

SHARES REVISITED

HYDE PARK: The basic principles of investing in the stock market are very simple however; it is very difficult for people to implement these principles consistently over time. That is why so many people think the stock market is only a good place to lose money. I believe anyone can create wealth by investing in shares if they are patient and disciplined – like all good things in life it requires consistent effort to be successful.

YOU NEED A GAME PLAN

It is possible for any person to become financially independent; you don't need to have wealthy parents nor do you need a specialised education or financial background. You just need to develop your own game plan for your money and then you need to stick to your plan. If you want to be financially independent, you should adopt the same approach as someone who is training for a marathon for the first time. Firstly, you need to start with a training programme; this means you should figure out what steps must be followed in order to achieve your goal. Then you need to break down your objective into a series of smaller goals that must be reached within a particular time. The key ingredients of any financial game plan are:

- A proper budget
- A debt management/avoidance plan
- A planned “financial freedom” date
- An investment plan

Each of these topics would qualify for a book on their own but this piece is about your investment plan, more specifically how to develop a game plan for investing in shares.

INVESTING IN SHARES

Many people have emailed me over the last few months asking how they should start their own share portfolio. It is important to understand that there are many ways to manage a portfolio; this is only one example of how you can do it. Personally, I believe the best way to start a share portfolio is to use an index as your core holding and then you invest in individual shares to compliment your core holding. When starting a portfolio, you should build up your index investment to a minimum value of R100,000 before you begin selecting additional individual shares. The total value of these individual shares should eventually comprise 30% of your overall portfolio.

WHAT IS A GOOD INDEX FOR YOUR CORE HOLDING?

I like the indices that have some form of fundamental filtering. This means an index that weights companies according to their real economic value i.e. value of dividends, actual profits or any other relevant measure. Good examples of these are the Rafi and Divi indices. You can buy either of these directly or via a stock broker.

WHAT ARE GOOD SHARES TO ADD TO YOUR INDEX?

There are different ways of enhancing your portfolio of indices with individual shares, you can buy specific shares that are already in the index but are very undervalued or you can buy shares that are avoided by the market in general. The main group of shares that are avoided by the market are small companies that are too small to be on the radar of large institutions and pension funds. Personally, I prefer investing in large companies via an index and then directly in a few small companies. The reason I like investing in small companies is that they are totally ignored by large fund managers and

most analysts, which means they are often mispriced. The secret to investing in small companies is that you must do proper homework on each share before you invest. This also means that you should not have too many of them in a portfolio as you need to become an expert on each company. There are some good small company fund managers and analysts in the market but it is difficult to get access to their research. One of better small company analysts is Keith McLachlan who runs an interesting site www.smallcaps.co.za. I asked him for some ideas on small companies that are currently offering good value and he gave us the following two:

“Litha Healthcare Group Ltd (LHG): A relatively cheap entry into the defensive pharmaceutical market with strong expected future growth and a highly strategic group asset in The Biovac Institute.”

“Pan African Resources Plc (PAN): A well-managed low-cost gold junior with a highly profitable PGM (platinum group metals) project soon to be contributing strongly to the bottom line. Coupled with the share's attractive value proposition, there is further optionality in the group's Mozambique gold exploration asset.”

YOU CAN JUST STAY IN THE INDEX

Many people think that investing in shares is a complicated business and so they end up with a range of different shares and ETF's because they try to take advantage of every “opportunity” in the market. This often leads to disaster – sometimes the best option is the simplest option. With share investing, this means that you can simply invest in one or two indices and build your wealth on them alone. There is a good chance that you will do better than most fund managers and other professionals.

Share investing is a rewarding way of creating wealth over the long term, you just need to follow the right steps and be disciplined.