13. Bear-proofing - low 'beta' stocks

This section of the course covers ways of protecting your capital against a bear market while still continuing to invest in shares as normal. First, we look at low beta stocks.

A 'beta' number is specific to an individual stock. It is calculated by comparing the day-by-day percentage changes in the price of a share with those of the market on the same days.

Betas generally vary between **zero and two**. The beta of the market as a whole is, by definition, 1. What beta essentially means is that based on past history, for any given movement in the market, the price of the shares will on average respond by a magnitude equivalent to its beta.

Stocks with betas of **less than 1** tend on average to move by a smaller percentage than any given movement in the market, and vice versa for high betas. Say a stock has a beta of 0.5. If the market gains 10%, it will tend to gain 5%. If the market falls by 10%, the stock will generally fall by around 5%.

Assume you wish to remain invested in shares, and the market is in a sustained bear phase. Logic suggests you should invest in stocks with a low beta, since these will fall least. In other words, beta is a measure of the likely volatility of the shares relative to the volatility of the market.

Betas are published regularly by organisation such as London Business School and available on some leading investment software packages and statistical services.

Even among large stocks betas vary considerably. In March 2006 the beta on these **top five UK companies** were as follows:

BP	1.46
Vodafone	1.07
AstraZeneca	0.97
HSBC	0.65
GlaxoSmithKline	0.54

So, BP was the most volatile of the 5, and GlaxoSmithKline the least.

Betas are not guarantees. They are based on historical data and cannot be assumed to have predictive value. But the odds are probably in favour of a stock with a low beta holding up better in a market decline than the market as a whole, and appreciably better than a stock with a high beta.