Google vs Grandma

Slide 1
Hi, My name is Chirag Rathod. In late 2013, I quit my job with Oracle India to take up equity investing as a full time career. In late 2015/early 2016 I created InvestR.co.in to help in discover companies worth investing. InvestR has more than 700 registered users.

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Why is this talk named "Google vs Grandma"? To answer that question we need to ask another question: "How are grandparents helpful to us?". One, raising grandkids! And two, guide us via their PERSONAL experience! When we twist an ankle or get a bad insect bite and we Google the symptom we get a ton of results. Some are extremely benign and some are extremely scary. But when we show our problem to our grandma, she will dig into her past experiences and mostly tell us, not to worry! And mostly we will be fine!

So, in a world where all of us have access to all the information that we desire. We have access to analyst reports, annual reports, books, Youtube lecture and interviews. **Why should you listen to me!?**

Just like our grandma, we all have a bunch of experiences … both good and bad. Profitable and loss making … and I feel you can benefit by knowing about mine! At the very least you can learn from my mistake and avoid making them … if you haven't already made them :-) To keep my thoughts as original as possible I have not looked up any books or Google for this talk.

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We will have a question and answer session at the end but during the talk if you feel a strong sense of dis-agreement with anything that I say then please feel free to interrupt me and we can have a quick clarification on it!

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I have divided this talk into 3 broad sections:

* Personal Investment Motos
* Buy/Sell Strategies
* Miscellaneous

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Personal Investment Motos

Over the years my personal investment motos has followed the Goldylocks and the 3 Bears story.

Too hot at one stage, too cold at some other stage and just right as of now!

Number of Companies Held

When I started direct equity investing in early 2008 (before that I had been a MF investor for 5 years), yes at the close to the top, I ended up holding 55 stocks over the next 12 months! Apart from the fact that I was a novice, the large number of stocks just showed that I was not confident in any of my picks. And I was just trying to reduce my risk by spreading it between as many stocks as I can. And as a result my returns were also diluted. I would have done been just buying NIFTY ETF. So that was definitely a wrong move.

At the other end in the 2013-2014-2015 period I held 3 to 4 stocks! While the portfolio returns were great, more than half of credit should be given to luck, I was always uneasy and tensed up before the quarterly results. I was like a kid before his board exam results. And my results would come 4 times a year. It was clear that a concentrated portfolio was not something that worked for me.

Then I decided that my portfolio should not be dependent of 1 single company and decided to hold 20 companies. I try to **maintain my exposure in 1 company between 5% to 10%**. And it has worked out well for me!

Diversification

Initially I did not pay minute attention to either diversification in either market cap or sectors. Now I make sure that I am **diversified 33-33-33 percent in LC-MC-SC companies.**

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Basic characteristics of the companies that I prefer to invest in

* **BUY COMPANIES THAT ARE MAKING/SELLING STUFF/SERVICE WITH LESS/NO DEBT AND MAKING GOOD PROFIT MARGINS AS A RESULT**
* **BUY COMPANIES THAT ARE MAKING/SELLING MORE STUFF/ SERVICE AND INCREASING THE PROFIT MARGIN WITHOUT INCREASING DEBT**

Just following these 2 rules help me eliminate 80% of the companies.

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I also make sure I hold atleast 6 sectors. Financials (Banks, NBFC, Housing Finance, Micro Finance), Auto, IT, Pharma.

I avoid companies that don't pay any dividend. When I start investing I prefer companies with a dividend yield great than 1.5.

I avoid companies that have a net profit margin less than 8%.

I avoid companies that pay more than 4% of their net revenues as interest.

I avoid companies whole PE is greater than (or closer to) its average higher PE bank.

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I **avoid companies that deal with commodities** as I don't understand how they work. So I don't buy metal companies and oil related companies.

I **avoid real estate and construction companies** as I feel they are into creative accounting. I would like to invest in cement companies as a proxy but I am not able to get a grip on their cycle.

I **avoid companies with fluctuating quarterly results**. And even companies that have 1 or two important quarters where 80% of their earnings are loaded. Which means I would not buy an Umbrella company. E.g. Navneet or Talwarkars or Fertilizer companies

I **avoid companies with complex PL statements and Balance Sheets.** Just compare the PL statement of a Tata Motors or Tata Steel with a HDFC Bank or Bata and you will see what I am talking about!

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Essentially I **hold companies that help me sleep well at night.** I don't do anything that makings me think about my holding at night. I don't buy companies because Porinju and Tulsian suggested it. I don't buy companies because Dolly Khanna or Rakesh Junjunwal bought it. I don't buy because my best friend holds it. I buy companies after filtering the companies thru my personal motos. I buy companies because I am at peace holding them. In fact I have observed that the TV channels and experts start discussing a company only after the first huge rally in a stock is over! So if you think you are holding an undervalued gem, then don't feel bad that it is not being discussed on the news media!

And we cannot be part of all the parties! So I try to be happy with what I am holding!

