

AlphaScreens: the market according to GARP

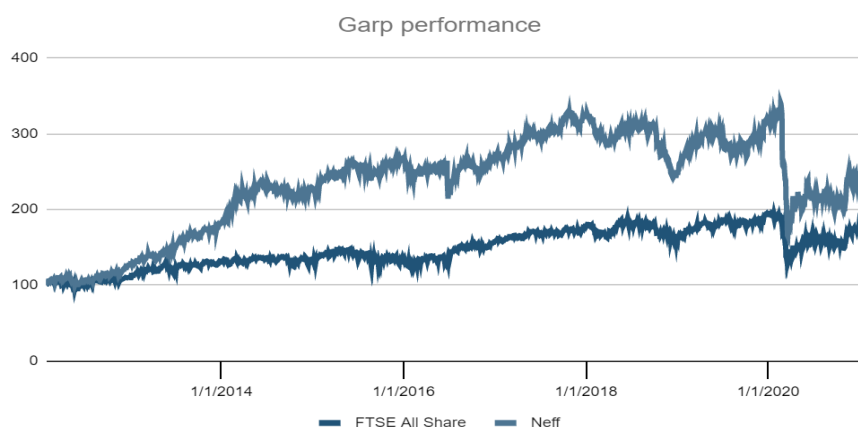
8 November 2021

Fairly priced for recovery?

Growth at a reasonable price, or GARP, has proved a reliable strategy that has previously generated market-beating returns. We run our GARP screens across three indices: FTSE All-Share, All Small and Aim

Comment by Alpha editor:

- Top of our large cap growth at a reasonable price (GARP) screen this month is sports fashion retailer JD Sports (JD), a perfect illustration of why screens alone aren't a buy signal. The Competition and Markets Authority ruling it must sell Footasylum will surely see a serious revision of JD's growth prospects.
- A UK listed company with significant US exposure is plumbing and heating products distributor Ferguson (FERG). The passing of President Biden's \$1.2tn infrastructure bill could be good news for the business.
- Our Aim screen is topped by Central Asia Metals (CAML), a business with significant copper assets. There is a strong long run bull case for copper but cyclical risks still exist.



Source: Refinitiv, Investors Chronicle

Finding that magic combination of value and growth

Buying shares that offer growth at a reasonable price (GARP) can generate strong returns. Prominent exponents of this style of investing include the likes of Jim Slater, Peter Lynch and, arguably, also John Neff. A key metric to assess whether companies offer the magic combination of value and growth is the price-to-earnings-growth (PEG) ratio. In its most basic form the ratio simply compares a share's valuation against its earnings with its earnings growth rate (historic or forecast). This approach is not overly exacting, but over many years it has proved a very effective way of identifying great investment opportunities when combined with other factors that suggest there are solid foundations to the value and growth measures used by the ratio.

Large-cap GARP criteria

Our large-cap GARP screen is run on all FTSE All-Share stocks and uses a PEG ratio based on the historic price/earnings (PE) ratio divided by a combination of the earnings growth rate and dividend yield. The earnings growth rate is calculated based on the average of the five-year historic growth rate and the average forecast growth over the next two years. The screening criteria are:

- A PEG ratio below the median average.
- A PE ratio that is higher than that of the lowest quarter of stocks screened (i.e. not suspiciously cheap) and below the top quarter (i.e. not dangerously expensive).
- A five-year historic EPS compound annual growth rate above 7.5 per cent but below 20 per cent (i.e. high, but sustainably so).
- A five-year historic revenue compound annual growth rate above 5 per cent (i.e. sales growth underpinning earnings growth).
- Year-on-year EPS growth in each of the past two half-year periods.
- Average forecast EPS growth of more than 7.5 per cent for the next two financial years.
- Positive free cash flow in each of the past three years.
- No downgrade to forecast EPS over the last three months.

Not many stocks pass such a stringent list of criteria. The ones that pass all the tests are listed at the top of the table at the top of page 4, followed by those failing one test, then those failing two tests and so on as detailed in the 'Tests passed' column. All stocks must pass the PEG test to feature in the table. While the primary ranking of the stocks is based on the number of tests they pass, inside each of these groupings, stocks are ordered

according to their attractiveness based on a combination of PEG and three-month price momentum.

