that the market, meaning the majority of individual investors interested in this company, is being greedy. It appears

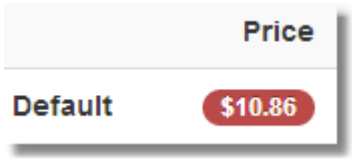
that they are paying inflated prices. Assuming you like everything else about the company, it would make sense to wait before buying because it is likely that the P/E ratio (in other words, the price assuming there is no change in earnings per share) will move to lower levels. At this time of greed, we need to be fearful about buying shares in this company.

Conversely, if the P/E ratio was below 11, say, the we could interpret that the market is being fearful. Assuming that you like the company as a business, this would likely be a sensible time to buy. At this time of fear, we could be greedy because it is more likely that the P/E ratio (in other words, the price assuming that there is no change in earnings per share) will move to higher levels.

Remember, Price = P/E Ratio × EPS. So that, assuming we have continued growth in EPS, the best investments are going to be those for which we also get an increase in the P/E Ratio. (Chapter 11 of *The Conscious Investor* has more details on this important formula.)

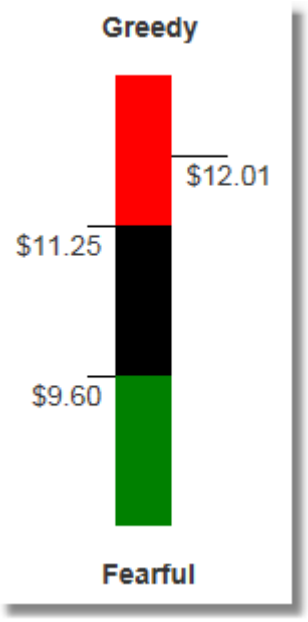
Market Fear-Greed Index

As a guide to when the market is fearful regarding a particular stock, when the current P/E ratio is at the lower end of its historical range over the past four years we mark the share price in the STRET/STRETD panel green. Conversely, as a guide to when the market is greedy regarding a particular stock, when the current P/E ratio is at the upper end of its historical range over the past four years we mark the share price in the STRET/STRETD panel in red.



Price Shown in Red

In the bottom right corner of the Price page there is a vertical column shaded red at the top, black in the middle and green at the bottom. This portrays the transition points for the Market Fear-Greed Index. Specifically it shows the transition points when the price would change from red to black and from black to green.



P/E Ratio Colour Transition Points

The current price is $10.86. In the red red section indicates that the current P/E ratio is high compared to its values for the past four years.

The actual proportion of green black and red in the column varies from company to company. It depends on history of the P/E ratios and the range and scale of the P/E ratio data.

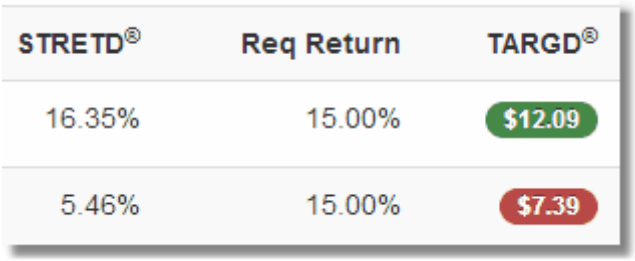
Note: As a technical point, the price is shown in red (resp. green) if the current P/E ratio is approximately in the top (resp. bottom) quartile of its range over the past four years. Otherwise it is shown in black.

Warning: This is only a general guide when the current P/E ratio is at the upper or lower ends of its historical range. It should only be used as a part of a full analysis to make any buy, sell or hold decisions.

5.8.3 TARG/TARGD Levels

The target price displayed in green when it is equal to or higher than the current price. This indicates that it is safe to buy at the current price to get the required return assuming that the projections are met. Otherwise the calculation is displayed in red. In the image below, there are two calculations of STRETD, 16.35 percent and 5.46 percent. Since 16.35 percent exceeds the required return of 15.00 percent, the target price TARGD of $12.09 is shown in green. The conclusion is that it is possible to pay up to $12.09 to achieve the required return of 15.00 percent provided the assumptions of growth, etc are met. (It is not in the image, but the current price is $11.40.)

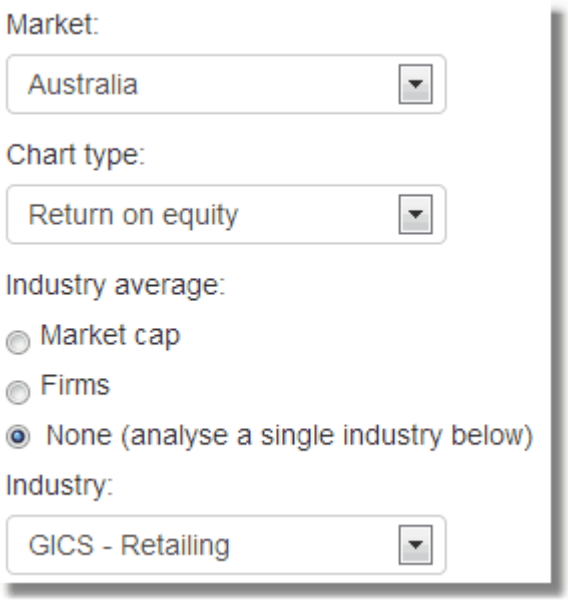
For the second calculation, STRETD is 5.46 percent which is less than the required return of 15.00 percent. Hence the target price TARGD of $7.39 is shown in red. The conclusion is that if a return of 15.00 percent is required, the maximum that should be paid is $7.39.



