10-K Important Clues

* Start from the last page (print the last page first)
* Current assets are at least double their current liabilities
* Long term debt does not exceed working capital
* Eps has increased 100% or 7% annual in the last 10 years
* Current price is no more than 15 times average earnings.
* No more than 1.5 in price according to book value.
* Multiply the P/E ratio by the price to book ratio and see if the result is below 22.5
* Read at least 5 years’ worth of reports
* Proxy statement that discloses the managers compensation, ownership, and potential conflict of interest.
* At least one year’s worth of 10-Q reports
* When a company has over 60% shares that are owned by institutions, it’s scarily «overowned»
* If the largest owners of the stock, is moneymanagment firms that invest in a style similar to your own, that’s a good sign.
* **The company’s «general long term prospects»**
* What makes this company grow?
* Where do (and where will) its profits come from?
* OPM addict = borrows money from banks and sells stock to raise money. «cash from financing activities», «Statement of cash flows»
* Acquisitions in «management discussion’s and analysis» (cross-check with footnotes to the financial statements)
* Relying on one customer or a few, for most of it’s revenues
* A strong brand identity, a monopoly or near-monopoly (isn’t as important regarding small cap companies)
* If cash from operating activities is consistently negative, while cash from financing activities is consistently positive, the company has a habit of craving more cash than its own businesses can produce
* The company produces steady growth at 10% (pretax) or 6-7%(after-tax), anything near 15% and over is illusional
* Spends money on research and development, sows and reaps
* **The quality of its management**
* The executives should say what they will do, and then do as they say, take responsibility for errors they make.
* Obscene paychecks for the CEO’s are a warning, and so is repricing, reissuing and exchanging its stock options for insiders.
* “Option overhang”
* Form 4 at sec.gov shows if the insiders have bought and sold shares. Big red flag if the CEO sells a lot
* Managers or promoters?
* 8-K filings: If “nonrecurring” charges keep recurring, “extraordinary” items crop up so often that they seem ordinary, acronyms like EBITDA take priority over net income, or “pro forma” earnings are used to cloak actual losses, you may be looking at a firm that has not yet learned how to put its shareholders’ long-term interests first.
* **Its financial strength and capital structure**
* Generates more cash than it consumes
* Statement of cash flows reveals if the company’s cash from operations has grown steadily in the past 10 years.
* Owner earnings (how much would you have in your pocket if you owned 100% at the end of the year) : net income + amortization and depreciation – normal capital expenditures, costs of granting stock options, “unusual”, “nonrecurring”, “extraordinary”, income from the pension fund.
* Owner earnings per share should grow at a steady average of at least 6-7% over the past 10 years, then it’s a stable generator of cash, and its prospects for growth are good.
* The company’s capital structure (balance sheet), long term debt should be under 50% of total capital (pay attention to fixed or variable rate)
* “Ratio of earnings to fixed charges”
* **Its dividend record**
* Companies should buy back their shares when they are cheap— not when they are at or near record highs.
* Managers who use splits to promote their stock is a warning.