IFB252: Retirement Calculators, P/B and P/S ratios, and Reinvesting AT&T Dividends

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Dave

0:00

All right, folks, welcome to Investing for Beginners podcast. Tonight we have episode 252. We are going to answer or we're going to answer two great listener questions. And we're also going to talk about some feedback we got from a listener about something that we put out to the audience.

So without any further ado, I'll go ahead and read that first feedback. And then we'll talk about that and move on from all the other fun stuff. So high. In a recent podcast, discussion about safe withdrawal rates from retirement investments, and calculators for such a thing. I don't think this is the full biscuit though it might come close. It's a coast fire calculator. But as useful for thinking about investment aims and goals, it can mess with your head a little as the inflation is taken into account. Plus, if you hit the coast part of the fire, it will assume you don't contribute any more.

And let the investment compounding take the heavy lifting. If you want to use it as a straight compounder tool, then enter a high spending and retirement number and zero the inflation. One interesting thing about this calculator for me was the ability to see when you get to a critical mass in your investments, choosing to alter retirement, retire age, or to be able to make lifestyle choices about semi retirement example, the so called barista fire. So Chris shared a link, which I will put in the show notes, as well as another link that

Andrew will talk a little bit about. So Andrew, I know this is something you just investigated. So you want to give us your feedback on Chris's great reveal to us.

Andrew

1:29

Sure. So basically, what we're trying to talk about here is, how much money do you need to retire. And then what's a safe amount of money that you can take out or put in to reach your retirement goals. So there were a few jargon, things thrown around. So I'd like to just give an intro. If this kind of stuff like It's like speaking your love language, then I would highly recommend a subreddit called the fire or financial independence subreddit. So fire stands for financial independence retire early.

That's basically I used to read them, they used to go on Reddit when they had an office job. But it's basically people they say like they want to get out of the rat race, and they want to retire early. So they it's like, you know, financial freedom, I think at its essence. And so they have a really a lot of cool ideas and resources on there. One of these is Chris is talking about here, the Coast fire, which is basically I think it's something we talked about in the podcast before.

But if you have enough money now, where by the time you hit retirement, you're going to be able to retire. So as an example, if I had like $50,000 now, and I determined, okay, I want to spend $50,000 a year in retirement. And if I have $50,000. Now, if that's enough to hit, I don't know, a couple million dollars, then you would hit Coast fire to say, Okay, I already have enough now in my retirement account, or I don't necessarily need to add more. If everything goes according to plan and the stock market multiplies my money like it's supposed to, like it has over decades, then by the time I retire, I will have a full retirement that I can withdraw from.

And so if I'm Coast fire, quote, unquote, then I don't have to add any money, because I already have, like the snowball, basically. So that makes sense. Yes. So this calculator that Chris share with us, which you can find that wallet bursts.com. And you could probably search just coast fire calculator. It will let you input your age, your retirement age, how much do you think you'll want to spend in retirement? How much you have invested now, how much you're going to add to these investments? And what rate of return do you expect from your investments.

So a good starting point would be 10%, because that's the average stock market return and lets you put in inflation. So if you think inflation is going to stay like at 3%, instead of the 2%, historically, we'll calculate all that. And then it will give you an input for like, how much do you want to withdraw from your portfolio. So that's a whole can of worms that we won't get into. But people have different debates on how much you should take out of your retirement to maintain over the rest of your life. But that's a tool that you guys can use.

Thank you for sharing. Chris, we were hoping to find out a tool just like this where you can put in your own information. And you can see on a really pretty chart as it moves, you can say okay, well, if I contribute how much by contribute this much, how much will I be at or, you know, maybe I want to spend a little bit more retirement or maybe I'm okay, spending a little bit less.

And you can see and you might be surprised that to get to this coast fire, which sounds like a pretty cool goal might not need as much money as you think depending on how much you think you're gonna invest and how much you think you're gonna spend in retirement. It's a pretty cool thing, and you can change retirement age too. So if you're a couple years behind, you can just assume I'll just work a couple of years more. That's awesome.

