IFB260: Which Companies Would You Use to Teach a Finance Class?

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Dave

0:00

Alright folks, welcome to Investing for Beginners Podcast. Today we have episode 262. Today, Andrew and I are going to discuss why you should buy boring businesses when you invest. This is a topic that probably doesn't come up a lot. And this is something that Andrew and I were chatting about off air and we thought it'd be might be kind of a fun conversation to talk about. When we think about investing.

Most of us think about exciting, sexy, glamorous, shiny objects, you think about all the new tech that comes out and, and everybody gets super excited about those kinds of companies, I think there's probably been more ink spilled or more audio spilled on a company like Tesla, for example. Then there has been on a company like Martin Marietta, for example. And some of you out there are probably going Martin Marietta who, and have never heard of this company.

And it's a fantastic business that's had great returns over the last several years, but nobody knows about it. And the market is full of those kinds of companies out there. These air quote, pick and shovel type businesses that really drive the economy and drive the industries that they're in, but people don't know about them, don't talk about them. It doesn't get appreciated. And I thought maybe we could talk a little bit about that today. So Andrew, what are your thoughts on buying boring businesses, and maybe why you should consider that as opposed to the shiny new object out there,

Andrew

1:25

I feel like I've been pounding the table on this so long that I'm probably the most biased person you'll ever ask. But boring is good, because it is predictable. And there's not much that can change for a lot of these businesses. So you don't have to worry if, for example, you're investing in Netflix, who was able to disrupt the cable industry, the cable TV industry, they disrupted it in like a breath that seems like and then you fast forward three, four years, and it seems like there may be getting disrupted by all these other alternatives that are popping up.

Sometimes when you have a boring business, that that took them like 30 years to, quote, unquote, disrupt, and grow into something big. Sometimes those businesses can continue for another 30 years, because for somebody to come up and replace them, they'll have to grow for decades to just to catch up. So it's almost like the thing that can kind of make people weary of it and be like this is boring, it's not growing as high that could actually be an asset, in the sense that it's just an industry where you have to build it slow and steady. And it takes time. So that investment could be safer.

Dave

2:39

Yeah, it could be safer. And there is a benefit in safety. And there is something to be said for the margin of safety, which we've talked about recently. And there's also the idea of not losing money and having the wherewithal to stay within the market. And sometimes one of the struggles for newer investors in particular, is they can't handle the volatility, they can't handle the ups and downs.

And when you're buying when you're investing in companies that could be disruptors, a lot of times, I think you're probably going to see a much greater degree of volatility in those than you will in something like a Walmart, for example, or progressive or Prudential, or some of these air, quote, boring businesses, because there isn't as much volatility in those businesses, there isn't as much ups and downs in the business. They aren't disrupting, they're more mature, they're more stable companies. And there's something to be said, for having those kinds of companies in your portfolio because they can act as a rock or an anchor, if you will, that can help.

Especially new investors see Oh, okay. All right. So this part of my portfolio is blowing up. But this one is just, you know, slow and steady, just getting the job done and doing well for me. And it can help. I think it can help keep people in the markets, instead of being discouraged by all the volatility, they may get from buying a company like Sofi, for example, and seeing all this volatility, or it's constantly down, even though the company does well and all its earnings reports. And everybody just want they lump them in with FinTech or banks, and those are bad.

And that can be very discouraging and hard for newer investors to stay in the market when they see all this volatility. And think about a couple years ago, when people were buying everything into the moon, you know, up into the right kind of idea. And how many of those companies are still successful today? Not a lot. And I would probably guess, without any hard facts here, but just thinking of human nature. A lot of the people that invested those companies that have lost majority of their investments have probably sold at a loss and are out of the market now, which is a shame. And so that's why I guess I'm advocating for boring businesses. So

Andrew

4:50

I do have a thought on okay, it makes it really difficult because it's really like the shiny objects you're talking about that explode up and then kind of fan out in a lot those end up to be failures, like you said, we've seen so many of them lose money. Well, it makes it so difficult. A lot of times, it's those shiny objects that get people to start investing in the first place. So you have this catch 22 of like, it's awesome that people find excitement from all of these ideas. And it's, I think it's better to be an investor than not being an investor. But hopefully at a certain point, you learn the difference between fun investing, and maybe smart or intelligent or prudent investing. And hopefully, along the way, you don't have too many scars in learning that lesson. And so hopefully, it's something that can be a message that's more shared.

