Capital preservation is key: Prime Value

Identifying stocks that will perform poorly is as important for investors as identifying those that will perform well, according to Prime Value Asset Management.

BY STAFF REPORTER
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A small number of poor performing stocks is “all it takes” to damage a portfolio, the company said, and Prime Value Asset Management chief investment officer Leanne Pan said investors should consider capital preservation as much as potential returns when picking stocks.

“With any stock, you need to ask what can go wrong? Where are the risks? Sometimes today’s returns don’t tell the whole story,” she said.

Ms Pan said when picking stocks there were five signs to look for that typically indicate a stock may perform poorly, namely that the business model is overly complex, the business may be subject to regulatory change, the stock is running “too hot”, the management team has a poor record, or the business may fall victim to structural change and disruption.

Complicated business structures can conceal a number of problems, Ms Pan said, and if the model is so complex that a potential investor can’t explain the model to a friend, that investor won’t be able to adequately assess the business model themselves.

Additionally, Ms Pan cautioned that, much like complicated business models, “high performance can mask underlying issues” and investors should be wary of buying stocks that are already hot.

“The key is always being mindful of valuation – you need to work out if it is fairly valued, and if the company can keep it going,” Ms Pan said.

“You need to know your timeframe and understand that surprises come along.”

Structural and regulatory change both pose risks to shareholders as they can create both crises and opportunities, and investors need to understand the potential for change to affect their portfolio and the risks associated with those changes.