TARGD displayed in Green and Red

5.9 Industry Charts

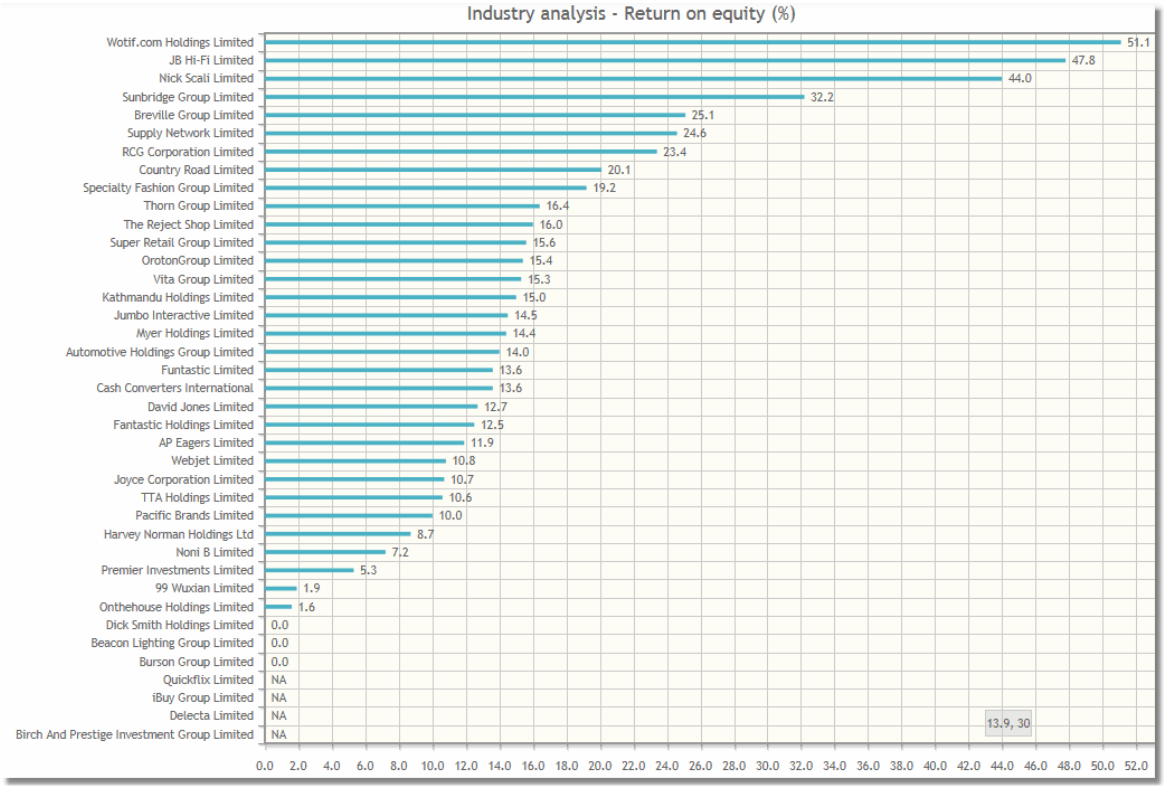
On the main toolbar there is a link called "Industry Charts". There are two types of industry charts: Single Industry and Market.



Industry Chart Panel
The selections shown are:
Market: Australia
Chart type: Return on equity
Industry: Retailing

Single Industry Charts

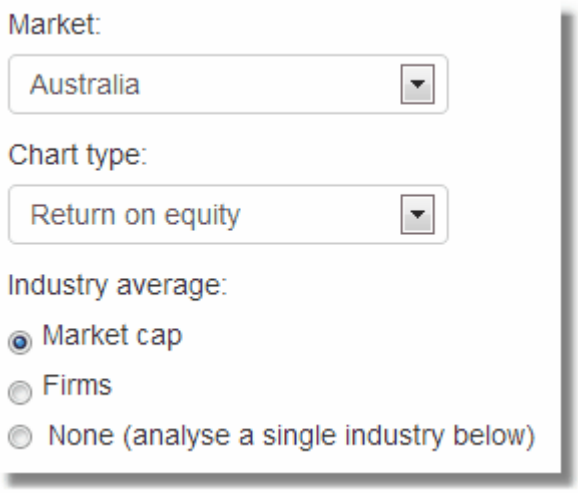
A single industry chart is a chart showing a financial measure for all the companies within a single industry within a market. For example, the selections in the preceding image allow the comparison of return on equity for all Australian companies in the retailing sector. The actual chart is shown below.



Return on Equity for all Companies in a Single Sector

Market Charts

Market charts allow the comparison of the average of different financial measures between different industries. For example, the selections in the following panel allow the comparison of the average return on equity for all industries here the average is weighted by market cap.



Industry Chart Panel
The selections shown are:
Market: Australia
Chart type: Return on equity
Average: Use market cap

The chart resulting from these selections is shown below:

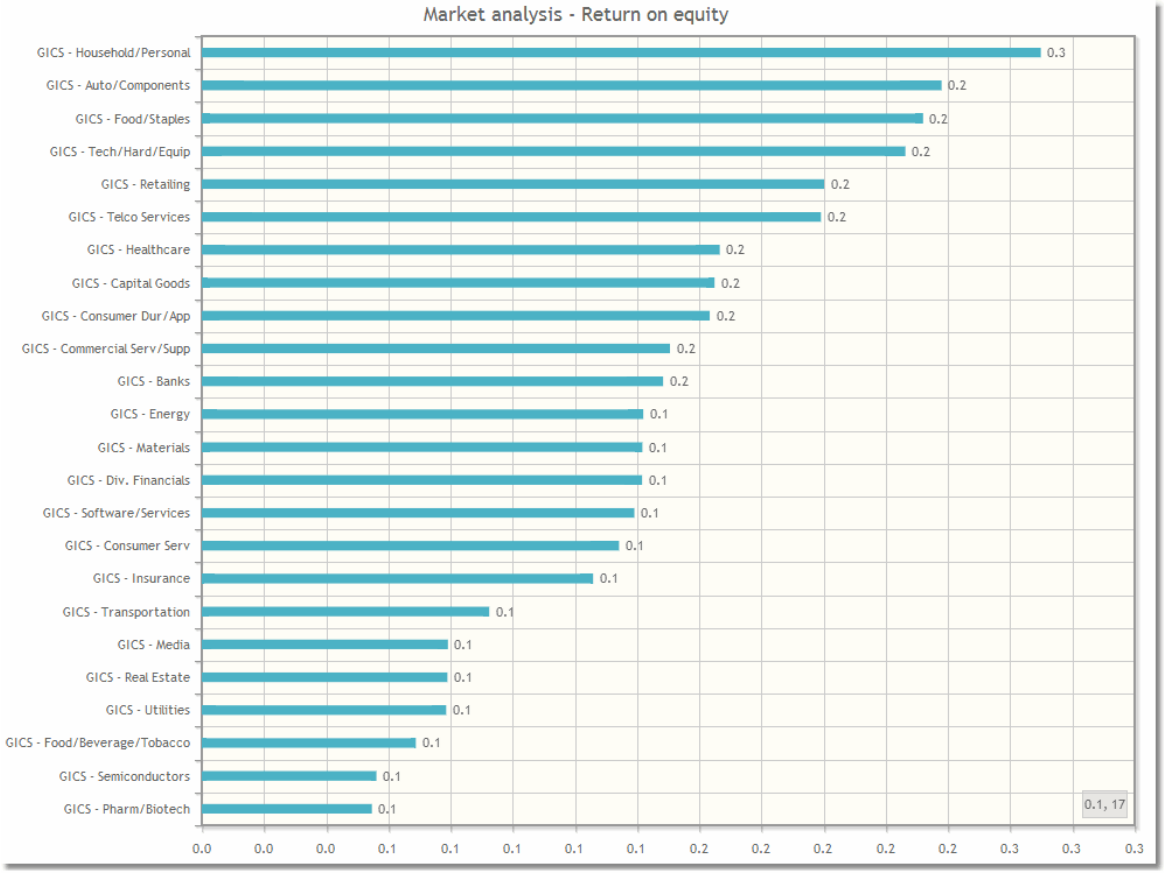
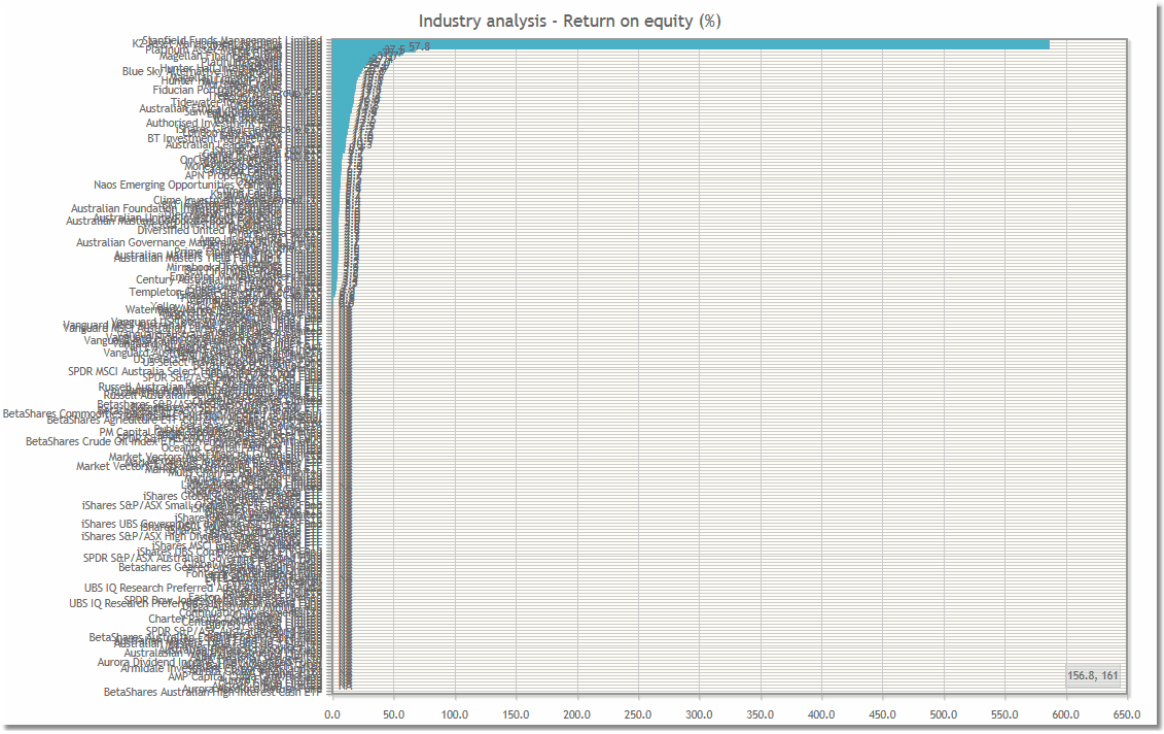


Chart Comparing Average Return on Equity for Different Industries

Zooming

In may cases there are too may companies in a sector to be able to distinguish clearly the results for individual companies for the single sector charts. Similarly, for some countries there are too many sectors to be to distinguish clearly the results for the individual sectors.



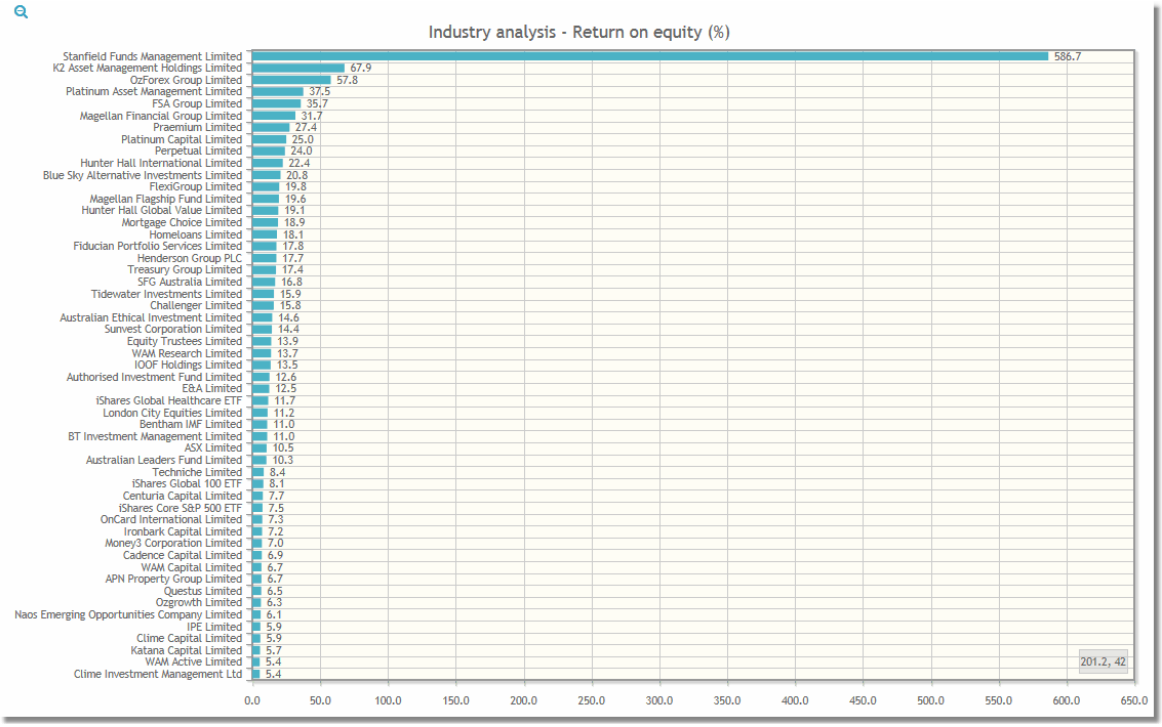
Example of a ROE Chart for Diversified Financials in the Australian Market

In these cases it is possible to zoom in to the chart. This is done by placing the cursor in the chart area in the centre of the area that interests you. The cursor will turn into a "+" sign.