Dave

5:41

Yeah, there needs to be a balance, you know, it's okay to buy the shiny object, if that gets you excited about being an investor, and you think it has the potential to do well. And there's nothing wrong with, you know, taking a flyer on that. But the whole goal of investing is to build our wealth. And it's not necessarily to get rich quick. And I think about this, I saw this quote a few times on Instagram, over the last few weeks, where Jeff Bezos is having a conversation with Warren Buffett, and he Jeff Bezos, I'm gonna paraphrase all this here. So keep that in mind.

But Jeff Bezos basically says Your ideas are so simple, and so effective. Why do you think more people don't adopt them? And Buffett says, because people are, are impatient, and they don't want to wait to get rich. And I think that kind of encapsulates, I guess the whole Buffett Munger approach is they're not they have never really gone after the shiny objects. And yes, he is an investor, a big investor in apple today. But you could argue that that's air quote, a boring company now, because the iPhone has been around for so long, that it's not really I'm not saying the apple is not innovative. So please don't take what I'm going to say as they're not innovative. But comparatively, they're not innovative.

They're really driving a new idea. No, it's never. Yeah, they keep reiterating it and keep improving it. Some people would argue not but they keep improving it. But it's not a new idea. Yes, that's exactly right. And one of the things I love about investing in a company like Berkshire Hathaway is that I get to partake in what Warren is buying. But I also get to partake of these boring businesses like utilities, electric generation, and, you know, insurance and retail, you know, Fruit of the Loom is by far not one of the more exciting companies, you know, Michael Jordan, ads aside, it's not an exciting business. But it certainly generate great returns for him over a long period of time, kind of the same idea with Dairy Queen, you know, it's it's a basic, simple business. But it's done really, really well over a long period of time.

And same with Geico, and some of these other businesses that he owns. And so when I own a company like Berkshire, it's really, really sexy because of Warren Buffett and Charlie Munger. If you take those two guys away, it's not a it's not an exciting business. And I think most people when they look at the actual business itself, oh, that's what it does. Yeah, that's what it does. And but it's done amazingly well over the last 60 years, like 20% returns over the last 20 to 60 years compared to 10% for the s&p. So I think that's I'd be okay with 20% returns over the next 60 years, if I can, you know, live to be 115, I guess. So. I'd be okay with that.

I think when you set out to invest, I think you should try to find the best companies that you can find they're going to generate your wealth for you over a long period of time. And I guess, what are your thoughts on that idea? Like, what do you think of when you're sitting down at the table or your desk to try to think about what am I going to pick for this month? You know, how does that what we're talking about? How does that kind of formulate the idea of like the pond that you're going to fish in, I guess,

Andrew

8:51

I'm a very numbers oriented person. I understand a lot of people are not that way. But I like to have filters that I use to kind of put myself in the box, I have the pond to find and it's become a pretty loose pond as I've gotten more experience and knowledge, but there's still a pond there. So by having that framework of filters I'm using it keeps me I don't have to think one second about do I want to buy zoom.

Do I want to buy peloton, a lot of the more expensive names are automatically excluded from my pond. And that saves me a lot of time. So I can spend more time on things that are more reasonably priced. That's that's really how I go about starting that process. But if I was in the new investor shoes, it literally can be as simple as the P E or price to earnings ratio. And you just start there because everything else kind of of is a more complex iteration of really the P E ratio. So you can literally start with something that is like you know what, for my first stock, I'm gonna find On the stock, that's a P E, lower than the s&p 500. Or maybe right around there, maybe a little bit above it. But maybe you start there.

And then out of that universe of stocks, you say, which business is most appealing? To me? Which one can I see myself have fun learning, and getting to know and diving deep into a rabbit hole about this business? And that's where I would go. And I think a lot of my process has been following, you know, staying in the pond, but then following where I think is interesting, has upside, like, in five years, 10 years, can I see this business growing? And then how does it fit with my portfolio as it is, like, I felt like I've said a lot the past year, I'm not gonna buy Apple six times in a row.

So maybe that also means you don't buy Apple and another smartphone maker like Samsung, maybe after you've bought some apple, it's like, what do I need next for my portfolio? Okay, maybe I'll look at something boring, like insurance or something. But that's kind of the framework I would use, and then you just over time, you start to get better and better and better. And it really does compound that as far as your knowledge and your abilities.

Dave

11:08

Yeah, it totally does. And that's a great way to think about it. And it's a great framework to help, I guess, guide you, as you put it, filter, try to filter out ideas and find things that you're going to be interested in. And I think that's one of the things that I know helps me as an investor is looking for companies or businesses that I think are going to be interesting to learn about and read about.

