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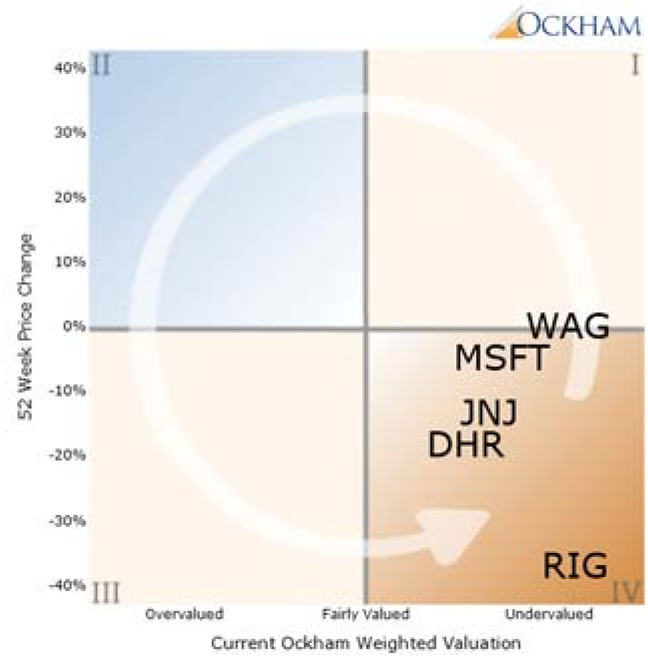
5 Blue Chips Fit For Ben Graham

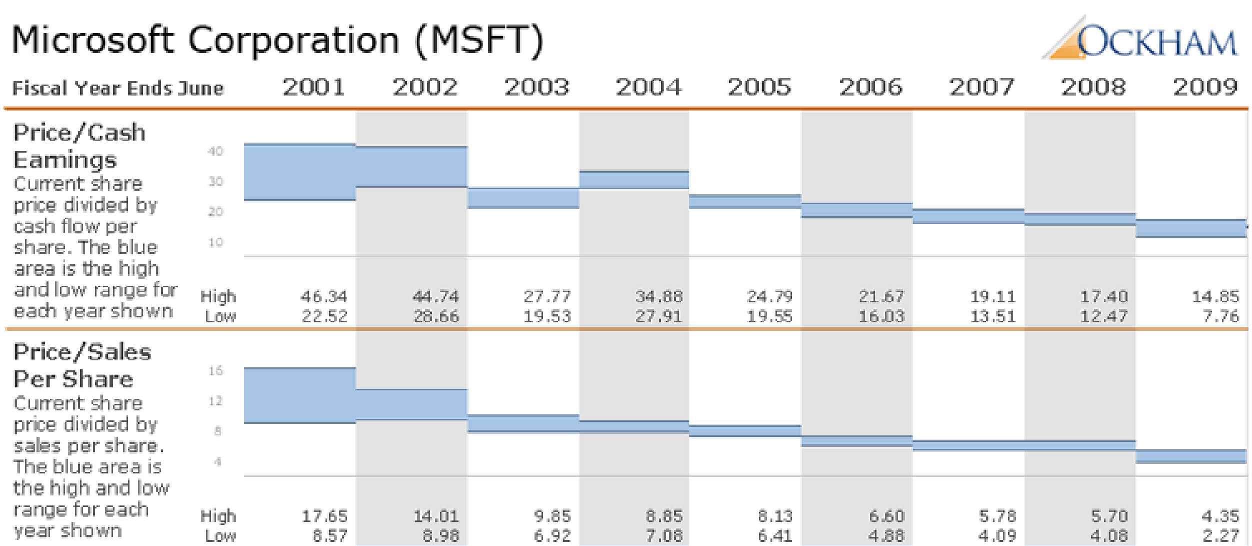
Looking at large cap stocks, we have determined five that we believe have a great margin of safety for an uncertain environment. Each one is currently trading well below their historical price-to-cash earnings and price-to sales ranges over the last ten years. This tells us that they have currently fallen out of favor and the market is not valuing them as richly as it has in the past.



The teachings of Ben Graham have been applied to investment theory for decades and have proven their worth. Recently, the market has seen terrific growth and margin expansion over the last few months, which makes it all the more important to make sure that you are not overpaying. Remember, as Ben Graham himself once said, "Price is what you pay; value is what you get."

