Projecting Growth from a Decline - Notes
RM Chapter Model Investment Club
October 18, 2023

Slide 2

This presentation is a demonstration of How To Do.. It is not a recommendation to Buy, Sell or Hold. You need to do your own studies. This is being recorded for future reference.

Slide 3

Sometimes we have a company in our portfolio, or we want to study a company that has negative earnings in the most recent year. We are not sure how to make judgements in these situations. So, I am sharing what I have learned.

My journey began, When I helped my sister review her portfolio, we came across TGT and I had to learn to make projections from a negative year.   Then, someone in another club asked me to take a look at AMZN. It was more challenging because there were multiple things going on. It took me several days and multiple times to figure out all the effects. Many investors may have TGT or AMZN in their portfolios.

Slide 4

TGT is the simplest as it was the more straightforward of the two companies.

Slide 5

This is the SSG is at the 2022 year-end before any adjustments. This presentation is meant to help go through the slides without hearing the presentation. At least that was my intent.

Also, Take note of the Sales before adjustments on the SSG. Ten-year Sales are 4.9%. We will use this mental note when projecting future sales on Slide 12.

Slide 6

This slide is a narrative to walk you through the steps. Start with Projections off the Trend Line. This will even out the ups and downs. Then. eliminate the outlier years. Outlier years that are outside the average or normal such as a negative year or rapid growth years followed by a slowdown.

Eliminating outlier years helps us project off of a positive number. Then use the EPS projection from the EPS Trend Line at end of the year to get a positive number. In the next slides we will demonstrate this process step by step.

Slide 7

I am going through the process, step by step, so you may follow what I am doing. By using slides of the steps, you may refer back later as a refresher when you do your own studies.

Step 1 - we need to project from a positive number: Start the Projection Start Point click on "Trend"

Slide 8

Step 2 - Click off the negative year and earlier years of rapid growth for a more recent growth history

Slide 9

Step 3 - Hover EPS at end of trend line.
Step 4 - jot down number. We will be using this number in several steps.

Slide 10

This a capture of all the steps in slides 7-9, giving you a quick look back at all the steps.

Slide 11

Sometimes, I have seen this Annual Data used but not always, so I am including it.

Next, we will want to update the Annual Data. Click on the **Data Tab** by # 1,

Step 2. There are several choices, select **Annual Data.**

Step 3. This Screen below pops up.

Step 4. Does $12.10 seem reasonable to replace $5.98 in 2022? Notice the previous year was $14.10.

Step 5. Click Update Study

(Moving back to slide 10):
 In this slide, notice sales and EPS the rapid growth in 2021 during COVID, there is a steep rise in EPS between 2019-2021 followed by the decline in 2022. To me, $12.10 seems reasonable. The trend Line helps to even out the growth through the ups and downs.

Slide 12

After updating the Annual Data, complete the Fundamental Data on Page 1. In the Orange Box, we have the Analyst Estimates from Morningstar on the front of the SSG.

We now have the opportunity of looking back at Value Line: January before year-end reporting, April after year-end reporting and the recent October report. We notice analysts do change their numbers. Also note in the January and April reports Value Line is estimating Sales above the historical averages.   From Morningstar and Value Line, we have 2 yrs est. and 3-5 yrs est.

In Step #1
In Fundamental Data: I chose to go slightly less than historical average of 4.9 to be as growth tends to gradually slow down. The Historical Sales were 4.9%. (refer to Slide #5)

Reminder: A company is not likely to grow SALES faster in the future than it did in the past. Notice that Value Line's earlier sales estimates were higher than the historical average. This is a mature company and it will not be opening NEW stores like it did in the past.

In Step #2, For, EPS. Consider geo-political situations that affect future estimates: We are in an inflationary period; companies are trying to move away from so much dependency of China and TGT, like other retailers, is also experiencing pillage. These challenges will affect future earnings. Notice I am in line with Value Line with my EPS estimate and below the historical EPS due to geo-political concerns. Also EPS are not likely to triple sales in the future

Slide 13

Now we go to the Valuation and Return green Tab to look at the P/E's. We want to eliminate any outliers. Outliers are the numbers that stand out from the other numbers in Column D & E. In Column D: 42.6 is far above the numbers in the 16-23 range.