And sometimes you're going to come across things that you just never thought you would ever be interested in. And for me, something like the electrification idea of looking for different companies in the electric utilities, like thinking about, like, looking at utilities was something that didn't get me super excited. But if I went down the chain a little bit and thought about maybe how they produce batteries, or maybe how they you know, they generate electricity. Some of those ideas, I think are more interesting. And so you never kind of know where it's going to go. And I think something I'd like to talk about is I'd like to hear your ideas on maybe moving down the chain, let's say that you're looking at Apple, but maybe you don't want to buy it six months in a row, like you said,

So where can you like how do you kind of move down a chain from maybe one company you start with? And you kind of looked for different businesses that are related to Apple, but maybe aren't necessarily they are an apple? So how do you I guess, how do you kind of go about, you know, kind of filtering, I guess, further down the chain, if you will?

Andrew

12:37

That's a great question. And a great thought, I feel like it's kind of Sherlock Holmes, you know, we got stratosphere.io, or by the brightens, Bill, a crazy, great tool. And you can find a lot of ideas from there, even something as simple as Google Finance, if I type in apple. And then you scroll down to the bottom, I mean, that the page is changing. So if you're listening this three years from now, you know, figure out if they've changed the design, but a lot of times with like a company like Apple, it will show what other companies people Google search.

So Apple is a tough one because they're in so many businesses, right? But maybe if I looked at AMD, who does semiconductors, and you put that into Google Finance, you can go to the bottom and you will see all these other semiconductor related companies, Nvidia, Intel, Texas Instruments those kinds of companies will show up and that can give you the next piece of your little treasure hunt. And and you just start collecting these tickers. And then you got to do the research, right? You got to start reading about these businesses.

And for me, because I've been doing this for years and years, I like going to the annual reports. But if I'm a beginner starting this my first month, I'll probably start with some basic news articles, right? And just try to build your knowledge and, and understand it's going to take time. And again, you just follow that what's that quote about getting better every day? You kind of maybe take that mentality.

Dave

14:03

Yeah, the James clear idea of trying to improve 1% Every day is a small, little epic, he calls them atomic steps. But one little step every day improvement will magnify, you know, it will compound over the course of a year and it'll continue to grow. And I love that idea of going back to the 10 Ks. And I also like this idea of kind of expanding your knowledge. One of the things that I like about what Andrew does is he's more of a generalist and I have tended to focus more on specific niches.

And I liked the fact that Andrew is more of a generalist because it gives him a broader range of a pond to fish in where when I'm focusing on the FinTech, insurance, bank stuff, that's a much, much more narrow field to play in. And it can be harder to find ideas. It can also be harder to find ancillary ideas or side ideas off of those kinds of things. And one of the things that I like about what Andrew was talking about is like I Talking about electricity, a lot of people will just gravitate naturally towards maybe looking at a utility, for example, which boring business perfect. But let's say that you can't really find anything, but then you can look kind of down the chain and go. Okay, so these electric companies, they produce electricity, but how do they get them into our homes? And are their businesses around that idea that the electricity that Con Ed produces here in Illinois?

How did they get that into my home? And are there businesses that maybe I could invest in that and there are some, and so then you kind of look at those and go, Okay, maybe that's not the greatest idea, then you look at, okay, let's think about batteries, or, you know, and then who are battery producers, and there's lots of them are across the globe. And then you can think about the minerals that they put in the batteries, the batteries just don't become batteries, they have to mind the lithium and cobalt and copper and magnesium and all nickel and all the other minerals that they put in there. So you can look into those businesses.

And then okay, maybe those don't get to get you say it, but then you can think about, okay, how do they dig the holes? Or how do they make the how do they mined for the actual minerals, and then you can look at a company like Caterpillar, or you go to John Deere, Caterpillar, or maybe Cummins, these companies that produce the machines that these mining companies use to dig these holes. And maybe that gets you excited. So there's an all along that chain, they're all arguably pretty darn boring, except maybe batteries because of the whole electric car thing.

But that can even be a way of segwaying from cars into something that could be maybe a boring, more, quote, stable business. I'm not saying Tesla or GM are bad investments, but maybe they're not. Maybe they're not your cup of tea for whatever reason. And then you can kind of move down the chain, or you can kind of slide sideways if you just think about how these companies produce what they produce. And then you can think about, Okay, are there companies that maybe I can invest in that take advantage of that. And so there's lots of different ways that you can kind of move around, I guess, the food chain, if you will have these, you know, the top businesses that everybody's talking about.