Small-cap GARP criteria

Our small-cap GARP screen is run on all stocks in the FTSE All-Small and Alternative Investment Market (Aim) indices, with the results from the individual indices listed in separate tables. The screen uses a PEG based on the historic PE ratio and average forecast growth for the next two financial years. The screening criteria are:

- A PEG ratio in the bottom quarter of all stocks screened.
- EPS growth forecast for each of the next two financial years and an average growth rate over the period of more than 10 per cent and less than 50 per cent (i.e. high, but sustainably so).
- Either a return on equity (ROE) of over 12.5 per cent or an operating margin of over 15 per cent (i.e. an indicator of a quality business that may have a sustainable advantage).
- Either three-month share price momentum better than the median average or earnings upgrades of 10 per cent or more over the past three months (i.e. recent reasons to feel positive).
- Operating cash conversion of 90 per cent or more.
- Net debt of less than 1.5 times cash profits.
- A market capitalisation of more than £10m (i.e. not severely illiquid).

Not many stocks pass such a stringent list of criteria. The ones that pass all the tests are listed at the top of the tables on page 5, followed by those failing one test, then those failing two tests and so on as detailed in the 'Tests passed' column. All stocks must pass the low PEG test to feature in the table. While the primary ranking of the stocks is based on the number of tests they pass, inside each of these groupings, stocks are ordered according to their attractiveness based on a combination of PEG and three-month price momentum.

Stock screen and methodology by Algy Hall

Large-cap GARP selection (passing 6 out of 8 tests)

Name	TIDM	Mkt cap	Price	Fwd NTM PE	PEG	DY	EPS grth FY+1	EPS grth FY+2	3-mth momentum	Net cash/debt(£) in £	Tests passed (out of 8)	Test failed
JD Sports Fashion	JD	£11,565	1,121	22	0.9	0.1%	56.4%	4.5%	19.6%	-591m	8	na
Macfarlane	MACF	£208	132	13	0.6	2.1%	58.9%	2.9%	9.1%	-58m	8	na
Sirius Real Estate	SRE	£1,469	138	20	0.3	2.4%	53.6%	-7.4%	14.0%	-	7	/HY EPS grth/
Ferguson	FERG	£25,067	11,315	20	1.0	1.5%	8.5%	7.0%	10.6%	-2,523m	7	/5yr EPS grth/
LondonMetric Property	LMP	£2,482	273	27	0.5	3.2%	3.4%	5.8%	5.6%	-	7	/Av FY2 Fwd EPS growth > 7.5%
Segro	SGRO	£15,980	1,329	43	0.5	1.7%	11.2%	11.4%	4.7%	-	7	/5yr EPS grth/
Pets At Home	PETS	£2,472	494	22	0.9	1.6%	50.1%	13.3%	6.2%	-195m	7	/5yr EPS grth/
Greencoat UK Wind	UKW	£2,877	135	10	0.3	5.3%	121.4%	-2.8%	-0.9%	-	7	/5yr EPS grth/
Lucoo	LUCE	£609	378	18	0.6	1.9%	31.5%	9.5%	-4.7%	-58m	7	/5yr EPS grth/
Keller Group	KLR	£651	900	10	1.2	4.0%	-18.9%	20.2%	-6.7%	-446m	7	/Av FY2 Fwd EPS growth > 7.5%
Tyman	TYMN	£762	388	11	0.7	2.1%	18.6%	6.6%	-9.4%	-69m	7	/5yr EPS grth/
Assura	AGR	£1,955	73	22	1.1	3.9%	12.6%	5.6%	-7.7%	-	7	/HY EPS grth/
Severfield	SFR	£221	72	9	0.8	4.1%	14.7%	12.1%	-10.7%	-60m	7	/HY EPS grth/
Hikma Pharmaceuticals	HIK	£5,535	2,391	15	1.1	1.6%	16.5%	14.6%	-9.5%	-495m	7	/HY EPS grth/
IG Group	IGG	£3,409	790	11	0.8	5.5%	-28.8%	12.4%	-13.3%	-	7	/Av FY2 Fwd EPS growth > 7.5%
Alfa Financial Software	ALFA	£579	193	37	-71.2	0.5%	-21.7%	5.1%	32.6%	19m	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
SThree	STEM	£766	573	18	0.6	1.4%	144.6%	10.4%	14.6%	-130m	6	/5yr EPS grth/HY EPS grth/
Fresnillo	FRES	£6,639	901	15	0.3	2.6%	73.8%	14.6%	10.5%	534m	6	/5yr EPS grth/FCF/
Legal & General	LGEN	£17,493	293	9	0.3	6.1%	61.0%	4.8%	7.9%	-	6	/5yr EPS grth/FCF/
B&M European Value Retail SA	BME	£6,252	624	17	0.9	2.8%	-14.5%	1.2%	12.3%	-513m	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
Spirit Communications	SPT	£1,752	286	23	0.8	1.6%	15.0%	6.5%	10.4%	63m	6	/5yr EPS grth/HY EPS grth/
3i	III	£13,357	1,372	6	0.3	2.8%	50.4%	-27.8%	5.2%	-	6	/HY EPS grth/FCF/
S&U	SUS	£350	2,880	11	0.4	3.5%	115.7%	-1.2%	3.2%	-	6	/5yr EPS grth/HY EPS grth/
Big Yellow	BYG	£2,802	1,523	31	0.5	2.2%	12.2%	7.6%	2.0%	-27m	6	/HY EPS grth/FCF/
Tritax Big Box REIT	BBOX	£4,232	227	30	0.7	2.9%	3.8%	2.7%	1.3%	-	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
LSL Property Services	LSL	£466	443	11	0.4	0.9%	139.1%	6.2%	-0.7%	-	6	/5yr EPS grth/5yr Rev grth/
City of London Investment	CLIG	£259	512	10	1.0	6.4%	3.2%	5.5%	-1.2%	-	6	/Av FY2 Fwd EPS growth > 7.5% Fwd EPS/
Vistry	VTY	£2,559	1,151	8	0.4	3.5%	138.0%	14.4%	-4.8%	-625m	6	/5yr EPS grth/HY EPS grth/
British American Tobacco	BATS	£58,376	2,544	7	0.9	8.5%	-1.5%	7.6%	-4.2%	-12,097m	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
Antofagasta	ANTO	£13,482	1,367	15	0.2	3.8%	163.5%	-16.9%	-9.3%	1,498m	6	/5yr EPS grth/Fwd EPS/
Kingfisher	KGF	£6,973	332	10	0.8	3.6%	26.0%	-14.8%	-10.1%	-2,041m	6	/Av FY2 Fwd EPS growth > 7.5% 5yr Rev grth/

