



Toughest Investing Decision: SELLING







**Presented by
Bob Houle**

Director, North Florida Chapter


Proud RM for the Northwest Buckeye Chapter






Celebrate SELLING !!

Winners Know How to Sell








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What We're Going to Cover

What Are We Really Doing When We Buy a Stock?

<p>Why is Selling a Stock More Complicated than Buying a Stock?</p> <p>Are Buy & Sell Judgments Different?</p> <p>Why Sell a Stock We Own?</p> <p>How Do We Know When to Sell a Stock?</p>	<p>Sell Signals <u>ON</u> the SSG</p>	<p>Sell Signals <u>NOT ON</u> the SSG</p>
	<p><u>Not Sell Signals</u></p>	<p><u>Bad Reasons for Keeping a Stock</u></p>

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When We Buy A Stock

We're taking an ownership position in a company that we highly regard and we're adding it to our existing portfolio of owned companies because we believe:

- It has high quality growth potential, and
- We're confident that management can continue to deliver this performance, and
- That, when added to our existing portfolio, it will contribute to the portfolio achieving our
 - target rate of return ...
 - ... at an acceptable level of risk

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Why Do We Buy Stocks?

We buy stocks to **SELL** them in the future at a profit

- We are **NOT COLLECTORS**
- We are **SELLERS**

HOLDING is a buying decision

SELLING is a reversible decision

SELLING is about locking in your gains

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Buy and Hold -- *bad advice*

Wrong attitude since "Hold" is often "Hope"

Buy and Hope is not a useful investment strategy:

- "Hope" shields our ego
- It often damages our wealth
- At best, "hope" prevents considering potentially better opportunities

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Buy, Don't Hold




"Should you find yourself in a chronically leaking boat, energy devoted to changing vessels is likely to be more productive than energy devoted to patching leaks."

- Warren Buffet

Always strive to be a SMART SELLER

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 **Buying** requires us to make judgments on:

Company expectations


- Growth rates (sales, profits, earnings)
- Operating metrics (margins, taxes, leverage, capitalization, payouts)
- Management performance (did they do it? can they do again? can they be trusted to act on our behalf?)

External factors

- Industry expectations
- Market expectations
- Competitor expectations
- Regulatory expectations, etc, etc




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 **Selling Is More Complex Than Buying**

Selling a stock requires us to:

- **Re-assess our current stock holding expectations**
 - Why did we buy it?
 - What did we expect it to do?
 - What did it do?
 - Why are we considering selling it?


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 **Selling Is More Complex Than Buying**


Selling a stock requires us to:

- **Re-assess our current stock holding**
 - Why did we buy it?
 - Why are we considering selling it?
- **Deal with the human emotions associated with selling**
 - Accept that our initial judgment was wrong
 - Learn from our “mistakes”
 - Apply the lessons learned to a new buy

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 **When we consider selling we're often confronted with the reality that ...**

The company isn't performing as I projected so ...



- ... I must have made a mistake in buying it
- ... because my analysis was faulty
- ... and I should have known better
- ... and more guilt trip stuff


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 **Selling Is More Complex Than Buying**

Selling a stock requires us to:


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 - Why did we buy it?
 - Why are we considering selling it?
- **Deal with the human emotions associated with selling**
 - Accept that our initial judgment was wrong
 - Learn from our “mistakes”
 - Apply the lessons learned to a new buy
- **Buy a replacement stock**
 - The cycle repeats

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 **So, Why Sell a Stock We Own?**

Only three reasons to sell:

- We need the money

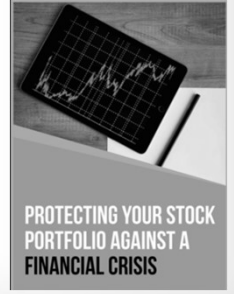


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 **So, Why Sell a Stock We Own?**

Only three reasons to sell:

- We need the money
- We need to protect the portfolio from harm




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 **So, Why Sell a Stock We Own?**

Only three reasons to sell:

- We need the money
- We need to protect the portfolio from harm
- We want to improve the portfolio



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Why Buy?		Why Sell?
We bought because <u>ALL</u> of these were true		
We had extra money to invest		
We found a high quality growth company that was an industry leader		
Based on our SSG judgments, the price of the stock suggested the potential return was adequate ...		
... and that the potential for loss was acceptable		

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Why Buy?		Why Sell?
We bought because <u>ALL</u> of these were true		We sell because <u>ANY</u> of these are true
We had extra money to invest		We want or need the money
We found a high quality growth company that was an industry leader		The quality (fundamentals) has serious problems.
Based on our SSG judgments, the price of the stock suggested the potential return was adequate ...		Replacing a stock would improve the quality or potential of our portfolio.
... and that the potential for loss was acceptable		It is grossly overvalued with little remaining upside potential.