Dave

4:59

So If I want to live on a beach in Hawaii, does it take that into consideration for me?

Andrew

5:05

Yeah, I mean, how much you're gonna spend on margaritas? Probably. She's put that in annual retirement spending

Dave

5:16

probably way, way too much. That's awesome, Chris, thank you very, very much for sending. We were hoping for something like this. So that's awesome. We will definitely put that in the show notes. And all credit goes to Chris for digging that up and sharing that with us. So thank you very much.

Andrew

5:30

Yeah. Thanks, Chris. So let's move on to the next one. This one says Hi, Dave, thank you so much for all the information you provide for newbies like me. I have a question about two companies that I have compared just to get an understanding of are moving in the right direction. I hope you can help me. Feel free to use this in your podcasts too. It's a good question.

The two companies are peyto exploration and Devon Energy. Both got a P E of around 16. PS around for a pedagogia PB of 1.26 and Devon 4.7. Both companies seem to be doing good on cash flow and reports look like they are expanding every year. Now with PE that would be the better company to invest in because the PB is lower. I know I'm missing a lot of information. Hearing you folks talk about stocks is incredible. I know the way to knowledge is time spent. Hope that you can help me. Thanks, Freddie. So Dave, what's this PB thing P S? And what's your answer to for this question here.

Dave

6:30

All right, so let's unpack some of the jargon here to help folks that are not familiar with those. So the P e is what's referred to as a price to earnings ratio. And this is a very common ratio that people will use to help value a company. And the easiest way to think of this is you think of the price per share that you would see in the stock market over the earnings per share that the company generates that you would find on a financial website like stratosphere.io.

Or you would find it on a financial report, whether it's through bam, sec, or sec.gov. All those sources of information will give you the idea of what a P e is. And the P e is a ratio that we use to value companies. And generally, as in finance, it depends. Anything lower means that the price is cheaper. And that's compared to the earnings. And so that's kind of what the P e is. And so he's asking if the PE of both of these companies 16, which means for every $16 in price that's equal to $1 of earnings of the business. And so that's kind of the easiest way to think of it. price to sales is the same kind of idea. Or the PS, which equals price to sales is the same kind of idea, you're comparing the price to the sales or the revenue of the company. And generally, again, the lower the better. So the price again, you could find in the stock market on any of your favorite websites, or you could find the sales, basically the same places. So it really kind of depends.

But both of these two metrics we talked about are they're considered valuation metrics, which means they help tell us how expensive or cheap a company may be. And it's not based on the dollar amount, it's based on the value of the business. Now price to book is the same kind of idea. It's a little more complicated than price to earnings or price to sales. But it operates on basically the same idea where you're looking at the book value of a company, which you could relate to the shareholders equity or the equity of the business. And you could compare that to the price of the business. And again, generally the lower, the cheaper.

And that's the easiest ways to think of those. So all three of these ratios are very common ratios that investors will throw around to help quickly determine whether companies are cheap or not, without doing a lot of extra intrinsic valuation work. And it's also jargon that investors will throw around between each other to help give us relative metrics to determine al Hey, is Devin cheaper than paito? is Devin cheaper than Chevron? You know, any of those kinds of things. So that's kind of where Freddie is going with asking us some of those jargony type questions. So I hope that helps kind of explain that overview. So Alright, so let's move on to, I guess, actually thinking about looking at these companies. So again, not investment advice, please do your own diligence.

These are not companies that I am super familiar with. I'm actually not familiar with them at all, but I did some little quick checking on both of them. They're both in the oil industry. Hato is actually based out of Canada, and it has an over the counter ticker symbol. So here in the United States, it's not traded on any of the major exchanges. So you'd have to buy it over the counter, which means that it's something you you would buy through your broker over the counter. Then we also have Devon Energy which is based out of Oklahoma The city. So that's a US based company. And that does trade on the Dow, I believe. Anyway, so both of those companies are in the oil industry. And that's not something I'm super familiar with, it's not really doesn't really fall into my wheelhouse.

