

What is a Signature PE

The *price/earnings ratio* or P/E is a value calculated by dividing the price of a share of corporate stock by its underlying company's earnings per share—the amount of its profit allocated to each share of its stock.

This value is important because it reflects the important relationship between the profitability of a company and the value placed on it by its investors or owners. As with the price per gallon of gasoline, or the price per pound of coffee, the price per dollar earned for a company's owners is a unit value without which any measurement of actual value is impossible. (How can one compare the cost of two tanks of gas without knowing how many gallons each contains?)

Without such a unit cost, it's impossible to determine whether the current price being charged for a commodity is high or low, compared with its traditional cost. We certainly were aware of how high the price of gasoline has climbed, in view of our experience over time and the average cost over a long period.

A "signature P/E" is a device that performs the same function for shares of a company's stock. It's nothing more than the historical mean or mid-point about which one would consider the price paid for a dollar's earnings per share high or low. Some use the five-year trailing average PE; I prefer the ten-year trailing median. Either is close enough.

Depending upon the industry, and the company's rank in that industry, that signature PE will remain pretty steady over time, with the price growing as earnings grow.