



Track a fading star

Directors' dealings can give you insight into a company's prospects, says Roger Montgomery

ONCE UPON A TIME JB HI-FI WAS a category killer: its returns on equity were stratospheric and unassisted by debt, and it was all reflected in a strong share price. But something has changed.

I wrote previously, and commented elsewhere, that JB Hi-Fi was maturing, that returns on equity were flattening and that the sun was setting on the ability of the business to reinvest profits at the very high returns of the past.

When business performance begins to mature, it's often worth watching what directors do with their shares for some further insights.

JB Hi-Fi's CEO, Richard Uechtritz, had been at the company for a decade before his retirement in 2010 and those watching his share dealings may have drawn a different conclusion from those being lulled by a bullish share price.

At the outset, let me say there is no impropriety in a director selling his shares and none is suggested here. Directors are free to sell shares within the bounds of their staff trading policy and are required to report their dealings to the market.

And it's through these announcements that the investor can see what directors are doing with their shares.

On August 20, 2009, JB Hi-Fi's CEO held 2 million shares and 627,315 options and he exercised options to buy another 180,048 shares at \$7.27. A week later, he had sold all the shares he had just purchased for an average price of \$17.65.

Then, between September 2 and 3, 2009, another 500,000 shares were sold at an average of \$18.22. By now JB Hi-Fi's CEO held 1.5 million shares and 447,267 options.

Another 174,656 options were granted on October 14, 2009, and then, in early Febru-



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ary 2010, JB Hi-Fi announced the retirement of Uechtritz. Having sold 680,048 shares in the seven months before the announcement, he sold another 500,000 shares during the first five days of March 2010 at an average price of \$19.74, leaving him with 1 million shares and 621,923 options.

In his final director's interest notice in May 2010, he listed his direct equity interest in the company at 1 million shares and the 621,923 options.

For investors who are interested in gaining a possible inside track on the prospects and potential of a business, it may be useful to watch directors' dealings in their shares.

Of course, sometimes the selling can mean nothing at all, but my tip is to watch the selling. If motivated by urgency, a desire to lock in lofty share prices or grim expectations, information about directors' selling can be more useful than watching their buying.

In April 2011, Uechtritz returned to JB Hi-Fi as a non-executive director. Until his return, he didn't have director's obligations so he was not obliged to make public any of

his private share dealings. Upon his return, however, he revealed that he owned only 421,000 options. In other words, he subsequently sold the 1 million shares he held at the time of his retirement.

JB Hi-Fi shares do not enjoy the lofty levels they once commanded and investors who tracked the sale of its shares by Uechtritz may have been prompted to look deeper into the company, its prospects or at least the impact of those prospects on its share price.

JB Hi-Fi's latest results were less than spectacular and, while it will continue to win the race with its listed peers, the reality is its margins remain under increasing pressure, it's losing share to the internet and its remaining store rollout plan is contributing to a maturing set of metrics.

Oh, and the share price now? Just \$11.18. Keep an eye on directors' share dealings.

Roger Montgomery is a portfolio manager at Montgomery Investment Management. For his book Value.Able, see www.rogermontgomery.com.