Now left click. This will zoom or expand the chart centred on the cursor location. Repeating this action will continue the zooming process.

Once a chart has been zoomed once, a small icon will appear with a "-" in the centre. This is for "unzooming". Clicking this icon will undo the most recent zoom step. (See the previous chart.) Repeated clicking will return the chart to the original size.

The next chart shows the previous chart after two zooming steps. Notice the small "-" in the top right hand corner for reversing the zooms or unzooming.



Chapter 6

What is a Conscious Investor?

6 What is a Conscious Investor?

The name of the software is Conscious Investor®. There are a number of reasons for this. The biggest cost to investors is that they are not conscious of what they are doing, what I call unconscious investing, which means following the crowd and not asking the right questions. In the case of this software, I hope that through using it you will not just follow the crowd. Rather, you will learn that, despite all the hype and madness on the surface, underneath you are dealing with real businesses with real products and services, and that you can profitably invest in them using the well founded, proven methods of Conscious Investor. I hope you become a conscious investor and experience the stock market as a lot of fun, with the process of building wealth and financial security through finding Wealth Winners® a pleasure instead of a stressful duty or fearful necessity.

I also use the term conscious investor (which, by the way, was coined by my wife, Sandy) in another way: someone who invests in companies with products and services they believe in and perhaps even use. In this sense, another component to being a conscious investor is accepting the responsibility of recognizing that investing in companies also includes how the money is made, and not just the amount that is made. Investing in this way provides not just quantity, but also an additional layer of quality. It is like making a small nudge toward your own version of a better society and a more caring world.

This component of being a conscious investor relates to questioning your own values and the values of society. There are three aspects to this: thinking like an owner, products and services, and actions of management.

1. Are you thinking like an owner?

The first part of being a conscious investor is the recognition that shares are part of the process of providing capital for companies to allow them to build their businesses in a way that would not be possible by simply relying on their own funds or taking on debt. Doing this allows individual investors to think of themselves as part owners of these businesses and to share financially and emotionally in their success.(This is one of the reasons why so many people enjoy attending annual meetings of Berkshire Hathaway: to see the personal pleasure that Warren Buffett gets from the success of the companies he has chosen to invest in and his association with their management.

2. Products and services: what is their impact on society?

The second aspect relates to the actual products and services provided by each company. When we invest in a company, we want the revenue and earnings to increase. This means an increase in the actual sales and services provided by the company. Being mindful of the consequences of such an increase is part of being a conscious investor. For example, what would be the social and community consequences if the company increased sales of a particular product or service by 10 or 15 percent each year? What would be the effect on the wellbeing of society and the environment?

Again referring to Buffett, he remarked to the shareholders at the annual meeting in 1997 that he was offered the chance to buy a company that manufactures chewing tobacco. He and Charlie Munger, his vice chairman, knew that it was going to do very well and subsequently it has. They did not, however, go through with the purchase. As Buffett explained, “We sat in a hotel in Memphis in the lobby and talked about it and decided that we didn't want to do it.”

On the other hand, Buffett does own the Buffalo News which takes cigarette advertisements. Remarking on this, he said, “I just know that the one bothers me and the other doesn’t bother me. I’m sure other people would draw the line in a different way.” Munger added, “I think each company, each individual has to draw its own moral lines,” a comment which equates with being a conscious investor.

3. Is management honest, rational and acting in the best interests of shareholders and

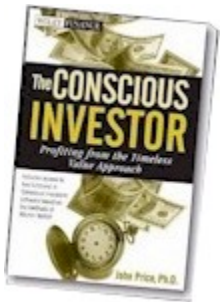
other stakeholders?

The third aspect relates to the way the company does business. In Teaminvest Masterclasses and SMaRTs (the facilitated process used by Teaminvest to analyse companies and their management) we always ask the vital question: is management honest, rational and acting in the best interests of shareholders? But being a conscious investor requires more. It means expecting management to act in an ethical manner towards all the stakeholders: employees, customers, suppliers, shareholders and everyone who comes in contact with the business.

These are personal questions with no definitive answers since individuals have different values. Yet addressing questions such as these ties together the two roles of conscious investing: the role of making money, gaining financial security and, in many cases, increasing the support of foundations and charities you believe in, and the role of providing capital and supporting those companies that you believe play a positive role in society with minimum harm to people, animals and the environment.

6.1 Book: The Conscious Investor

Another way to get the most out of your membership of Conscious Investor:



The stockmarket is an extraordinary outcome of human ingenuity. This is the opening sentence in *The Conscious Investor: Profiting from the Timeless Value Approach* by John Price. This book sets the framework for the methods in the Conscious Investor Cloud and helps explain why CI Cloud contains the steps, functions and processes that it does.

But much more than that, it gives a discussion of just what is meant by value and looks at over 20 different valuation methods. The result will be to help you get much more form your subscription to CI Cloud as well as make you a more savvy investor. Hopefully, also, it will make your investing more enjoyable and fun.

In a review on Amazon, Geoffrey Wells (Author, *Sustainability in Australian Business: Fundamental Principles and Practice*) wrote:

> John Price's excellent book is destined to become a classic, sitting alongside Benjamin Graham's The Intelligent Investor and Phillip A. Fisher's Common Stocks and Uncommon Profits. Like those great works, The Conscious Investor stands apart from the ubiquitous recipe books of investing which offer fragmented advice with no discernible intellectual foundation and doubtful practical value. In contrast, this book is well-founded, rigorous, and innovative; and, one might add, comprehensive, accessible and useful. It is a significant contribution to the literature of investment principles and practice.
>
> John Price's book is fascinating in many other ways. He touches on nearly all the main topics of the investment literature, expressing a firm view on them from the steady foundation of his analysis. He draws widely on the history and literature of business and finance, and on case-studies and anecdotes which illuminate the principles. His lucid, conversational style, and his obvious care for reader, make him a delightful as well as knowledgeable guide. Throughout the book, it is a privilege to be in his company.