But as I generally kind of looked at both of the companies, it looks like, just from a quick overview that Devon has a better better revenue growth and stronger revenue growth. Now, the company's market caps are quite varied. paito is less than 2 billion, and Devon has around 35 billion, so they're one is much bigger than the other one. So it's not quite apples to apples, per se, but they kind of operate in the same kind of industries. One of the things that I noticed when I was kind of just skimming through the financials for these companies using stratosphere diode to help me quickly look at these companies. Devin had negative revenue growth over the last five years.

And as over the last three years, it's also seen negative earnings growth over the last five years and an ex last three years, so that's not great. paedo, however, has seen revenue growth over the last five years and three years as well as earnings growth. So those were things that I think, you know, give you an overview of, hey, maybe this company is a little stronger than the other one operationally.

But without really digging into the businesses, it's hard for me to definitively say, hey, this one is better, and hey, this one's better. But here's what I would recommend to Freddie is if I was looking at investing in those companies, is looking at these kinds of things that I'm looking at right now, the valuation metrics are fine to look at. But once you need to start digging in deeper into the actual companies, to see what they're doing and how they're doing it, and start asking yourself questions. So the first question that I would ask myself is, why is Devins revenue growth? Negative for the last five years and three years combined? Why? Why is that? What about their business? Is it the fact that it's based on oil commodity, and maybe paedo is not as much. So getting to the bottom of that is going to go a long ways towards telling you whether one of these companies is a better company than the other?

Because no matter how cheap one is versus the other, if the cheaper one is also producing less revenue growth, then what are you buying? You just buying? You're buying a dying ember? I'm not saying that both these companies are dying embers. But I guess my point is, is that as you work through these kinds of companies start asking yourself questions, why is the revenue growth down for one and not the other? What is it about these businesses that is causing one to have negative earnings growth? And the other one to have positive earnings growth? Is that because of where they are? Is it because of what they're doing?

These are all questions that you want to ask yourself and answer them. Because if you can't answer those questions, then we shouldn't be buying these companies. And I also noticed that one of them is seeing negative growth in their dividend. Well, that's not great. So that tells you why. Why is their dividend not going up? If they're growing revenues, but they're not growing their dividend? Why?

So I don't have those answers. And unfortunately, I don't, but one of the things that we really tried to do is teach you how to fish and not give you the fish. And so these are just some simple questions that you can ask yourself, that are all part of analyzing a business. And those are the things that I do when I work through company reports is I ask myself questions, and then I try to answer them. And that helps me get a better insight into the different businesses that I may buy or not buy. So now that I've talked a lot, Andrew, what are your thoughts on? On all this?

Andrew

13:51

I think those are all excellent questions to ask. And further, I think it's great that you're starting to wade into some of the basics. And that's a fantastic place to start. If this kind of thing is appealing to you, and you enjoy the activity of looking at individual stocks. What I'll say is, I think it also depends. I know this is kind of big picture. But I think it also depends on like, what kind of an investor you're trying to be.

Because I think embedded in this question, you're kind of asking is this stock cheaper than that stock. And I think when you're in that frame of mind, it's an approach that works for some people, but it means buying and selling a lot. And that's the way I've seen it work. Or if you buy cheap stocks, you buy them when they're cheap, you sell them when they're expensive. And you just flip through that like over and over and over again. The type of investor that I've become now over the years is more of a long term where I just want to buy it and let the business do the work for you. So I think the questions of like, what I buy and hold this company for 10 years, those are going to be a lot deeper Fred, and they go more towards what Dave saying, like, what's happening in the business?

