The Intelligent Investor Summary

The Addicted Reader

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Before reviewing the summary of the book, it is important to know the author.

The Intelligent Investor was written by Benjamin Graham which is known as the father of value investing.

However, what I and most of you will find interesting is the fact that he was Warren Buffet's mentor, which gives you some insight into the thought process behind Buffet's stock picking.

The last time Benjamin Graham revised his book was in 1973.

Although old, his teachings are eternal.

Graham's view of Value Investing

In his book, Graham puts a lot of emphasis on the fact that speculating is a loser game. He believes that investing is accomplished by a thorough analysis and having only expectations of adequate return.

With that in mind, if you want to speculate, limit yourself to 10%.

Moreover, Benjamin Graham, knows that everyone does not have the same objective and risk tolerance so he categorized investors into two groups.

The Enterprising Investor and the Defensive Investor.

Returns being the the cornerstone for both of these categories, Graham says that inflation should be one of your concerns.

To protect yourself against it, he suggests owning a house or investing in a precious metal fund.

Also, he does not believe in the motto that the past predicts the future, so you should not give too much weight to the past in your analysis.

One of the most important topics in the book is his portfolio allocation policy.

In the Intelligent Investor we can read:

“We have suggested as a fundamental guiding rule that the investor should never have less than 25 percent or more than 75 percent of his funds in common stocks, with a consequent inverse of between 75 percent and 25 percent in bonds. There is an implication here that the standard division should be an equal one or 50-50, between two major investment mediums. Furthermore, a truly conservative investor will be satisfied with the gains shown on half his portfolio in a rising market, while in a severe decline he may derive much solace from reflecting how much better off he is than many of his more venturesome friends.“

The paragraph will be of great help for you in building your portfolio.

The Defensive Investor

It is stated that for the passive investor, the above portfolio allocation should be followed.

Here are the rules that a defensive investor must follow when selecting their securities:

1. The company must be of adequate size:
   Graham says that all minimum numbers in his book are arbitrary and especially with regard to the required size.

   The idea must be to exclude small-cap stocks.

2. The company must have a solid financial position:
   This means that the current assets must be at least twice as much as the current liabilities and whose long-term debt does not exceed working capital. For utilities, debt should not exceed double equity (at book value).

3. Stability in profits: The company should have profits for the last 10 years, however small.
4. Payment of dividends uninterrupted for at least the past 20 years.
5. A minimum increase of at least one-third in earnings per share over the past 10 years using three-year averages at the start and end.
6. The current price should not exceed 15 times the average profit of the last three years
7. A moderate market value to book value ratio: That is, no more than 1.5 times.

The Enterprising Investor

Investors who want to outperform defensive investors return need to spend more time on the task and take additional risks.

The Intelligent Investor states that if you only want to do it part-time then you should follow defensive investor rules of selection.

According to him, being aggressive they have more liberty so there is actually no ideal pattern to follow.

However, it does provide some guidelines.

1. **Strong financial condition:** Current assets at least 1.5 times current liabilities and debt not more than 110% of net current assets (for industrial companies)
2. **Income stability:** no deficit over the past five years
3. **Dividend balance:** Some current dividend
4. **Profit growth:** The profits of the previous year must be higher than those of 2007
5. **Price:** less than 120% of net tangible assets

Additionally, if you want to be sure that you are paying a fair price for a stock, you should also consider these points:

- **The company's "General long-term prospects":**
  At least 5 years of annual reports should be gathered to find evidence to help you answer two overriding questions:
  -What makes this company grow
  -Where do (and where will) its profits come from?

- **The quality of its management:**
  -Do they accomplish their projections? Read past annual reports to see. Do they walk their talk? If not, what is the reasons?

- **Its financial strength and capital structure:**
  – A company should generate more cash than it consumes. See whether cash from operations has grown steadily throughout the past 10 years. It's good if company earnings per share have grown at a steady average of at least 6% or 7% over the past 10 years

  -Look at the debts, long-term debts should be under 50% of total capital.

- **Its dividend record:**
  An uninterrupted record of dividend payments going back to the last 20 years or more is an important plus factor in the company's quality rating.

- **Its current dividend rate:**
  There should be a standard dividend payout policy if there is none, there should be justifications

Final note

Graham gives a warning that whatever technique you use, the important thing is that:

1. You are disciplined, consistent, and refuse to change your approach even when it is not in fashion.
2. Think a lot about what you do and how you do it, but pay very little attention to what the market is doing