

One concept that value investors keep in mind is that a good *company* is not necessarily the same as a good *investment*. An established firm with high revenue levels and a stable, strong earnings record, for instance, certainly sounds like a good company. But like any company, that firm only represents a good investment if it can be purchased at a favorable price.

Take Cisco Systems as an example. In April 2000, Cisco qualified as a good company by many popular standards. As a supplier of data networking products for the Internet, the firm was logging strong sales and demonstrating real earnings power, as well. In 1999, Cisco posted \$15 billion in revenue and \$2.5 billion in net income. Even as many technology companies were fading fast, Cisco's dominant market share in an important industry meant the firm's future prospects were bright.

Despite its strengths as a company, however, most value investors stopped short of calling Cisco a good investment. The firm's stock price translated into an astronomical market capitalization of more than \$465 billion – nearly half a *trillion* dollars! This figure dwarfed Cisco's revenue and earnings numbers, an indication that shareholders were counting on tremendous long-term growth from the company in the years ahead. If this growth failed to materialize, Cisco's market value faced the risk of substantial declines.

As a result, most value investors avoided Cisco and looked for stocks with prices that were less dependent on extremely high expectations. Such opportunities were widely available in April 2000. The table below lists 16 established companies with a combined market capitalization of less than \$465 billion. These firms – which include established businesses such as FedEx, Texaco, and DuPont – had combined 1999 sales of \$405 billion and earnings of \$30.7 billion.

Company	Market Cap: 4/00*	1999 Revenues	1999 Earnings
	All Numbers in U.S. \$ Billions		
Cisco Systems	\$468.0	\$15.0	\$2.5
Ford	\$65.8	\$162.6	\$7.2
Texaco	\$27.8	\$35.1	\$1.2
Merrill Lynch	\$37.6	\$34.9	\$2.6
DuPont	\$56.3	\$26.9	\$7.7
International Paper	\$16.4	\$24.6	\$0.2
Sara Lee	\$14.9	\$20.2	\$1.2
FedEx	\$11.0	\$17.4	\$0.6
McDonalds	\$44.0	\$13.3	\$2.0
Goodyear Tire & Rubber	\$4.5	\$12.9	\$0.2
JP Morgan	\$20.8	\$11.8	\$2.0
Anheuser Busch	\$30.6	\$11.7	\$1.4
Eli Lilly	\$82.6	\$9.9	\$2.7
Fox Entertainment	\$17.8	\$7.9	\$0.2
Consolidated Edison Hldg.	\$6.8	\$7.5	\$0.7
Apple Computer	\$20.6	\$6.8	\$0.6
Dow Jones	\$5.9	\$2.0	\$0.3
Total	\$463.4	\$405.3	\$30.7

*Source: Worldscope, as of 4/30/00

Effectively, investors could purchase slices of all 16 firms for the same price as an equivalent slice of Cisco and receive much more in terms of underlying sales and earnings. Accordingly, most value investors passed on Cisco shares. The firm qualified as a good company but not as a good investment.

Brandes, Charles. (2004). *Value Investing Today*. McGraw-Hill. p. 57-59.

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