Microsoft (MSFT)

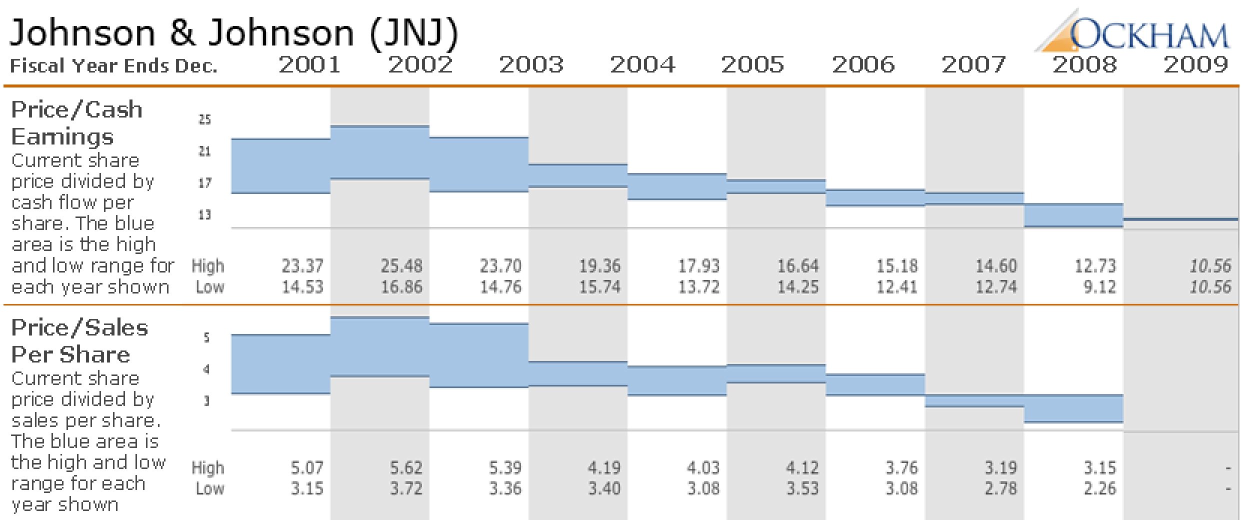
Microsoft meets many of the typical Ben Graham criteria. It is selling for a reasonable multiple of just a shade over 14x earnings. Microsoft's earnings have shown impressive resiliency to the downturn, and they have established a trend of growing EPS (diluted) of about 16.5% per year over the last five. This is more than five times better than the minimum earnings growth allowable under Graham. Microsoft continues to grow dividends on schedule. Furthermore, Microsoft remains one of only a handful of stocks that has retained its AAA credit rating, and in May MSFT tapped the debt market for the first time in years. With more than $31 billion in cash on hand, the company has the flexibility to be more aggressive in the lead up to launch of its Windows 7 operating system.



Fiscal Year Ends June		2001	2002	2003	2004	2005	2006	2007	2008	2009
Price/Cash Earnings Current share price divided by cash flow per share. The blue area is the high and low range for each year shown	High	46.34	44.74	27.77	34.88	24.79	21.67	19.11	17.40	14.85
	Low	22.52	28.66	19.53	27.91	19.55	16.03	13.51	12.47	7.76
Price/Sales Per Share Current share price divided by sales per share. The blue area is the high and low range for each year shown	High	17.65	14.01	9.85	8.85	8.13	6.60	5.78	5.70	4.35
	Low	8.57	8.98	6.92	7.08	6.41	4.88	4.09	4.08	2.27

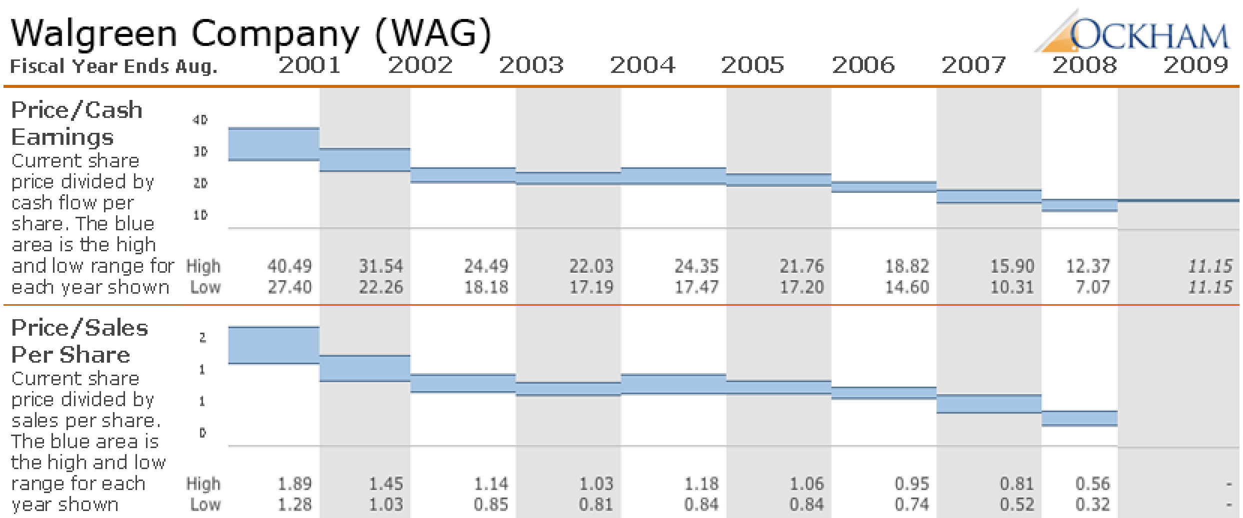
Johnson & Johnson (JNJ)