What's impacting this business's revenues? Why are their profits moving like this? Why, you know, what makes this business special compared to its competitors? Those are the kinds of questions I'm asking now. Because I want to hold the company for a long time and don't have to touch it or think about it. If you're playing the game, where you're jumping in and out of law stocks and buying cheap and selling high, then, you know, a focus on the numbers like P, E, and PB and stuff, I think is more appropriate. So I hate to say like, Hey, pick a road and stick to it. But I think maybe in picking that road that might help answer the next step in the path of figuring out what kind of stocks I want to buy.

Dave

15:45

Yeah, exactly. And I think the along with that is deciding what kinds of areas of investigation interests you and appeal to you, and you feel like you can have some strength in. And for me, something like these are commodity based businesses. And that falls a little bit out of my wheelhouse at this point in my investing journey. And so when I consider looking at something like this, I also have to take into consideration that I have to learn more about the commodity business, to understand these businesses. And if I can't understand the commodity business, then I'm never going to be able to understand these businesses.

And so I think that's something that to keep in mind as well. And I'm not trying to discourage Freddy from investing in these companies. If this is something that he has a passion for, that by all means dig into it and learn as much as you can about the oil business, the commodity business, because that'll hold you in good stead as you continue your your investing journey, because that knowledge will compound and you can use it to look at other commodity businesses or other commodity like businesses as well. And it can be very, very helpful.

So this is all great stuff ready? And these are all great questions. And, you know, just try to keep a list of questions that you have, consider what kind of investor you want to be. And consider if these kinds of things fall into your circle of competence or your wheelhouse, and are things of passion that you want to learn if they are then man, go for it, dig into it, and learn as much as you can. And then hey, you could get back to us and tell us how you did with either one of these companies. That would be awesome. All right. So let's move on to the last question.

So we have Hi, Dave and Andrew big fan and I've been following the podcast closely since the pandemic started, which is also when I started investing. My question is related to dividends and dividend reinvestment. Andrews wheelhouse around 65% of my portfolio is in IBV s&p 500 index, with a balance focused on individual stocks AT and T is one of those stocks and makes up about two to 3% of my total portfolio. Currently, at&t dividend is about five to 6% and I have thus far been reinvesting to compound at&t. However, as I see it has limited upside in terms of growth potential because it is a more mature company.

This leads me to my questions. Number one, would you agree with my very basic analysis of AT and T, even with the recent spin off and my primary question number two, instead of reinvesting the dividends back into at&t, would it be smart to take the dividends as cash and use that cash to invest in other stocks with more growth potential? In my case, more IBV? Hope that is clear. Thanks so much, Mike. Andrew, this is a great question. And I'm going to be really interested to hear what you have to say because I'm not entirely sure how I'm gonna answer it yet.

Andrew

18:34

Well, thanks for writing in Mike, I'm a big fan of this question. I generally agree with Mike's analysis here of at&t looks muttered and Thoresen for me, like a really simple way to kind of figure it out. Because I think when we talk about businesses that everybody knows, I think it's easy that sometimes let how we feel about the business kind of dictate how we think it is, which might may or may not be the reality. But if you look at the numbers behind this business, then you can have cold hard evidence on whether it has the characteristics of a maturing business or not. So you can use a website like quick fs.net or stratosphere.io.

And you can pull up the income statement of any business. And at the very top line, there's the revenue line. And you can see on how that revenue line is changing from year to year. And so if that revenue lines declining, or the revenue growth is really, really small, like just a couple of percentage points, then you might have found a business that's maturing, I kind of see that when I look at a TNT. I haven't looked deep into its business model, but just kind of from poking around between at&t and like T Mobile and Verizon and some of those guys. It seems like they spend a lot of free cash flow in like five or 10 year periods. So it's like they have this big lump sum, where they're paying for the The licenses that they need for this 5g stuff. So that kind of turns me off to it. And then the revenue growth isn't too exciting.

