When Is the Best Time to Buy a Stock?

Description

Warren Buffett's favourite holding period is forever. However, that doesn't mean that investors should just buy good stocks and then hold them forever.

All stock holdings should be monitored periodically — perhaps every quarter or every year. And if the story has changed, investors need to decide if they should hold or sell and move on.

What makes a buy-and-hold-forever stock?

Investors should have reasons to buy a stock. It could be that they like the stability of the business and that the stock was priced at a discounted valuation.

The big Canadian banks have been one of the most profitable groups of businesses in Canada available for the public to invest in. They also have a track record of increasing their profitability. Furthermore, the big banks are good at maintaining a payout ratio of about 50%, which leaves an ample margin of safety to keep the dividend safe.

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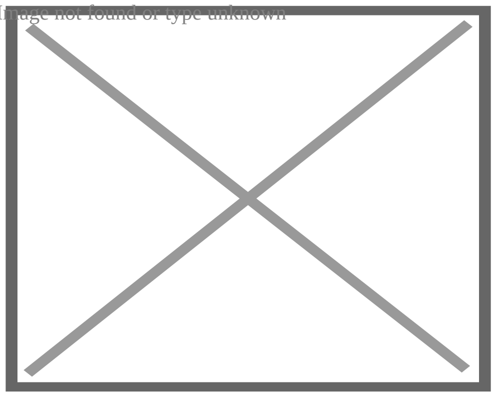

If you don't want to trade in and out of stocks, you can pretty much buy them at a good valuation and just sit on the shares and collect safe dividend income as one core part of your diversified portfolio.

In the first quarter of 2016, it was a great time to pick up shares of **Royal Bank of Canada** (TSX:RY)(NYSE:RY

). At the time, the leading bank traded at a price-to-earnings ratio of about 10.2 at roughly $69 per share. That was a discount valuation compared to its long-term normal multiple of about 12.3.

If you happened to have bought shares then, you could just hold on to the quality shares and collect dividends from them. From the $69 price, the yield on cost is nearly 5.3%. The dividend adds meaningful returns to the price appreciation of 46% to over $100 per share.

What stocks are not buy-and-hold-forever stocks?

Businesses that have above-average uncertainty should not be bought and held forever. An obvious one is oil and gas producers. **Peyto Exploration & Development Corp.** (TSX:PEY) is one of the most efficiently run gas producers in Canada, but if you look at its multi-year stock price chart, you'll understand why it shouldn't be a buy-and-hold-forever stock. Because of the reliance on commodity prices, Peyto's business performance and, subsequently, its share price can experience large up and down swings.

Investor takeaway

There's a commonality between buy-and-hold-forever stocks and stocks that are not. The risk is much lower, and the reward is much higher for investors if they buy the stocks when no one wants them.

Right now, Peyto seems to be closer to that reality than Royal Bank. That said, it's hard to call the bottom. So, investors who can stomach the volatility of Peyto might consider averaging in to a position over time, but don't expect a quick trade. Shareholders might need to wait a few years for Peyto's share price to recover to +$30.

CATEGORY

1. Bank Stocks
2. Dividend Stocks
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TICKERS GLOBAL

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2. TSX:PEY (Peyto Exploration & Development Corp)
3. TSX:RY (Royal Bank of Canada)

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