One of the best managed companies in the world, Johnson & Johnson is as consistent a stock as you will find. At Ockham, we view Return on Equity as a way to measure management performance, and JNJ achieves a very impressive 25% or better with regularity. Johnson & Johnson shares some similarities with Microsoft, it is also one of the most credit-worthy companies in the world according to the ratings agencies. Surely, Graham would have found no trouble in the balance sheet. As far as valuation, it sells at just over 13x earnings. EPS has grown at about 13.5% on average over the last five years. Earnings growth has cooled during the recession, but in comparison to the rest of the market, flat is acceptable. As you would expect, Johnson & Johnson has increased its payout to shareholders on a regular yearly schedule. Also, there is less risk in this stock than in a typical drug maker, as they also have the steady consumer products division as well.



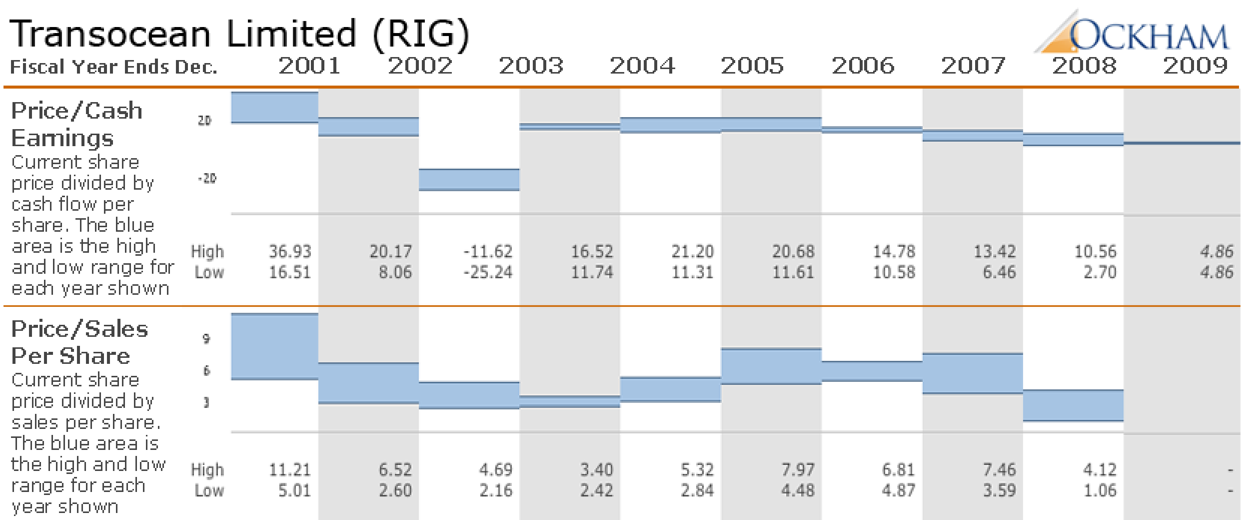
Walgreen Company (WAG)

Walgreen's aggressively expanded its network of drug-stores leading to impressive revenue growth of 12% per year for the last five years. That growth strategy has understandably slowed over the last year, but we think that strategy has put it in a solid competitive position. Walgreen's sells for a slightly richer P/E multiple than we would or Graham would prefer at about 15.5x. However, earnings growth of 9.1% on average over the years will dampen doubts about its valuation. The company has a strong balance sheet with a current ratio of 1.75 as of the last reporting, which has improved for the last two quarters. Still this is not quite where Graham would have liked it, with a current ratio of two being his rule. What is perhaps most impressive about Walgreen's is their streak of 34-straight years of increasing dividends. This is in addition to the impressive growth during that time, a feat of management spanning a few decades.