Other reviews of the book include:

Only someone with Dr. Price's mathematical background could separate the story telling from fact when it comes to valuing a stock. His excellent book walks the reader through the different methods of calculating value and does the investing community a great service. This book should be on the desk of every investor.
—Charles Mizrahi, Editor, Hidden Values Alert & The Inevitable Wealth Portfolio; Author, Getting Started in Value Investing

Every once in a while someone takes the trouble to step back from the noise of investing to renew our perspective. In providing us with the tools to answer the question 'what is it really worth?' John Price has done just that. His advice is not only as timeless as the value-based approach he advocates, it's also refreshingly insightful.
—James O'Loughlin, CEO JOL Consulting; Author, *The Real Warren Buffett: Managing Capital, Leading People.*

John Price is appropriately named to write a book explaining the difference between Price and Value. So often investors confuse the two terms and unconsciously think that price is equal to value. Readers of this book will never make that mistake and only invest when an asset is trading at a price below its value. Participants in the stock market are like an iceberg, with 95 percent below water and unconsciously trading while 5 percent are above sea level and consciously investing. John Price's book will steer you to the rarefied air, keep you breathing easy and thinking clearly on top of the masses.
—Robert P. Miles, author, *The Warren Buffett CEO*, *Warren Buffett Wealth*, and *Warren Buffett's Berkshire Hathaway*.

The Conscious Investor is an extraordinarily comprehensive and intensive study of valuation methods. John Price lays out all the approaches to identifying mispriced stocks and systematically details their comparative strengths and weaknesses. The result is a book of exceptional practical value for serious investors.
—Martin Fridson, Global Credit Strategist, BNP Paribas Asset Management; author, *Unwarranted Intrusions: The Case Against Government Intervention in the Marketplace* and *Financial Statement Analysis: A Practitioner's Guide*, and other books

There may be more to being a savvy and rational investor than can be learned from this excellent book, but not much. John has made a large part of the wisdom of the world's greatest investors accessible to anyone.
—Steve Dalton, Director of Analytics, Tradition Group; Director, Eigensys Ltd.; Author, *Financial Applications Using Excel Add-in Development in C/C++*

Packed with useful tips to improve your stock market results.
—Hewitt Heiserman, author, *It's Earnings That Count*

You can purchase the book on Amazon and other book sites, or through your local book store.

6.2 Conscious Investor Fund

The Conscious Investor® Fund is a wholesale fund that focuses on finding long-term value through investing in quality companies — companies likely to give attractive but safe returns over the long-term. The companies may be Australian or overseas listed securities. It may also invest in unlisted securities. One of the Fund's distinctions is that it is both conservative and innovative.

Even though currently you may be managing all your own stock market investments, some of the

reasons for investing in the Fund include:

Peace of mind: Instead of having the anxiety and responsibility of all your funds with a single fund manager or you are managing it all yourself, consider diversifying some of your funds into a fund with the same Conscious Investor® and Teaminvest principles that you understand and trust.

Stepping down: Putting some of your money into the Fund is a prudent step towards preparing for the time when you no longer want to, or are able to, manage all your assets.

Fair dollar fees: Not just the usual "Assets Under Management" fee, but a simple fixed monthly fee so that fees as a percentage of your total investment decline as your investment rises above a certain limit. Plus the fund only makes money when you make money.

But perhaps the strongest reason and the one that makes the Fund exceptional is that is that it is actually a mini-Berkshire Hathaway. Just as for Berkshire Hathaway, the fund has the mandate to be able to invest in the best public companies wherever they may be, for example, Australia, the USA, Germany or the UK. Even better, the Fund has the mandate to be able to invest in carefully selected private companies which, as we know from Buffett, is often the place where you can find the best value.

Highlights

- Proprietary Conscious Investor® software rigorously scans the entire Australian and selected overseas share markets to find quality businesses with a proven track record of stable business growth, showing good prospects for this continuing.
- Teaminvest methodology classifies and weighs the risks of potential investments, and assesses their ongoing economic strengths.
- Systematic methods evaluate whether or not the board and senior management are acting honestly, rationally and in the best interests of shareholders.
- Scientific proprietary valuation methods calculate the price to pay, with a margin of safety, to secure an attractive return based on a full evaluation of the company.
- Fixed dollar fees mean that as your investment balance increases, your fees as a percentage of your total investment declines: there are also no management fees based
- on funds under management.
- A success fee for performance above an absolute return hurdle: our business is aligned with your success.

For further details, visit www.consciouscapital.com.au.

6.3 Teaminvest

Teaminvest was formed by Howard Coleman, Mark Moreland and Dr John Price. Their idea was simple: They would form a community of experienced and successful investors - people just like themselves. The group would meet regularly to discuss potential investments in a structured and collaborative environment. Teaminvest took its first members in 2009.

All the members are automatically subscribed to Conscious Investor®: it plays a core role in the evaluation and discussion of companies. Conscious Investor, by its very nature, focusses on the quantitative side of stock filtering, research and return analysis. This is then augmented by the collective experience, insight and knowledge of Teaminvest members which guides the decisions of individual members. Starting with around 2000 companies on the ASX, the aim is to find genuine Wealth Winners®.

Teaminvest has a four-step approach to no-nonsense investing:

- Screening - Using Conscious Investor® software, we run the 2000+ companies on the ASX through a 19-stage filter. Less than 100 currently pass the test for performance and stability. These are given to our members for study.
- Studying - Participating Members are grouped into teams called SMaRT panels and use their personal expertise, experience and networks to research and analyse an individual business in fine detail.
- Collaborating - At regular meetings throughout the year, the teams report their findings to the full membership. Members discuss the findings and add any intelligence they know.
- Deciding - Having taken in the collective findings and conclusions of the group, each individual Member decides what to do with his or her own money.

Membership is by invitation only. For further details, visit www.teaminvest.com.au.

6.4 Teaminvest Private

Teaminvest Private is the private equity arm of Teaminvest. Through Teaminvest Private, some of the companies that its members have equity stakes in include:

- Graham Lusty Trailers, the 'Rolls-Royce' of aluminium semi-trailer manufacturers.
- Whites Diesels Australia, a supplier of spare parts to the truck and bus market in eastern Australia from offices in Brisbane, Gold Coast, Townsville, Sydney and Melbourne.
- DecoGlaze Splashbacks, the premier supplier of glass splashback products in New South Wales.
- Found Beverages, a carbon neutral manufacturer and distributor of premium juices and sparkling infused waters.
- East Coast Traffic Control, a Queensland based provider of traffic control solutions to Government and the construction industry.
- The Outdoor Furniture Specialists, Australia's largest Australian retailer of outdoor furniture.
- Automation Group, one of Australia's leading experts in SCADA (Supervisory Control and Data Acquisition) and telemetry products for use in the water, energy and mining sectors.

Generally, through Teaminvest Private, members seek to invest in companies in the size of A$5m to A$50m (though we will consider other investments on a case by case basis). While we predominantly seek control of our investments (i.e. greater than 50% ownership), we are prepared to consider strategic stakes in businesses where a smaller investment is in the company's long term interest.