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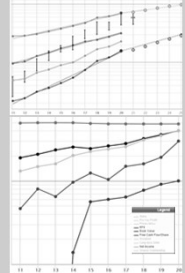
When to Consider Selling?		
We NEED the Money	PROTECT Portfolio (Defense = Quality Issue)	IMPROVE Portfolio (Offense = Valuation Issue)
When the need arises subject to tax and other considerations	This is an <u>urgent</u> process that needs to be done every quarter as new fundamental data is made available: <ul style="list-style-type: none"> based on quarterly SEC reports <u>not</u> driven by price or cost considerations <u>not</u> driven by market gossip 	While this is an <u>important</u> process it can be done anytime: <ul style="list-style-type: none"> Current price is a driver, but <u>only</u> for those high quality stocks that passed the Defense screen This is a valuation issue only (quality was already considered by successfully clearing the DEFENSE screen)

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How Do We Know We Need to Sell?		
We NEED the Money	PROTECT Portfolio (Defense = Quality Issue)	IMPROVE Portfolio (Offense = Valuation Issue)
The need arises external to the investing process: <ul style="list-style-type: none"> Personal: buy home, college, travel, retirement income, harvest tax loss, etc Club: club withdrawal cash out 	<ul style="list-style-type: none"> Fundamentals not living up to our expectations, or A threatening trend in the fundamentals <p>Note:</p> <ul style="list-style-type: none"> - Can only be done quarterly - It has nothing to do with stock's current price - It has absolutely nothing to do with how much we paid for the stock 	<ul style="list-style-type: none"> Company's stock price is so high that there is insufficient future return potential Other companies offer better investment opportunities are available Portfolio diversification is seriously out of balance <p>Note: Can be done anytime, driven by current price. This only applies to companies that <u>passed</u> the Defense screen</p>

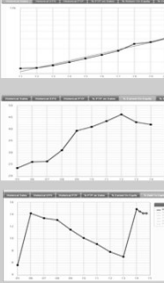
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Sell Signals ON the SSG

SSG ^{PLUS} Section	BUY Factors	SELL Factors
QUALITY ANALYSIS: (Growth) 	Primary growth rates (sales, pre-tax profits, and EPS growth) increasing steadily at an acceptable rate.	Growth slows to an unacceptable rate.
	Growth is consistent.	Growth is erratic.
	Sales and EPS growing at a similar rate.	EPS grows much slower or faster than sales.
	Most recent quarter is equal or better than the historical and projected growth rates.	The most recent quarter is significantly less than the historical and projected growth rates
Confirming growth rates are consistent with primary metrics and each other	* Net income is going down while EPS is steady or rising * Free cash flow is diverging from net income * Book value is diverging from free cash flow	

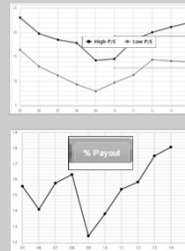
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Sell Signals ON the SSG (cont'd)

SSG ^{PLUS} Section	BUY Factors	SELL Factors
QUALITY ANALYSIS (Management) 	Profit margin and ROE are stable or trend steadily upward.	Profit margin or ROE trend downward.
	Profit margin and ROE are above the industry average.	Profit margin and ROE are significantly below the industry average.
	Debt/Equity: no or low debt; debt declining from low level	Debt/Equity: high, increasing, well above historical levels for company and/or industry



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Sell Signals ON the SSG (cont'd)

SSG ^{PLUS} Section	BUY Factors	SELL Factors
VALUATION 	Historical High & Low P/Es appear reasonable and predictable. Very few, if any outliers. Current P/E is within bounds	Current P/E is well outside historical envelope (Relative Value) Lot's of data points that just don't fit
	Payout ratio is stable or increasing slightly and is low enough to leave earnings to fund growth.	The payout ratio is decreasing due to dividend cuts. The dividend payout is increasing faster than earnings, thus lowering the future EPS growth rate.
	The payout ratio can decrease if it is due to increasing earnings and stable dividends.	Dividend is cut

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Sell Signals ON the SSG (cont'd)

SSG ^{PLUS} Section	BUY Factors	SELL Factors
RISK ASSESSMENT 	The Relative Value* is roughly between 85% and 150%	The Relative Value* is significantly more than 150% or is less than 80% due to company problems.
	The upside-downside ratio is greater than 3 to 1 (but below 10 to 1 or more)	The upside-downside ratio is less than 1 to 1.
5 YR POTENTIAL RETURN 	The total return meets or exceeds our target return for a company of that size	The total return and/or projected average return is significantly less than our target rate.