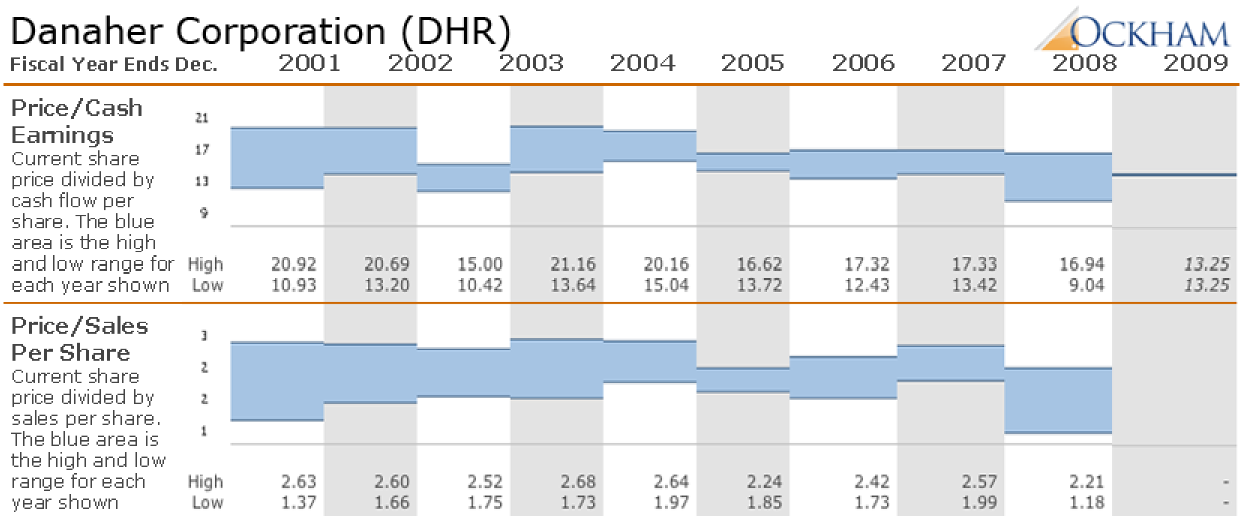
Transocean LTD. (RIG)

Transocean being one of the predominant deep-water drilling operators is of course directly tied to the price of crude oil. The company is selling for a ridiculous 5.2x last fiscal year's earnings, but that year was affected by record oil prices. Using the forward looking earnings multiple, it is still only selling for 6.2x. This is extremely attractive, especially considering the explosive growth of RIG in the last five years. Revenue has nearly quadrupled in that time, and profits have grown at an even more impressive pace. For a business as capital intensive as this, it is not surprising to see long term debt on their balance sheet, but it is not so much as to cause worry. One thing to be aware of, this stock does not pay a dividend as management would rather reinvest and grow. This is a strike against it for a Graham investor, but we believe the valuation is compelling enough to overcome. Unless you think the price of oil is going to crater over the next few years, we think that RIG has very attractive value. It currently sells for 1.45x book value of $51.69 per share.



Danaher Corp. (DHR)

Danaher is conglomerate that manufactures high-tech equipment for a variety of industries. The stock is currently selling for just above 15x last year's profit. Danaher is one of the rare companies that anticipated a contraction and the U.S. economy and worked to diversify itself and now claims half of its sales outside the U.S. This has lessened the effect of the recession significantly, although not completely. They have grown sales at about 19% over the last five years coming into this fiscal year; growth has largely come from savvy acquisitions. Earnings per share have kept up with that sales growth at a pace of 18.5% per year. The company shifted strategically in the early part of the decade to slash its dividend, which has enabled them to focus on growth through acquisition. As a byproduct of this strategy, there are no major debt concerns on the balance sheet. At the same time, no one will be impressed by the small dividend yield, even as it slowly climbs.



Ockham Research is an independent equity research firm based in Roswell, Ga. Using a methodology derived from the philosophy of Ben Graham, Ockham uses a value investing approach to cover more than 5000 stocks and ADRs. In addition to equity reports, Ockham also features news and sentiment analytics tools, a portfolio analyzer, and a weekly newsletter called The Enterprising Investor's Guide. [Click here for subscription information for both professional and individual investors](#).