So it's like, okay, kind of pass and move on. So I think, you know, unless there's something about 18 t's business model that I don't know about, I kind of side with that idea that it's probably mature, it seems to me like the cell tower networks are just fighting for customers between each other. And I don't know, what the other growth Avenue is, I think there has been the argument has been made that 5g can be sold to businesses. And that could be a new avenue of growth. But I mean, until we see the evidence, I kind of think that it's a mature stock, do you see a TNT in a similar light?

Dave

20:45

I certainly do. And I think a couple things to think about along those lines, you know, I think you're right on about the the capital expenditures, the money that they've been spending is to build out this infrastructure for 5g. And that could be the potential growth driver for the company. But that's been in play for all these big companies for several years now.

And you don't really seem to be seeing to that. And it could be taking longer than maybe they expected or we expect, and that's certainly possible. But the other thing that I think about too, is they've also spent a lot of money on trying to buy other businesses to spur growth that are kind of outside of their circle of competence, if you will. And I, to me, that signals that they know that their growth is slowing, and has a plateau that they may be approaching. And so they're trying to diversify or pivot into something different, to continue to generate more growth.

And you've seen that with att. We've also seen that with Verizon. And you've seen that a little bit with T Mobile when they bought, who's the other one that they just bought recently? During sprint? Yes. So you see them trying to grow by taking on another cell phone provider, but at some point, they're going to kind of hit a ceiling, too. So it seems like it's kind of a saturated, mature business to me on the outside.

Andrew

22:13

Okay, so if we're assuming that we think that we have a matured business, that doesn't seem to have much avenue for growth, and it's making up a pretty good part of the portfolio two to 3%, I would say that's a pretty good part of your portfolio. The question is, do you reinvest the dividends? Or do you take the dividends and take and put them into a different company? My question is, if you're considering reinvesting dividends into a different company, why not just sell the position? And just find a new company?

Dave

22:44

Yeah, that's why I wasn't sure how I would answer the question. Because that's, you know, I understand. I mean, it's great that they're giving you a dividend of five to 6%. But I think a lot of the, unless you're in retirement, already, a lot of the, I guess, in benefit and really desire to drip is to grow the value of the business that you're already own. And if you're taking those dividends out and investing, and you're taking those dividends out and investing in visa, why don't you just buy visa and have a drip on visa, as opposed to owning a company that you think has limited upside, but it pays you a great dividend,

I think your overall return would be much better to buy a company that has potential to grow further, and pays you a dividend. That's the best of both worlds where this is kind of more half of a good world, but maybe not so great. Have a half have a good world, you know, so it seems like it's kind of, you know, I guess that's my thought, What are your thoughts?

Andrew

23:45

I agree with all of that church is trying to like think outside the box, if this is somebody, so I'll give an example. My my grandpa actually had a bunch of at&t stock, he worked there for a long time. So if we were talking about him, before he passed, maybe you have tax implications. So like, if you're holding this in a taxable account, and then you know, that if you sell this, I gotta dish out, you know, 20% in taxes or something, then, you know, I can kind of see the dividend argument that way. So I feel like taxes can maybe drive this conversation as much as the actual stocks themselves, so that that would be something to keep in mind. It's funny, we were answering this recently recording our episode on See's Candies.

So I don't know what the timing will be like if people will, if this is a spoiler alert or if people have already doesn't matter. The bottom line is we you know, See's Candies looks like a great investment because they were matured, but they were a cash cow. When you get what you can get with mature businesses or companies other not cash cows, because they're having to put a bunch of free cash flow back into the business, whether that's to build infrastructure, whether it's to pay for licenses, whatever it is. So when you see a big dividend payment from a company like that, it might not be because it's a cash cow, it might be because the stock is so cheap, because investors don't want to touch it because it's matured.

And so that's where you have to be careful of, if a stock has a high yield, meaning you're getting a high dividend percent for buying the stock, sometimes it's because it's a cash cow. And they're able to just take a lot of their profits and give it back to investors, like paychecks is a good example of that.

