

Oil, Patience, and Value Investing

Written by Rob Copeland

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Every investor's dream is a stock or bond that goes straight up and earns them a great return with zero stress.

But that's not how investing works: While good picks have rewarded investors handsomely, each and every one has involved some level of volatility.

Take Facebook, for example. When it went public in May of 2012 at \$42 per share, most investors thought it was a cant-miss investment. Over the following three months, however, it plummeted to less than \$20 per share on fears that it was overvalued. Smart investors kept their nerve and held on to the stock. And they were rewarded for their patience: Facebook now trades above \$74 per share, a 76% total return!

Buying low and selling high is what value investing is all about. But it does involve volatility, and it requires patience and a strong stomach. Right now, oil and energy are testing many investors' patience. These companies have run into trouble as oil prices have plunged.

But it's precisely the sort of volatility that we're seeing in the oil and oil services sectors that can create great opportunities. Right now, it's possible to identify great companies whose stocks and bonds are "on sale" because the markets are negative on the whole industry. And because bond prices have fallen, very strong yields are available.

Investing in oil-related companies' debt is a bet that oil won't fall dramatically lower and stay there for an extended period. Given oil's plunge in the past few months, it's easy to be pessimistic. But, although I cannot see the future, I do know that oil is a finite resource. When demand for oil increases to overtake supply, I believe oil prices will go up.

That will lift stock and bond prices on these beaten-down securities. And it will help to ensure that solid companies do well enough to repay the interest and principal on their bonds. The key is to invest in companies that are strong enough to make it through the next several years even with oil prices at or below our current levels.

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Are the prices of oil-related stocks and bonds at their bottom? It's hard to say, and it's nearly impossible to buy any investment exactly at its bottom. But you don't need to identify an investment's bottom to make money in the long run. In the case of stocks, you simply need to make a case that it will go higher over time. For bonds, you have to determine that the company will be strong enough to keep paying interest and then repay the principal upon maturity.

And then you need do one of the hardest but most profitable things in investing: Exercise patience.