

AlphaScreens: the market according to GARP

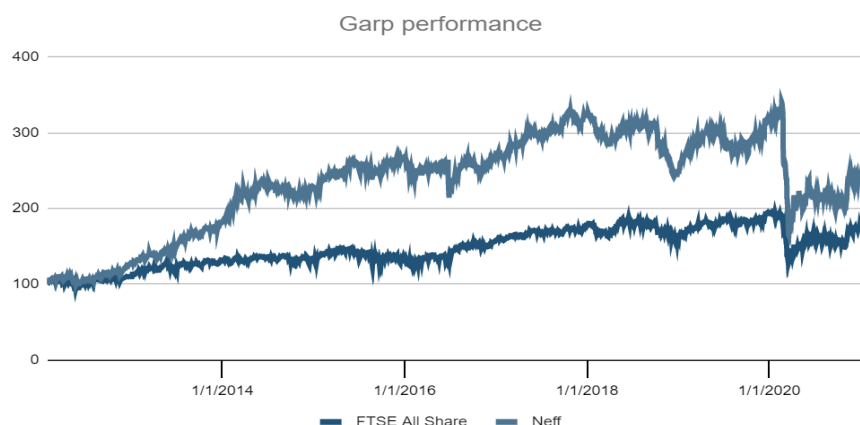
2 August 2021

Property-backed companies proving resilient

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:

- Once again, companies are finding it difficult to pass all of the tests on our Growth at a Reasonable Price (GARP) screens after the pandemic played havoc with growth forecasts over the past year. Among both the large-cap and Aim indices respectively only two companies passed all the tests set by the screen while in the small-cap universe no companies passed all seven tests.
- Among the large-cap selection property-backed companies performed well with Safestore (SAFE) passing all the screen's tests and others such as Sirius Real Estate (SRE) and Assura (AGR) passing all but one of the tests while Segro (SGRO), Tritax BigBox REIT (BBOX) and LSL Property Services (LSL) passed six out of eight of the tests.
- On Aim, Sureserve (SUR) and Smart Metering Systems (SMS) topped the charts as the only two companies to pass all seven tests, although 13 companies passed six of the seven tests set for the junior market screen.



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 at least 6 of 8 tests)