Investment Criteria

Unlike many private equity investors Teaminvest Private not limited to any specific industries or investment types and are prepared to consider investments in both listed and un-listed equity. Even though Teaminvest Private focuses on private companies, tools in and principles of Conscious Investor® form part of the analysis and due diligence of the companies. General criteria for companies to be considered for Teaminvest Private include:

- the company has a minimum of a four year operating history;
- earnings are growing and have a high degree of stability (STAEGR®);
- return on equity is greater than 10%;
- the company will have little or no debt post our participation (predominantly <50% debt to equity ratio); and
- management is in place and experienced.

Investment Types

Teaminvest Private is capable of providing growth capital, facilitating management buyouts (MBOs),

or providing a staged exit for business owners.

Teaminvest Private is particularly interested in providing capital to profitable businesses looking to take advantage of market conditions to grow in a responsible manner. We do not believe in loading companies up with debt, or changing management – Teaminvest Private seeks to invest alongside the business, rather than to redefine it.

Most importantly of all, Teaminvest Private operates on a BYOM basis – Bring Your Own Management. While Teaminvest Private is happy to help owners and management transition towards a staged exit, we are not interested in investing in businesses where the management is intent on exiting immediately.

For more details about how to become a member of Teaminvest Private and invest in companies through Teaminvest Private, see www.teaminvestprivate.com.au

6.5 People

John Price PhD
As the developer and prime mover of Conscious Investor, John started his career as a research mathematician with positions in major universities around the world. After publishing two books and over 60 papers in peer-reviewed journals in mathematics, physics, and finance, by chance he attended the annual meeting of Berkshire Hathaway in 1998. This was a turning point. First, John made Warren Buffett his research project reading everything that he could obtain written by Warren Buffett and about him. Second, he set himself the task of understanding the investment methods of other great investors such as Benjamin Graham, John Burr Williams and Peter Lynch.

He personally programmed, tested, and compared over 30 different stock valuation methods in his search for the best of the best. With this background, he wrote some investment software for his own use. But others heard about it and wanted copies. Eventually this led to John developing Conscious Investor.

Apart from the overall structure of the three steps, Filtering, Analysing and Pricing, John developed all the other tools within Conscious Investor. These include the proprietary functions STAEGR®, HGROWTH, STRET/STRETD and TARG/TARGD, the automatic margin of safety functions ESAFETY, PESAFETY and PRSAFETY, and the inclusion of the Wizard with the descriptions of key charts.

More details of the ideas behind Conscious Investor can be found in his book *The Conscious Investor: Profiting from the Timeless Value Approach* (Wiley, 2011).

Paul Shields
The original version of Conscious Investor was implemented and maintained by Paul. He is a co-founder and Director of Oyster Consulting, a management consulting company for resource industries. As well as building the original version in 2000, he implemented many new benefits and features over the next twelve years.

Scott Daley and James Gifford PhD
The current version of ConsciousInvestor Cloud was implemented and is maintained by Scott and James, the principles of Thought Patterns, a software engineering company in Canberra. They did an expert job of transforming the original version of Conscious Investor and making it available on a range of computers and tablets covering the spectrum from PC computers to Apple iPads . This meant diving deeply into the structure and algorithms of Conscious Investor and rewriting everything.

In order to make Conscious Investor available on the maximum number of computing devices, it

was decided that it needed to be cloud-based, using modern web technologies and best practice design patterns. This combination provides the system with agility to respond to future developments of Conscious Investor as well as web advances whilst reducing maintenance costs.

6.6 History

The original Conscious Investor was released in July 2001. The first test versions of ConsciousInvestor Cloud were distributed in February 2013 and beta versions were distributed in May 2013.

The key differences between Conscious Investor and ConsciousInvestor Cloud centre on the fact that, since the latter version is housed "on the cloud", it is possible to store individual reports and settings which are then available from almost any computer. These reports and settings are stored securely and can only be accessed by the individual subscriber.

A more technical benefit is that as we develop new features, remove bugs and refine the presentation, all members will automatically benefit from them as soon as they are released. There is no need to download new software.

Some of the specific differences between Conscious Investor and ConsciousInvestor Cloud are:

1. Operates on a full range of computers and operating systems including PCs, Macs, iPads and other tablets.
2. You can tag groups of companies such as the stocks in your portfolio and companies that you are watching. Then you can run these groups through the filter process in the same way that you did for industries.
3. You can combine sectors, tagged and individual companies within the filter stage.
4. The RAP summaries for Australian are now loaded into Conscious Investor. You can see them when you analyse a company in the Research stage.
5. Important Teaminvest news regarding companies can be displayed within Conscious Investor.
6. You can type personal reports on companies and recall them for later reference.
7. STRETD and TARGD (or STRET and TARG) are displayed together in the one line.
8. Default and margin of safety calculations for STRETD and TARGD (or STRET and TARG) are automatically displayed in the Return step.
9. You can add your own margin of safety and store it for later reference.
10. Default values for the P/E ratio and dividend payout ratio in the STRETD and TARGD (or STRET and TARG) calculations have been modified to give more emphasis on data in recent years.

Version and Selected Build History

Version 1.0

Build 7236 Released 1st August 2013

Build 7268 Released 19th August 2013
- Charts made higher with automatic resizing when the window size is changed
- Ability to step through charts with a single click
- Add radio buttons for choice between rollback and no rollback
- Correct problem when changing from rollback to no rollback

Build 7294 Released 27th August 2013
- Correct problem when all the markets for a subscriber have expired

Build 7326 4th September 2013
- All links from Company Summary on the Research | Details page set to Profile page of Yahoo Finance

Build 7341 10th September 2013
- Addition of ability to remove user-defined settings in the Filter section

Build 7360 19th September 2013
- Addition of ability to sort companies in Watch List by date and symbol
- Automatically rank companies in Triggered List by symbol
- Fixed bug when a company was added to Watch List for alert for new data

Builds 7487 - 7533 1st November 2013
- Correction of payout ratio labels
- Correction of disappearance of charts when company is changed
- Display P/E ratios with 2 decimal places in Filter results
- Solved problem of company changes with iPads

Build 7527 1st November 2013
- Calculations activated by pressing "Enter" in Return section

Build 7660 17th January 2014
- Fixed ability to add links in text in Summaries
- New section for Training Information on Home Page