Source: FactSet, 8 November 2021

Small-cap GARP selection (passing 5 out of 7 tests)

Name	TIDM	Mkt cap	Price	Fwd NTM PE	PEG	DY	EPS grth FY+1	EPS grth FY+2	3-mth momentum	Net cash/debt(£) in £	Tests passed (out of 7)	Test failed
LSL Property Services	LSL	£466	443	11	0.08	0.9%	139.1%	6.2%	-0.7%	-	6	/Fwd EPS grth/
Kenmare Resources	KMR	£460	419	5	0.02	2.6%	668.5%	1.8%	-0.7%	23m	6	/Fwd EPS grth/
JKX Oil & Gas	JKX	£65	38	3	0.03	0.0%	161.3%	-	33.3%	-2m	6	/Fwd EPS grth/
Headlam	HEAD	£388	455	13	0.11	1.7%	121.4%	17.9%	-15.1%	-132m	5	/Fwd EPS grth/Hi RoE or Marg/
Forterra	FORT	£606	265	13	0.10	2.3%	159.9%	23.6%	-14.5%	-41m	5	/Fwd EPS grth/Hi RoE or Marg/
Foresight	FSG	£499	461	18	0.00	0.4%	13977.5%	31.0%	13.8%	-	5	/Fwd EPS grth/Hi RoE or Marg/
Robert Walters	RWA	£633	826	18	0.09	2.0%	406.5%	26.0%	25.9%	-38m	5	/Fwd EPS grth/Hi RoE or Marg/
Premier Miton Global Renewables Trust	PMGR	£37	201	4	0.00	4.3%	654.7%	53.4%	22.6%	-	5	/Fwd EPS grth/Cash Conv/

Source: FactSet, 8 November 2021

Aim GARP selection (passing 5 out of 7 tests)