Name	TIDM	Mkt cap (£m)	Price (p)	Fwd NTM PE	PEG	Div yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net cash/debt(-)	Cur	Tests passed (out of 8)	Test failed
Safestore	SAFE	£2,226	1,056	27	0.5	1.9%	23.7%	7.4%	24.0%	505m	GBP	8	na
Smurfit Kappa	SKG	£10,462	4,039	17	1.4	3.1%	6.3%	17.1%	8.8%	2,188m	EUR	8	na
Luceco	LUCE	£624	388	19	0.5	2.0%	30.8%	9.0%	20.9%	14m	GBP	7	/5yr EPS grth/
Sirius Real Estate	SRE	£1,257	119	18	0.3	2.8%	43.3%	-4.0%	17.3%	356m	EUR	7	/HY EPS grth/
Hikma Pharmaceuticals	HIK	£6,125	2,646	18	1.2	1.4%	11.2%	18.1%	8.4%	425m	USD	7	/HY EPS grth/
Keller	KLR	£637	881	11	1.3	4.1%	-28.4%	26.3%	6.5%	193m	GBP	7	/Av FY2 Fwd EPS growth > 7.5%
Pets At Home	PETS	£2,340	468	22	1.0	1.7%	47.5%	10.5%	5.4%	407m	GBP	7	/5yr EPS grth/
Assura	AGR	£2,096	78	25	1.2	3.6%	11.3%	5.5%	5.2%	908m	GBP	7	/HY EPS grth/
Greencoat UK Wind	UKW	£2,695	136	13	0.6	5.2%	58.8%	6.7%	1.3%	915m	GBP	7	/5yr EPS grth/
Severfield	SFR	£244	79	10	0.8	3.7%	15.0%	11.9%	0.8%	7m	GBP	7	/HY EPS grth/
Tyman	TYMN	£831	423	13	0.7	1.9%	14.1%	6.1%	0.2%	147m	GBP	7	/5yr EPS grth/
SThree	STEM	£669	501	19	0.8	1.6%	101.4%	13.9%	24.8%	-12m	GBP	6	/5yr EPS grth/HY EPS grth/
Big Yellow	BYG	£2,669	1,452	30	0.5	2.3%	10.8%	6.7%	21.4%	341m	GBP	6	/HY EPS grth/FCF/
SEGRO	SGRO	£14,613	1,217	41	0.5	1.9%	9.9%	10.0%	21.1%	2,275m	GBP	6	/mid PE/5yr EPS grth/
Tritax Big Box REIT	BBOX	£3,622	211	29	1.0	3.0%	-1.5%	6.5%	10.7%	1,285m	GBP	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
Alfa Financial Software	ALFA	£432	144	38	-3.2	0.7%	-45.5%	5.4%	5.9%	-20m	GBP	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
S&U	SUS	£328	2,700	14	0.9	3.3%	33.2%	37.4%	8.4%	100m	GBP	6	/5yr EPS grth/HY EPS grth/
Polymetal International	POLY	£7,402	1,563	9	0.3	6.0%	3.8%	9.1%	4.5%	1,012m	USD	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
LSL Property Services	LSL	£443	421	11	0.6	0.0%	139.1%	6.2%	2.7%	36m	GBP	6	/5yr EPS grth/5yr Rev grth/
Royal Mail	RMG	£5,042	504	8	0.4	2.0%	20.4%	-0.2%	1.7%	476m	GBP	6	/5yr EPS grth/HY EPS grth/
Kingfisher	KGF	£7,779	368	12	1.3	2.2%	14.3%	-12.7%	3.1%	1,382m	GBP	6	/Av FY2 Fwd EPS growth > 7.5% 5yr Rev grth/
Spirent Comms	SPT	£1,561	255	22	0.8	1.7%	9.2%	7.6%	0.3%	-156m	USD	6	/5yr EPS grth/HY EPS grth/
Brit. American Tobacco	BATS	£61,507	2,680	8	0.9	8.0%	-1.5%	7.5%	-0.1%	41,660m	GBP	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
Fresnillo	FRES	£6,029	818	13	0.6	2.3%	79.5%	16.8%	-0.7%	120m	USD	6	/5yr EPS grth/FCF/
B&M European Value	BME	£5,535	553	16	0.9	3.1%	-23.4%	9.4%	-2.3%	1,814m	GBP	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%
IG	IGG	£3,847	892	13	0.9	4.8%	-30.4%	14.5%	-2.6%	-687m	GBP	6	/HY EPS grth/Av FY2 Fwd EPS growth > 7.5%
Vistry	VTY	£2,651	1,192	9	0.9	1.7%	130.4%	15.9%	-3.6%	4m	GBP	6	/5yr EPS grth/HY EPS grth/
CMC Markets	CMCX	£1,311	450	12	0.6	6.8%	-40.7%	2.3%	-7.8%	-131m	GBP	6	/5yr EPS grth/Av FY2 Fwd EPS growth > 7.5%

Source: FactSet, 2 August 2021

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

Name	TIDM	Mkt cap (£m)	Price (p)	Fwd NTM PE	PEG	Div yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net cash/debt(-)	Cur	Tests passed (out of 7)	Test failed
SThree	STEM	£669	501	19	0.21	1.6%	101.4%	13.9%	24.8%	-12m	GBP	6	/Fwd EPS grth/
Kenmare Resources	KMR	£462	421	6	0.06	1.8%	616.0%	-5.8%	-3.2%	45m	USD	5	/Fwd EPS grth/Hi RoE or Marg/
PayPoint	PAY	£405	590	11	0.09	5.5%	135.2%	6.4%	-1.7%	48m	GBP	5	/Fwd EPS grth/Mom or Upgrade/
Robert Walters	RWA	£510	668	19	0.09	2.5%	300.4%	34.3%	-1.0%	-58m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
LSL Property Services	LSL	£443	421	11	0.13	0.0%	139.1%	6.2%	2.7%	36m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
Forterra	FORT	£691	302	16	0.12	2.0%	157.2%	23.2%	3.4%	-12m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
ScS	SCS	£111	292	11	0.01	1.0%	991.0%	-2.8%	5.0%	36m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
Carclo	CAR	£33	45	10	0.19	0.0%	58.3%	47.4%	11.3%	28m	GBP	5	/Fwd EPS grth/Debt/

Source: FactSet, 2 August 2021

Aim GARP selection (passing at least 5 of 7 tests)