But sometimes, they're not having much free cash flow, just what alert free cash flow they're giving back is a lot because the stocks are cheap. So I would, I don't want to say anything like to say, yeah, 18 t's can be a terrible investment or anything where you should buy or you should sell. I'm just saying, as a general rule, this is how I look at mature stocks. And that's how I would look at the decision. If there's taxes, that's one thing, but if we're just talking straight up, Roth IRA, retirement, that kind of a thing, then I would lend itself towards the kind of logic we've been using for this business with a lot of other kind of businesses.

Dave

26:07

Yeah, I would agree with that. And the tax implications is an interesting angle to think about. And that's, that's something you need to consider we, we don't have all that information, but Mike does. And that's something that he would be able to make an assessment on. Another thing that I was thinking about, too, as Andrew was talking about, you know, these companies that maybe, maybe they're very profitable, and they can generate a lot of cash flow, but if they have to throw it back in to try to maintain the growth of that they have, then that can be value destroying as well.

And sometimes, we have to think about businesses in kind of an evolution of their lifecycle, if you will. And I was listening to a video with Professor Dumbledore and recently, and he was talking about this kind of idea of companies that maybe produce a lot of cash, but are has he put it dead men walking, but don't realize it yet. And they are spending a lot of money to try to maintain their livelihood and their youth, when they're really past their prime. And they really should just be buying back up a bunch of shares and paying a lot of dividends, and realize that their best days are behind them. And that sounds like an old man talking it is.

When you think about a business like at&t, and again, I'm not saying it's a good or bad investment. But that's something that you want to consider is where are they in their evolution of their lifecycle. And you could argue they're on the other side of, of the trough, and they're probably on the way down. And so you have to consider is that something you want to continue to be invested in or not, or start to invest in just because it has a nice big fat dividend, which is related to their their price, which is driven down because other investors think the same way that we do? And so those are all things to consider when you're thinking about analyzing companies and deciding what is it that I want to do with companies that are in my portfolio? And how do I want to go forward with that? So this is a great question.

Andrew

28:09

So what's a simple metric, or ratio or something? Somebody can point that to be like, alright, this might be a dead man walking bull?

Dave

28:20

That's a good question. I think there's two things that bring to mind. Number one is when you see revenue growth, dropping to match or below the growth of the overall economy that the business operates in. So for example, if you're in the United States, and it's and their revenue grows for a long period of time, you know, once in a while, you know, economic conditions arise like the pandemic or the the great financial crisis, you may see a company's revenue growth drop.

But if you see over a long period of time, that they're matching the revenue growth of the GDP, that's not a good sign. So that's part of it. The other part of it would be, and this is a little more inside baseball, is if the returns on capital start to move towards the cost of capital of the business, then you're going to start to see some value destruction or the company is maybe more along the lines of a dead man walking because if they can't reinvest more efficiently than the cost, that it cost them to invest, that's not good. And that will lead to a decay in a business over a long period of time.

Andrew

29:32

So safe to say, ROIC below 10. If you combine that with low growth, that could be waste a lot money on makeup and stuff.

Dave

29:43

Yeah, exactly. That's the way I would think about it. Yeah, me too. All right. Well, with that, then we will go ahead and wrap up our conversation for today. I wanted to thank everybody for taking the time to send us those fantastic questions. And Chris, thank you for sending us the calculator. That was awesome.

So, for those of you out there that are looking for more information on what is price to book, what is price to earnings? What is this ROIC thing? Or what is this cost of capital thing, please check out our website e investing for beginners.com. We have this huge resource, great search bar at the top of the page that can type in price to earnings and you'll find all kinds of information to help you learn more about that if that's something you're not familiar with. So it's a great resource for there for you to help you learn more about investing. There's about 1100 articles there.

So there should be a thing or two for you to find to read. So without any further ado, good and good. sign us off you guys go out there and invest with a margin of safety emphasis on the safety. Have a great week, and we'll talk to y'all next week.