Build 7806 11th March 2014
- Introduction of years of history slider on the stability tab
- Correction of an error in the My Assumption calculation when using dividend reinvestment
- Change TARGD to Target Price in My Saved Assumptions
- Change STRETD to Return in My Saved Assumptions

Build 7828 24th March 2014
- Corrected latest daily volume which was too high by factor of 100
- Change scale for earnings charts
- Corrected scale charts for P/E market charts
- Use two axes for EPS and SPS charts
- Changed title to Greedy and Fearful from P/E Analysis in Return Page
- Added discussion on Market Fear-Greed Index to manual

Build 8510 4th November 2014
- Added EPSttm in EPS charts
- Made a common "0" line in multiple charts with negative data
- Fix iPad menu bar when in full screen
- Workaround for Chrome bug on Android
- Added ability to count number of logins
- Ability for user to modify data
- Ability to load and crop photos

Version 1.1 Addition of extra markets

Build 8476 2nd December 2014
- Addition of a further 24 markets (total of 27 markets)

Build 8934 9th March 2015
- Text to replace Fear-Greed chart when data is poor

Version 1.2 Addition of extra debt series

Build 9547 24th September 2015
- Add different colour for EPSttm in EPS chart
- Add new chart series Debt to Market Cap
- Change debt to equity "orange" threshold from 60% to 75%
- Change Interest Cover Threshold from 2.0 to 5.0

7 Glossary

Definitions and terminology frequently vary between sources. From our point of view of looking for long-term value, if a company meets your criteria using one definition, but fails using another, it may be better to move on to another company.

amortization A systematic, gradual reduction of the value of intangible assets over a given period of time. It is also used to describe the periodic repayment of debt, particularly when it is long-term.

asset Something of value that is owned by or owed to the company.

balance sheet A financial statement containing the three basic elements of a company: assets, liabilities, and stockholders' (or shareholders') equity. These three elements must balance according to the formula: Equity = Assets – Liabilities.

basic earnings per share The earnings of a company (quarterly, semi-annually, or annually) divided by the number of shares outstanding, not taking into account options or warrants issued by the company.

beta A statistical measure of the riskiness of a stock in terms of the variability of a stock price with respect to the variability of the market as a whole. Using this measure of risk, assets with a beta exceeding 1.0 are riskier than average. Assets with a beta below 1.0 are considered safer than average. See capital asset pricing model.

book value This term usually refers to the stockholders' equity of a company on a per-share basis. This is an accounting measure of value and the actual value may be quite different. See also price-to-book ratio.

capital The sum of the equity and long-term debt of a company. It is sometimes referred to as invested capital or capital employed. Capital can also include current debt.

capital asset pricing model (CAPM) The CAPM is a general model describing the relationship between risk and return in equity markets. The simple definition of risk using beta, a statistical analysis of stock prices, is at variance with the goals of long-term investing.

capital spending Total outlay on plant and equipment. It does not include funds spent on acquisitions. It could be expressed on a per-share basis.

cash This is the most liquid of the assets of a company and appears as the first line in the current assets in a company's balance sheet. It consists of money on hand and on deposit in banks.

cash equivalents Security investments that can be readily converted to cash. Also referred to as marketable securities.

cash flow The net earnings of a company plus depreciation, depletion, and amortization, less preferred dividends (if any). It may be stated for the entire company or on a per-common-share basis.

cash from operations The net income of a company plus depreciation, depletion, and amortization. It may be stated for the entire company or on a per-common-share basis.

clean surplus relationship The assumption that the book value at the end of a period (generally a financial year) equals the book value at the start of the period plus the earnings less the dividends over the period.

cost of sales The cost of producing a company's inventory, such as the cost of raw materials, labor, and production overhead.

current assets Assets of a company that are cash, or are reasonably likely to be turned into cash within the next 12 months.

current liability A liability of a company that is due within the next 12 months.

current ratio The ratio of current assets to current liability.

debt ratio The ratio of total liabilities to total assets. Also called debt-to-assets ratio.

debt-to-equity ratio The ratio between the funds supplied by creditors, which is debt, and the funds supplied by investors, which is equity. In the event of bankruptcy, creditors must be paid before owners, so the debt-to-equity ratio is a measure of risk associated with the business.

Usually the debt-to-equity ratio includes the debt that is interest bearing.

Debt-to-market cap ratio The ratio of debt to market capitalisation of the company. Usually the debt-to-equity ratio includes the debt that is interest bearing.

depletion The equivalent of depreciation applied to the use of natural resources such as oil and gas, minerals, and forests.

depreciation The accounting procedure that allocates the cost of a fixed asset such as plant and equipment (land is not depreciated) over its estimated useful life. It is generally included in the cost of sales item in the income statement.

diluted earnings per share The earnings of a company (quarterly, semiannually, or annually) divided by the number of shares outstanding plus the number of unexercised options and warrants issued by the company. See basic earnings per share.

discontinued operations These are operations that have been or will be discontinued. They are reported separately from continuing operations in the income statement to improve the comparability of earnings from year to year.

discount rate The rate at which entries in the discount valuation are discounted to compensate for their level of risk or the cost

dividend A payment in the form of cash or stock by a company to its shareholders.

dividend payout rate See payout rate.

dividend yield The percentage formed by dividing the annual dividend by the market price of the stock.

DuPont analysis A decomposition of return on equity (ROE) into three components describing markup (net profit margin), turnover (total asset turnover), and debt (financial leverage multiplier).

earnings A term used interchangeably with income and profit; also often referred to as net earnings, net income, or net profit. It is all the revenue of a company (operating and nonoperating) less all the expenses (direct, indirect, taxes, etc). It may or may not include income from discontinued operations. For investment purposes it is usually stated as earnings per share.

earnings per share (EPS) The net earnings (after preferred dividends, if any) per share of common stock for a financial year or a particular quarter. Earnings per share can be quoted as basic or diluted.

earnings per share trailing twelve months (EPSttm) The sum of the quarterly earnings per share for the previous four quarters. In Australia, the sum of the two most recent semiannual earnings per share.

EBIT, EBITDA Acronyms standing for earnings before interest and taxes, and earnings before interest, taxes, depreciation, and amortization.

efficient markets A theory or hypothesis that the prices of assets accurately reflect the information in the market place.

equity The general term used to describe the theoretical value of the investment that the shareholders have in a company. Also referred to as net worth and **stockholders' equity** It is the difference between total assets and total liabilities. See also book value.

extraordinary item An entry in the income statement relating to transactions or events of a type that are outside the ordinary operations of the business, and are not of a recurring nature. Reporting them separately improves the comparability of earnings from year to year.