Name	TIDM	Mkt cap (£m)	Price (p)	Fwd NTM PE	PEG	Div yield	EPS grth FY+1	EPS grth FY+2	3-month momentum	Net cash/debt(-)	Cur	Tests passed (out of 7)	Test failed
Sureserve	SUR	£142	88	12	0.28	1.1%	65.8%	17.4%	11.4%	1m	GBP	7	na
Smart Metering Systems	SMS	£1,024	903	66	0.15	2.8%	34.4%	13.3%	11.2%	-37m	GBP	7	na
Griffin Mining	GFM	£156	89	6	0.07	0.0%	315.0%	9.0%	-35.6%	-12m	USD	6	/Fwd EPS grth/
Michelmers Brick	MBH	£122	129	15	0.43	1.9%	59.6%	10.1%	-11.6%	0m	GBP	6	/Hi RoE or Marg/
Central Asia Metals	CAML	£431	245	8	0.15	5.7%	87.6%	-1.6%	-11.9%	24m	USD	6	/Fwd EPS grth/
Numis Corporation	NUM	£386	358	9	0.14	3.4%	56.6%	-	-6.0%	-80m	GBP	6	/Fwd EPS grth/
MP Evans	MPE	£387	710	16	0.46	3.1%	54.2%	11.5%	-3.3%	57m	USD	6	/Debt/
Breedon	BREE	£1,821	108	20	0.42	0.5%	63.1%	30.6%	4.5%	292m	GBP	6	/Hi RoE or Marg/
STM Group	STM	£20	33	8	0.35	4.2%	29.6%	34.3%	8.2%	-13m	GBP	6	/Hi RoE or Marg/
Kape Technologies	KAPE	£721	322	15	0.32	0.0%	74.9%	23.7%	8.4%	-6m	USD	6	/Cash Conv/
Steppe Cement	STCM	£108	49	9	0.22	7.1%	56.1%	-3.8%	10.0%	2m	USD	6	/Fwd EPS grth/
Wynnstay	WYN	£115	570	15	0.44	2.6%	37.5%	3.3%	16.3%	5m	GBP	6	/Hi RoE or Marg/
Frenkel Topping	FEN	£69	63	20	0.32	2.2%	126.2%	19.3%	22.3%	-13m	GBP	6	/Fwd EPS grth/
Enwell Energy	ENW	£87	27	10	0.24	0.0%	148.1%	76.0%	37.1%	-44m	USD	6	/Fwd EPS grth/
Morses Club	MCL	£109	82	11	0.19	3.7%	36.3%	100.4%	45.6%	2m	GBP	6	/Fwd EPS grth/
Argentex	AGFX	£107	94	10	0.45	2.1%	37.3%	37.0%	-25.7%	-32m	GBP	5	/Mom or Upgrade/Cash Conv/
Robinson	RBN	£21	122	8	0.20	6.9%	69.0%	7.0%	-18.3%	7m	GBP	5	/Hi RoE or Marg/Debt/
Caledonia Mining Corp.	CMCL	£111	935	4	0.28	3.0%	30.5%	35.9%	-11.4%	-9m	USD	5	/Mom or Upgrade/Cash Conv/
Wentworth Resources	WEN	£44	23	11	0.33	6.3%	51.3%	-6.6%	-2.1%	-13m	USD	5	/Fwd EPS grth/Hi RoE or Marg/
XLMedia	XLM	£134	51	16	0.07	0.0%	633.9%	168.2%	-1.0%	-10m	USD	5	/Fwd EPS grth/Hi RoE or Marg/
Titon	TON	£15	138	15	0.03	2.5%	1323.1%	31.1%	10.8%	-4m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
M Winkworth	WINK	£25	197	15	0.46	3.4%	46.6%	-5.2%	15.9%	-	GBP	5	/Fwd EPS grth/Debt/
Lok'nStore	LOK	£218	735	29	0.48	1.8%	126.5%	9.3%	16.7%	54m	GBP	5	/Fwd EPS grth/Debt/
Character	CCT	£146	685	15	0.12	1.3%	143.9%	4.2%	15.1%	-33m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
Alumasc	ALU	£91	252	10	0.09	2.1%	185.1%	3.7%	15.3%	6m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/
Marshall Motor	MMH	£167	213	9	0.43	0.0%	25.7%	-13.3%	23.1%	71m	GBP	5	/Fwd EPS grth/Hi RoE or Marg/

Source: FactSet, 2 August 2021

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