And you can find these other great investments, like Andrew found is great investment. We kind of mentioned at the beginning, Martin Marietta, they produce aggregate. And it's a little more complicated than that. But, you know, they produce stuff that we use to build things. And it's kind of a boring, boring business. But it's been a ridiculously good investment over the last few years. And it's just not something that most people would even discover or talk about. And that's one of the things I love about Andrews approach, you know, having a more generalist ideas that he can find ideas like that. So I guess, where do we go from here?

Let's say you want to find boring businesses, you kind of look down the food chain, you find all these things, then how do you start to kind of hone in on something that could be a good investment, I guess?

Andrew

17:53

Oh, boy. Yeah, billion dollar question right there, right? It is related to everything you've been talking about, talking about kind of sliding around following that path as you're learning. So to me, the next logical step after you've kind of established, okay, I'm interested in this company, is you would directly look at who they compete against. And you start to paint a picture for yourself of how you think this company does compared to others.

So that means, you know, with Martin Marietta, how do they compare with Vulcan materials, who does literally the exact same thing they do. And so what's dangerous is you could start to get excited about a company. And so if you put on this lens, that everything about this company is great, you won't really get a picture that's maybe true or clear, unbiased about how the business actually is. So again, to me, I go back to the numbers and I, I try to collect as much numbers as I can.

And if you're just starting out, it can be something as simple as well, what's the revenue growth been over the last five years, and I'm just going to compare Company A to Company B, because I know they directly compete and which one has had the highest revenue growth. And then you can extend that to earnings. And then you can extend that margins and capital efficiency return on invested capital. So those are to me, I feel like that's the next logical step of I'm interested in the business. And I kind of get the ecosystem now. Let's really figure out they say they have a moat, they say they have a competitive advantage. Let's prove it. By gathering some facts and painting a picture with about you,

Dave

19:33

I probably do a lot of the same thing. It's really, really, really hard to not put those rose colored glasses on when you start to investigate a company. And it's really hard to find things that disprove your theory. And I guess one of the things that always kind of sticks in my head is the idea that Charlie always talks about what the we've discussed before, invert, always invert, and always try to kill your babies is an hour thing that he said are kill your favorite ideas. And I love that idea of trying to look at it from both points of view. I think a lot about the numbers. But I also try to think about the story. I read this great book from my buddy, Professor Ellsworth, Dumbledore and narrative and numbers. And he was talking about it from the point of valuation. But I think it kind of overall kind of comes from the same idea.

Some people are more numbers, people, ie Andrew, and some people are more story people, you know, somebody else, maybe not necessarily me, but and I think if you can try to marry those two ideas, it can help give you a really good framework of what's really going on with the business and trying to marry those ideas of, you know, this is a great company, but the numbers back it up.

And every company's in their 10k says that there are leading in their industry and that they have a moat. But the facts are, they don't. Not every company can have a moat. It's impossible. So the idea for me is always to come at it from okay, I really liked this company, what can go wrong and try to find the downside of it. And that's that's the hardest part is because you always seem to come across this information that just confirms how great this businesses to you, you read an article, you read somebody else's viewpoint. And you come across all these ideas that tell you the hell man, yeah, this is great. This is great.

This is great. And, and sometimes it's true, and sometimes it's not. And so how to sift through that it can be very challenging, but I love the idea of coming back to the numbers, because they tell a story. And our job is you know, the Sherlock Holmes it is to figure out what what are those numbers telling us.

And the better that we can interpret those numbers, the better we can understand the story, the better, we're going to be able to understand the company. And that for me, it's an ongoing process every day, I'm trying to figure out how to get better at that particular process. And, you know, hopefully every day I get a 1% better. But sometimes it's really clear. And sometimes it's not. That's the challenge of investing for sure.

Andrew

21:59

And I would encourage kind of like the Peter Lynch of idea of like, maybe starting investing in what you know, I think about it sounds so simple. And so this is like coming from a numbers guy as a warning to other numbers type people, like don't get so lost in the numbers that you forget, like you're saying the story or even just the basic common sense of an idea. I remember when I was looking at sporting goods stores, as part of my research, I drove to every single one that was public that I was looking at, it sounds so simple, right? But it is research, and we are all customers and consumers. And we can all get a sense of businesses without having to know the numbers of a business. So I'll give you another example.