Name	TIDM	Mkt cap	Price	Fwd NTM PE	PEG	DY	EPS grth FY+1	EPS grth FY+2	3-mth momentum	Net cash/debt(£) in £	Tests passed (out of 7)	Test failed
Central Asia Metals	CAML	£402	228	7	0.11	7.0%	90.2%	2.7%	-6.0%	-14m	7	na
Michelmersh Brick	MBH	£118	123	14	0.28	3.0%	61.6%	8.7%	-1.6%	-2m	7	na
Pan African Resources	PAF	£337	17	5	0.33	3.9%	20.8%	7.0%	1.2%	-51m	7	na
Sureserve	SUR	£149	92	12	0.29	1.1%	66.4%	18.4%	2.8%	-38m	7	na
Somero Enterprises	SOM	£280	500	11	0.16	5.8%	76.2%	8.6%	6.4%	17m	7	na
United Oil & Gas	UOG	£17	3	2	0.01	0.0%	1170.4%	0.0%	-28.8%	-3m	6	/Fwd EPS grth/
Steppe Cement	STCM	£90	41	8	0.20	8.5%	46.2%	4.2%	-19.1%	-3m	6	/Mom or Upgrade/
Sanderson Design	SDG	£124	174	13	0.28	0.4%	54.2%	11.7%	-9.4%	-8m	6	/Hi RoE or Marg/
Journeo	JNEO	£10	114	9	0.29	0.0%	134.5%	173.6%	-6.5%	-6m	6	/Fwd EPS grth/
Wentworth Resources	WEN	£42	22	9	0.12	6.8%	86.1%	-11.1%	-2.2%	11m	6	/Fwd EPS grth/
STM	STM	£20	34	7	0.38	4.3%	29.6%	34.3%	1.5%	-	6	/Hi RoE or Marg/
Griffin Mining	GFM	£177	102	7	0.04	0.0%	285.1%	12.7%	20.1%	-19m	6	/Fwd EPS grth/
MP Evans	MPE	£478	874	15	0.09	3.1%	164.4%	-21.7%	23.1%	-32m	6	/Fwd EPS grth/
Serica Energy	SQZ	£536	199	4	0.01	1.8%	1424.2%	13.6%	27.8%	-6m	6	/Fwd EPS grth/
Enwell Energy	ENW	£127	40	7	0.01	0.0%	840.9%	-16.3%	46.2%	39m	6	/Fwd EPS grth/
Mission	TMG	£63	69	8	0.05	1.2%	500.0%	43.3%	-18.3%	-43m	5	/Fwd EPS grth/Hi RoE or Marg/
Time Finance	TIME	£21	22	6	0.18	0.0%	56.8%	65.5%	-10.9%	-	5	/Fwd EPS grth/Hi RoE or Marg/
Numis	NUM	£392	343	12	0.11	3.5%	68.2%	-33.6%	-7.3%	-	5	/Fwd EPS grth/Mom or Upgrade/
Breedon	BREE	£1,716	102	17	0.35	0.5%	72.2%	28.1%	-3.6%	-283m	5	/Fwd EPS grth/Hi RoE or Marg/
Appreciate	APP	£48	26	7	0.17	3.8%	199.8%	33.1%	-3.3%	-11m	5	/Fwd EPS grth/Hi RoE or Marg/
Warehouse REIT	WHR	£681	160	20	0.26	4.8%	42.8%	13.3%	-0.9%	-	5	/Cash Conv/Debt/
Filtronic	FTC	£25	12	44	0.16	0.0%	800.0%	-	2.2%	-1m	5	/Fwd EPS grth/Hi RoE or Marg/
XLMedia	XLN	£138	52	12	0.10	0.0%	759.6%	152.0%	4.0%	-7m	5	/Fwd EPS grth/Hi RoE or Marg/
Litigation Capital Mgmt	LIT	£132	111	8	0.17	0.0%	147.2%	67.7%	5.0%	-	5	/Fwd EPS grth/Cash Conv/
Portmeirion	PMP	£95	680	13	0.11	0.0%	651.4%	53.9%	9.7%	-7m	5	/Fwd EPS grth/Hi RoE or Marg/
Iofina	IOF	£28	15	6	0.06	0.0%	244.2%	39.1%	11.3%	-3m	5	/Fwd EPS grth/Hi RoE or Marg/
Frenkel Topping	FEN	£88	77	20	0.26	1.8%	146.0%	29.0%	18.3%	-	5	/Fwd EPS grth/Cash Conv/
Vertu Motors	VTU	£227	62	7	0.03	1.0%	168.1%	-54.5%	36.4%	-656m	5	/Fwd EPS grth/Hi RoE or Marg/

Source: FactSet, 8 November 2021

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