

Valuation Metrics



The price-earnings ratio (PE) is easy to understand and simple to calculate: It is merely price divided by earnings. It fails to directly take into account an imperative characteristic (we hope) of any stock—growth. It is, however, a measure of the market’s opinion of the company’s future prospects, including growth. From a pure price-earnings valuation standpoint, a stock that is trading at a price-earnings ratio of 10 is trading at a discount relative to a stock trading with a price-earnings ratio of 15.

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