And I'm not saying this bag on the company, or to say this is a bad business, it's very possible, probably whether it is maybe even restaurants in my area are going through a rough patch. So I'm talking about Chipotle, I've been a big fan of Chipotle since like, I don't know, like 2012 or 2013. Like, I've been there since the beginning. Okay, and I love Chipotle, I love that they can give you these macros that fit macros perfectly, and you know exactly you're gonna get, it's gonna be quick, and it's going to be good. But whether that's just the restaurants in my area, or whether it expands to the entire country, I've noticed the quality is different, not what it used to be three, four years ago.

So not to say that, if I had the stock, I would sell it or anything like that. But I feel like it helps those simple observations can sometimes help when you're painting that picture. And so don't neglect it. And also don't discount the kind of expertise you can have. Because I think sometimes the best person to know what the business really is doing, how it's performing can be their number one customers.

Dave

23:45

Yeah, absolutely. And all those ideas are fantastic. And I've done that before where I go to stores and I just observe what people are doing at the store. And working in the restaurant business for as long as I did. I drive my fiancee nuts because sometimes I'll sit down and go, Okay, our server has four tables intersection, we should get really good service. Or sometimes like oh my god, she or he are so overwhelmed.

They had this whole restaurant, there's nobody here to help us this is going to take a while. And is it your you don't see the manager, it's just all these little things that I noticed, because I worked in the business for so long. Those are things that I would watch my employees do, and try to make sure we didn't do those things.

But the whole point is, is that we can all observe where we work, or the places that we frequent for the things that we enjoy, like to do whatever it may be, whether it's going out to eat, whether it's going to a movie, whether it's going to buy clothes, buying a car, buying our insurance, any of those kinds of things, those are all things that we interact with on a daily basis our cell phone bill, our cable bill, how many of us here tried to cancel a Comcast and had fun with that. So you know, it's those are all things that we can observe. And those are things that you can take, that's knowledge you have you can use when you're investigating a company, any company and when you are start Hang out it I think Peter Lynch was right on the mark, I think looking at businesses that you're familiar with, or do business with, I think are a great way to start. You know, people always talk about Starbucks is a great place to start, I think it's a great place to investigate and learn about a company, especially if the if you're sitting in line for half an hour every day waiting for your coffee for your fix, that's half an hour, you could use investigating the company, you can think about the people in front of you, and behind you in the line, you can think about how the barista or the people that interact with you in the store.

And you can observe what people are buying, what they're not buying, how long they stay, whether people come and go, all those things are things that you can take away to think about the business model and what they're doing well, and what they're not doing well. And you can relate all that to what you read about in the company, because I guarantee you, the manager on duty is noticing that. And then their managers are noticing that it just filters up the chain until the decision maker goes, Yeah, we're not going to sell pizza anymore at Starbucks, not that they did. But it's just the whole point is they see that, you know, they see the numbers that hey, we're not selling pizzas. So let's not sell pizzas at Starbucks anymore.

Maybe we should do something more breakfast related, perhaps anyway. So I guess my point with all this is that I think, you know, observing what's going on in your world is a great place to start. Because those are great companies that you'll be able to have some knowledge of, and you're not just walking into a blind, like if you don't work in the tech world, and you don't really interact with tech much. And then you try to figure out what data dog does, that might be overwhelming.

But if you work in tech, and you understand all that, then data dog might be a great place to start. So I think there's lots of great places to start, I like to start with the boring businesses, because the Warren Buffett idea comes to mind always with this is, you know, rule number one is don't lose money. And rule number two is don't forget rule number one. And sometimes the boring businesses, they may not be super exciting, and they may not generate 30% returns over the next five years. But they're less likely to make money or lose money as well.

So that to me is I guess, one of my last pitches for boring businesses, if you will. And I think it's a great one. And I wholeheartedly agree. All right, well, with that, then we will go ahead and wrap up our conversation for today. I hope you guys enjoyed our little given take on buying boring businesses and our pitch, if you will, for going out and picking these kinds of companies, you absolutely have the ability to do all the things that we're talking about. There's nothing that we discussed today. That is beyond any of our listeners scope, you all are smart enough and have enough knowledge and wisdom to be able to do all the things that we're talking about.

So I encourage you, if you have not started investing, start today, open an account and start by one thing, one share of one thing and step off that ledge. I know it's scary, but you can do it. You got this and we're here to help you and support you. If you have any questions about anything that we discussed today. Whether it's the P E ratio, whether it's researching stocks, check out our website investing for beginners.com big huge search bar at the top can't miss it. You'll find all kinds of articles that are over 1200 There's something there for everyone. So without any further ado, I'll go ahead and sign us off you guys go out there and invest with a margin of safety. Emphasis on the safety. Have a great week and we'll talk to you next week.