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SSG Conservative Decision Making

Being "Conservative" means different things when BUYING or SELLING

SSG ^{PLUS} Section	BUY Judgments
Driving Concerns:	Paying too much
Judgments:	Assume low growth rates
	Assume little if any PE expansion
	Assume there there may be further significant further downside price drops

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SSG Conservative Decision Making

Being "Conservative" means different things when BUYING or SELLING

SSG ^{PLUS} Section	BUY Judgments	SELL Judgments
Driving Concerns:	Paying too much	Selling too soon
Judgments:	Assume low growth rates	Project optimistic but still realistic growth rates
	Assume little if any PE expansion	Assume possibility of PE expansion
	Assume there there may be further significant further downside price drops	Assume future low price no lower than current price

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Sell Signals NOT ON the SSG

- An adverse management change (eg, CFO suddenly resigns)
- Non-boilerplate auditor's letter
- Financial results show problems or worse - signs of manipulation
- Weird footnotes on financial statements
- Balance sheet issues (rising debt; inventories and accounts receivable rising faster than sales; etc)
- Unchecked raw materials costs
- Key management changes or they're making bad decisions
- Funding for R&D downward
- The price drops below our estimated low on the SSG for no apparent reason
- The customer base is shrinking
- Competition is tougher
- Product pipeline deteriorating
- Uncertain product cycles

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What are NOT Sell Signals?

MAJOR POINT:
Once we own the stock the rationale for retention or selling should all be addressed in context with our portfolio risk and return requirements.

We need to:

- (1) **root out bad stuff** before it poisons the rest of our portfolio and
- (2) **continuously seek improvements** in our portfolio's quality and performance

Don't sell just because:

- the price hasn't moved
- the price has reached its target price
- of a paper loss or a paper profit
- of temporary bad news
- of analyst downgrades
- of insider selling
- everyone else is selling
- you want to do something

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What are **NOT** Good Reasons for **KEEPING** a Stock?

- we're emotionally attached to a company
- we hate to admit that we made a mistake
- we hate to take a loss
- we want to wait until the price rises back to our purchase price before selling
- we don't know how to take advantage of a loss for tax purposes (wash sales rules, emotions, buy again)
- we don't know how to restructure the portfolio to improve quality
- we don't want to pay taxes

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What to Do When Deciding to Sell

- Update not just the company SSG you are considering selling but all companies in your portfolio and on your watchlist -- *challenge!*
- Understand objectively why you are considering selling
- Except in extreme circumstances, such as to protect the portfolio from imminent harm, have a replacement identified

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The Bottom Line

Good Sales:

- Any sale that results in a gain is a good sale
- Any sale that results in a loss but is accompanied by an understanding of why that loss occurred

Bad Sales:

- When sale is driven by emotion (fear and greed) vs data & analysis
- When we don't learn from the "bad sale" (or "good sale")
- Not knowing how to sell (eg, minimize fees & taxes)

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Keys to a Great Portfolio

Don't fall in love with your stocks

Use (and trust) your SSG

Buy and Hold only if it makes sense

Don't be afraid to sell

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CAN YOU PASS THE ACID TEST ?

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The Acid Test

If I didn't own the stock, would I buy it at this price today?

If your answer is anything but YES! then it is time to start re-thinking your ownership position.

Be a Seller, not a Collector

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What We Now Know

OWNERS (not TRADERS) should drive our decision making process

Selling requires more from us than prudent buying We know that buying & selling are complementary, linked but different processes We know why we should and should not sell our ownership position in a company	Sell Signals ON the SSG	Sell Signals NOT ON the SSG
	Not Sell Signals	Bad Reasons for Keeping a Stock

We have checklists to help take the emotions out of selling

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The "6T" Key to Being a BetterInvestor

Through our participation in investment training we've demonstrated that we have the **TIME, TALENT** and **TEMPERAMENT** to potentially be a successful investor.

To realize our potential we need to master the **TOOLS** and **TECHNIQUES** available to us and that takes **TRAINING**.


The **BetterInvesting** world is all about **training** though a variety of venues.

If you want to be a better investor, take advantage of all that's offered to you.

If you REALLY want to be a better investor, join the rest of the Volunteers in the Chapter who receive additional training so they may be even better able to help you.

Be a Chapter Volunteer!

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 **The #1 Barrier to being a Good Seller**

Your Emotions

The antidote?

Have your supporting Chapter visit your club and conduct an impartial
Portfolio Review


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 **References**

This briefing is entirely based on the seminal work of leading NAIC/BI members, most notably:

- “Take Stock” by Ellis Traub
- “BI Stock Selection Handbook” by Bonnie Biafore
- “BI Using Portfolio Management Wisdom” by Bonnie Biafore
- “Toolkit 6 Manual” by ICLUBcentral
- “Stock Selling Guide” by Douglas Gerlach
- Considerations of Stock Sale
- BIwiki.editme.com (When to Sell)

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 **Questions or Comments?**

Bob Houle
bob.houle@gmail.com

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