Financial Accounting Standards Board (FASB) The FASB is the primary organization for the development of generally accepted accounting principles.

financial leverage multiplier The ratio of total assets divided by total equity.

first in, first out (FIFO) A common method of valuing inventory as the cost of the goods purchased or produced earliest and still in inventory. In an inflationary environment it tends to maximize earnings since it understates current production costs. See LIFO.

fixed assets See property, plant and equipment.

Form 10-K Each public company in the United States is required to submit annually a 10-K form to

the Securities and Exchange Commission. Much of it is similar to the financial portion of the annual report sent to shareholders, but with more detail.

Form 10-Q This is the quarterly report that each public company is required to submit to the Securities and Exchange Commission.

free cash flow The net earnings of a company plus depreciation, depletion, and amortization, less the amount of capital expenditures. Other noncash charges also need to be added back. These could arise from deferred tax assets and deferred tax liabilities. Increments in working capital should be removed. Free cash flow may be stated for the entire company or on a per-common-share basis.

generally accepted accounting principles (GAAP) These are principles that have evolved and been developed over the years which are now agreed upon by the accounting profession in the United States.

goodwill Goodwill is an intangible asset that arises when the cost of acquisition of a company exceeds the equity value of the company.

HGROWTH HGROWTH is a companion function to STAEGR that measures the average annual growth rate of earnings using all the data points and not just the first and last point.

income See earnings.

income coverage See interest coverage.

intangible assets Assets in a balance sheet for nonphysical items such as patents, financing costs, and purchased goodwill. The value of these assets is reduced by amortization over a given period of time. Intangible assets are often by-products of acquisitions.

interest coverage Earnings from continuing operations before interest and taxes over a financial year (commonly called EBIT) divided by the interest expense over the same period. It measures how many times EBIT covers the interest expense. Some sources replace EBIT by net earnings before interest and after taxes. (When the debt is zero, there is no interest expense and so interest coverage cannot be calculated. However, to ensure reasonable scales for charts of interest cover and for consistency in stock scanning, Conscious Investor sets interest coverage equal to 10 when there is no interest expense.)

inventory A company's merchandise, raw materials, and finished and unfinished products which have not yet been sold.

last in, first out (LIFO) A common method of valuing inventory as the cost of the item most recently purchased or produced. In an inflationary environment it tends to minimize earnings since it overstates average production costs. See FIFO.

liability A debt or obligation of the company. See current liability and long-term liability.

long-term debt Borrowed funds that are due for payment after one year, usually over several years. It usually forms the main component of the long-term liabilities on the balance sheet.

net profit margin Net profit divided by net sales; a measure of the profit after allowing for taxes and expenses.

net sales This is the value from a company’s sales of goods and services. It is the gross funds from the sale of goods and services less such items as allowances, discounts, and returns. Sales and net sales are usually interchangeable.

net worth Same as equity. In some cases net worth is defined as the value of common equity plus the value of the preferred shares.

nonrecurring An expression used to describe earnings that are unusual or one-time events.

operating earnings A company’s net sales less the cost of sales and operating expenses. Depreciation may also be subtracted. In this case, operating earnings equals EBIT.

operating expenses See selling, general and administration (SG&A) expenses.

operating margin Operating earnings as a percentage of sales or revenues.

opportunity cost A measure of the sacrifice investors must make if they are to forgo the liquidity and relative safety of cash government securities in favor of common-stock investments.

owner earnings A term introduced by Warren Buffett, defined as the "reported earnings plus depreciation, depletion, amortization, and certain other noncash charges less the average amount of capitalized expenditures for plant and equipment that the business requires to fully maintain its long-term position and its unit volume." If the business requires additional working capital, the increment should also be subtracted. Apart from asking for the average amount of capitalized expenditures instead of the actual amount, this definition is the same as free cash flow.

payout ratio or dividend payout ratio The portion of the income of a company paid out as dividends rather than retained in the company.

preferred stock A security similar to stock except that it gives the owner a prior claim over stockholders with regard to dividend payments and distribution of assets should the company be liquidated. Preferred stock is normally entitled to specified dividend payments.

price-to-book ratio, P/B ratio The ratio of the market price of the stock and its book value.

price-to-earnings ratio, P/E ratio The ratio of the market price of the stock and its earnings per share. The earnings are generally stated for the previous year.

profit See earnings.

property, plant and equipment The collection of assets of a permanent nature required to operate the business. They are also referred to as fixed assets. Land, buildings, plant facilities, machinery equipment, furniture, and capital lease equipment are considered to be fixed assets.

quick ratio or quick test A ratio similar to the current ratio except that the numerator is restricted to the current assets that are cash or cash equivalents and trade receivables. As for the current ratio, the denominator is current liabilities. It is a more rigorous test of short-term liquidity than the current ratio since it eliminates inventory, usually the least liquid of the current assets.

retained earnings The earnings of a company that are not paid out as dividends but are retained within the company as working capital or to finance fixed investment and acquisitions. They are also referred to as undistributed earnings or profits, accumulated profits, or retained income.

return on _____ There are four major ratios used to describe the return of a company: earnings divided by assets, equity, capital, or sales. These would be referred to as return on assets, return on equity, and so on. There are another four ratios formed by replacing earnings by operating profit.

revenues Generally this term refers to the gross or total inflow of funds to the company, usually sales plus nonoperating income sources such as interest income.

sales See net sales.

selling, general and administration (SG&A) expenses A grouping of expenses in an income statement representing a company's operating expenses. They generally consist of salaries, advertising, sales commissions, marketing costs, office expenses, rents, insurance, travel, and entertainment.

STAEGR® A proprietary function that measures the stability of the growth of historical data from year to year expressed as a percentage.

shareholders' equity Same as stockholders' equity.

stockholders' equity The equity in a company. May also need to subtract value of preferred stock.

Tangible book value The equity in a less goodwill and intangible assets.

total asset turnover Net sales divided by total assets; a measure of the efficiency of a company in using its assets to generate sales or revenue.

total return The average annual return, capital gains plus dividends, that an investor would have received from holding an asset assuming that each dividend is reinvested in the asset at the time of its payment. The calculation is done before tax. Also called total shareholder return.

weighted average cost of capital (WACC) The average cost of the different components of financing a company, including debt, equity, and other securities used by it to fund its financial requirements. The costs are weighted according to the amounts required. It is used as the discount

rate in some versions of the discounted cash flow methods

working capital The capital required to run the daily affairs of the company, which is a measure of its liquidity. It is defined as the difference between a company's current assets and current liabilities.

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