

# Projected Average Return

Many are familiar with total return. It means that if we buy a stock at the present price and sell at the forecast high price in five years, total return will be our average annualized [compounded] return from a combination of price appreciation and yield [if any].

The forecast high price for five years hence is computed by multiplying the forecast high price-to-earnings ratio [PE] by the forecast earnings per share in that fifth year. If the forecast high PE is 20 and the forecast EPS is \$ 2.15, the forecast high price is:

$$20 * \$ 2.15 = \$ 43.00$$

A potential problem with total return is that assumes that we will always sell at the *highest* price in five years. History shows that not many are able to consistently do that. A more realistic approach is to use projected average return [PAR]. It assumes that you buy at the present price and sell at an *average* [not highest] price in five years.

PAR is computed by multiplying the forecast EPS by the forecast *average* [not high] PE ratio. This average PE is found by averaging the forecast high PE with the forecast low PE. If high PE is 20 and low PE is 10, then the average PE is 15. PAR is computed:

$$15 * \$ 2.15 = \$ 32.25$$

Certainly \$ 32.25 is a lower selling price than \$ 43.00, and intuitively, we know that a selling price of \$ 32.25 is much easier to reach than anything higher. PAR, therefore, is much more realistic to use. If the selling price actually turns out to be the estimated highest price, so much the better.

To further illustrate the different levels of return between total return and PAR, assume that in the above examples, the current purchase price is \$ 18.50. What would be the different returns between total return and PAR?

Total return: buying at \$18.50 and selling at \$43.00 in five years.

Your stock selection software or financial calculator will yield an answer of 18.4%

PAR: Buying at \$18.50 and selling at \$32.25. Your return is only 11.8%

Clearly, PAR results in a more realistic idea of what your return is likely to be.

Our advice? Shoot for PAR!

To find out how to configure Toolkit to display PAR,  
go to following page

The display for PAR, goes in Part 5 of the SSG [bottom-right corner on back of the SSG.] If PAR is missing, see directions below for ensuring that it will be displayed.

<b>OVER NEXT 5 YEARS</b>		Share Next 5 Years <u>1.71</u>		X Avg. % Payout	(367) <u>4.8</u>	=	<u>8.2</u>	=	<u>0.3</u> %
<b>AVERAGE ANNUAL RETURN OVER NEXT FIVE YEARS</b>		Potential (4E) <u>37.7</u>					Present Price \$ <u>24.620</u>		(5B)
5		7.5 %						<b>P.A.R.</b>	
-----		0.3 %						<b>Average Yield</b>	
Annual Return Over the Next 5 Years (5C)		7.8 %						<b>Annual Appreciation</b>	
								<b>% Compd Ann Rate of Ret</b>	
								0.4%	
								3.4%	
								3.7%	
								0.3%	
								7.3%	
								7.6%	



1. On the overhead toolbar, click on Options, then on Preferences.
2. Click on Stock Study.
3. Put bullet in space labeled "Display Projected Average Return on SSG Back"
4. Click on OK