In Column E: 22.9 is far above the numbers in the 10-11 range. We eliminate or cross out these numbers to achieve a reasonable average number for the P/Es. These averages are used to project the potential price and return in the SSG in Sections 4 and 5.

Slide 14

Next, we need to Determine High Price using the Average High P/E.

We fill in the number at Step 1.

Step 2 is a sanity check. For a mature company the high price should be less than double the current 52-week High Price.

Slide 15

Step 1. By the green #1, Enter the Average Low P/E

Step 2. By the Red Box at #2, Enter the EPS off the Trend Line, Noted in Slide 10

Step 3. By Orange #3, Note the 52-week low price and select a lower price of approximately 20% lower than the 52 week low price.

Slide 16

After determining the High and Low P/Es and Low Price we move down to Section 4 of the SSG: Evaluate the RISK and REWARD results. In this case we have a Risk/Reward of 3.7 to 1 giving us a Range in the BUY Zone.

Slide 17

Moving down to Section 5 of the SSG. In this section, Visually Check that the Dividend Yield filled in makes sense to you. I am accepting the defaults as it seems reasonable to me. Now, the SSG Results Summary are calculated for us. We have a projected return of 20.7% based on the High P/E and a Projected Average Return (PAR) of 15.7% based on the Average P/E. At the bottom right, checking with Value Line after the 2022 returns have been posted, we see that my numbers are in a similar range. Now I am more confident of my numbers.

Slide 18

Let's look at TGT, two quarters into 2023, We can see how TGT is starting to come back after two quarters. The 1st quarter was affected by a political boycott of TGT. This is not something we can predict. I hope to look back again in the future when more results are in. This is useful to learn if my projections are in range.

Are there any Questions?

Slide 19

After taking a detailed look at Target, you should have an understanding of the process. We are going to take a quicker look at AMZN. I suggest trying this yourself or another company. It will increase your understanding.

Slide 20

Amazon is more complicated because of all of these issues.
Go to Slide 21

Slide 21   This a screen shot at the end of 2022, before any adjustments. I will go over the issues noted in the previous slide
Now you may look at the SSG graph to notice what I am discussing.

- Multiple years of outlier earnings (2014 & 2022)
- Rapid growth during COVID for two years from (2019 - 2021)
- Slow down following COVID (2022) earnings decline
- Elevated High P/Es and elevated Low P/Es each year, that we will see in another slide

Slide 22

After making 2022 an outlier year, the blue EPS trend line is on the sales line. That is not reasonable. We need to another adjustment.

Slide 23

To move the EPS trend line down, make years 2013-2017 outlier years. This also gives the most recent history. Notice the EPS trend line moves down. Now make note the EPS $ amount at the end of the trend line.

Slide 24

Click on the Data tab to bring up the Annual Data. Enter EPS from the last outlier year noted at the end of the trend line on the previous slide. Add that number in the Green Box.

Slide 25

This is a situation where The High and Low P/Es are all elevated. Using the average P/Es will make the projected High Price in five years unrealistic.

Slide 26

To determine "What If" for a High P/E. It should be no more than double the projected High Price in five years.

Slide 27 Steps:

1. Using the earnings projection off the Trend Line on the front of the SSG,
2.   Fill in the Low EPS Forecast,
3.   Then use the **blue** Update Study.

Slice 28

For the Low Price, use a low-price estimate that will keep the U/D ratio lower than 10:1.

Using my estimates, the potential return based on P/Es between 17-23%

Slide 29

This is a capture of the SSG, two quarters into 2023. We see that earnings are moving up.

Slide 30

Any Questions? Here is my contact info if you would like me to explain the process I used or if you need help with a company you are working on, I am available.

Slide 31

Poll Question