One thing that has not changed for the years is that **I have alway bought a company in small chunks — on either price/valuation correction or time correction**.

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Knowing Personal Limitations

Knowing personal limitation is as important as knowing the strengths. I don't trade F&O as I know that I don't have the temperament for it. Open F&O positions keep me awake and night and that defeats the whole purpose of not working!

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Buy/Sell/Hold strategics/execution

Buying:
All of us follow a system. Most of the times it is a mental system. We have a mental calculation about our diversification (both for market cap and sectors). We look at a companies name, market cap, sector, what it sells, its balance sheet, cash flow, profit loss statement etc and decide if it is worth investing. While looking at these numbers we will also calculate rough growth numbers. We might also take services of some 3rd party services that will give us this information in more digestible form. My point is this system is in our heads. We do mental calculations and sometime we will round off numbers bases on our biases. This leads to inaccuracies. This mental system also limits our bounds while comparing two companies within same or different sectors.

Over the last many years I have realized that it is better to create a system that tracks and displays these things. Why load the brain with things that can be easily and more importantly precisely calculate via a spread sheet or the database.

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(IMAGE/SPREADSHEET: SECTOR DIVERSIFICATION MATRIX)

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(IMAGE/SPREADSHEET: MARKET CAP DIVERSIFICATION CHART)

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(IMAGE/SPREADSHEET: INVESTR.CO.IN)

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Long a go a close friend of mine had asked me: "What return do you expect from a company X?" I had replied: "Maximum or as much as possible." Now I know who wrong I was. **It is important to decide the return expectation from an investment (for a time frame) while buying it.** This estimate will generally be based on the growth. That way we will know if the company is performing to our expectations and it will also keep disappoints at bay! This becomes especially important while buying companies from sectors that are current out of market's favor (e.g. IT/Pharma). On the topic of contra buys, I believe that contra buys should be done only in sector leaders. As they will be able to weather the storm better than the tail-enders.

I like it the company's dividend yield is greater than its PEG. It is one matrix that combines the fundamentals and valuations in a simple comparison.

And once I decide to invest in a company I will wait for the price to fall below its 30 DMA. This means that I will not be buying the company at its tops. Again these things may not matter in a larger scheme of things but this is something that has worked for me, so I follow it.

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Holding:

Once I invest in the company, I don't let the stagnant stock price bother me if the company is showing consistent growth as per my expectations. If the growth continues then the stock price will catch up soon or later.

If the company underperforms for one quarter then I will give it one more chance. But if it underperforms for a second quarter in a row than I will generally have a relook at it.

Does this company give me joy? (The Life Changing Magic of Tidying Up)

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Selling:
For me there are 5 reasons to sell/book-profits:
* When I need money
* When the stock that I hold has become overvalued (I year f/w PE has become greater than its all time high PE)
* When the company comes out with results that were not expected
* When I find a better company (fundamentally and valuations wise)
* Company or its management is in negative news

I feel that, selling and holding cash amounts to timing the markets and I am not very good at that as a result I am fully invested at all times.

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3:15pm

As I am fully invested at all times, I need to sell something to buy something else. Over the years I have observed that on down day stocks are at their days lows or close to it after 3:15pm. This is because the brokerages automatically close the open positions of day traders. This increases the volatility around this time and the buyers end up getting a slightly better deal. So I will generally sell in the mornings and buy after 3:15.

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Accurate Tracking

[INSERT SPREADHEET TRACKING/GOOGLE CHART INVESTR TRACKING]

Accurate tracking of the portfolio is the most important aspect of equity investing. Eventually that helps me decide wether I should continue doing what I am doing or buy Mutual funds or ETFs instead.

I have been entering the daily moves of my portfolio for the last 3 and half years. And it has been a life changing experience. I can find how I performed on weekly, monthly, quarterly, yearly basis and compare these values with the known indices.

Miscellaneous

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Question 1: How long is long term?

Short answer is 3 years!
[INSERT 20 YEAR NIFTY CHART]

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Searching for multi baggers

Multi baggers are like these shells that you find of the beach. Most of us don't go to the beach to collect shells. We go to enjoy the sea but once in a while will end up finding this beautiful shell.

But we can try to create the odd, by buying companies with low PE and good growth. If we discover a company with a less than 300 crores market cap that is consistently growing at 30% and has a PE of 10. There is change of PE expansion and if the growth continues to be at 25% 30% during the PE expansion phase then we will have a multi bagger in the making.

Sadly, such companies during their initial phase will have low volumes and hardly any news flow. So one needs to have a very high conviction in holding them.

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Question 3: Sector Rotation

[INSERT SECTOR ROTATION CHART HERE]

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Question 4: Should I buy now?

[INSERT NIFTY EARNING, PE, NIFTY NORMALIZED CHART HERE]

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Stuff that I could not cover

I would have loved to talk about the psychological aspects that affect investing. Essentially stuff from the Black Swan and thinking fast and slow. But that would have required more time and me looking up stuff. So maybe there will be a next time!