Bird’s Eye View of Learning a New Industry

[This transcript was generated by artificial intelligence. Timestamps are not 100% accurate depending on the platform used for listening].

Dave

0:00

All right, folks, welcome to Investing for Beginners Podcast. Today we're going to do a bird's eye view of learning how to start analyzing an industry. So Andrew and I thought we would take a moment to kind of go over how we would start looking at something that maybe you want to dive into whether it's semiconductors, payments, maybe the cloud, maybe trains, you know, who knows anything like that.

But whenever you start to learn a new industry, there's there's a lot of information you need to learn. And this might be a good framework to help you kind of get started with that. So Andrew, would you like to go ahead and kind of start our conversation?

Andrew

0:35

Obviously, there's a million choices, you could go billion paths to go, when you're looking at an industry do you have one that you use in particular,

Dave

0:43

I guess the easiest way for me to kind of describe it is when I look at starting to try to get my head around a new potential industry. For example, when I was looking at payments, one of the things that I started to do was kind of use this framework of just gathering as much information as I could, whether that was books, whether that was podcasts, whether those articles, whether those were descriptions of different terminology, from the internet, just anything, any kind of information I could get, I try, just try to gather as much.

And so I just generally try to use, you know, the squirrel method, you know, go out and find as much about a particular subject as I could. And before I really started to wait in what about you?

Andrew

1:33

I think it'll be interesting, because we take different philosophical approaches to it. I try to really take like a bird's eye approach, I guess, for lack of a better word. But it's more about I guess, like identifying what would be the number 1234 biggest factors of that industry and then trying to not get too stuck in the minutia for me. But I think I'm more of a generalist in that way. Right. So it's like, if I'm trying to pay a picture, it's more on the financials basis than anything else. I noticed that that doesn't seem to be the way most people operate.

Dave

2:11

I don't think there's any hard and fast rule about how people can go about learning about a new industry. If you don't know anything about the train industry, and you want to start learning about it, I don't think there was any definitive, this is the way you do it. I think a lot of it just comes down to think how you're built and how you want to go about learning something new, I kind of liken it to learning a new language or just learning a new skill. And for me, it's always been about, I guess, diving into the deep end and kind of trying to absorb as much of the language as I can to familiarize myself, the way you do it is probably smarter.

And certainly probably, I think a lot quicker, but not in a bad way. But I think it's probably easier to assimilate the important things as opposed to just really diving into the deep end. Like when I started to learn the wine industry. When I was in the restaurant business, I would always go off the deep end and just started drinking a lot, of course, but but just work trying to learn the terminology and you know, picking up some of the hardest books and some of the most in depth magazines, and trying to learn about this particular industry from the inside out as opposed the outside in, I guess.

Andrew

3:33

Yeah, yeah, for sure. I guess from a financial standpoint, when I talk about trying to look at the number 1234 biggest factors, it's I don't know if this is like obvious, but that's for me as simple as like looking at what's the sales for different companies and comparing that. And then that helps to paint the first foundation of the painting of what's this industry like? So if I'm looking at shoes, for example, I wanted to look at all the obvious ones like what lockers in the news all the time. Dillards is another one. So you start to put all those together.

But then by the way, actually Nordstrom has a huge shoe department as well. And then when you overlay they actually sell more shoes than footlocker does. But I think when a lot of the people think of footlocker and the shoe industry, they they focus on that and kind of build off that. So I think when you look at the numbers, you get an advantage in picking up things that aren't always obvious. And like for me it wasn't obvious that Nordstrom out sells a locker and shoes, but that's something you can pick up by trying to paint the the biggest picture I guess.

Dave

4:46

Yeah, yeah. I mean, are you trying to when you do that, are you trying to get a an idea of the size of the market or the potential for the market by looking at the Like the revenue, for example, the shoe industry? Would that help give you an idea of maybe how much each company or different companies could potentially grow in the industry?

Andrew

5:10

Yeah, that's definitely one way to think about it, I guess I would want to know. So what's like an industry that everybody's very familiar with that we could take? Like? I mean, the iPhones probably one of the simplest, right, you would take the apple and you compare it to what Samsung and Google's Android, right, maybe not as obvious because those numbers like so the maybe could be even more like you can take Pepsi versus Coca Cola versus Dr. Pepper, right? It's very, very straightforward. And you can simply compare those two, but I think it's like one of those one we.

And I don't know if this is even obvious to most people. But I guess for stock market people, I think it is a little more obvious that those two are companies that are more mature, and maybe they have long histories are not going to grow crazy fast. And we kind of know that Pepsi and Coca Cola are pretty similar in size, whereas they're actually very similar. Were like not one of them's not like this fast newcomer. There's no like Uber of soda pop that we're familiar with. Right? So trying to do that with a brand new industry. Looking at those numbers can sometimes tell you, Okay, here's some of the bigger ones. Are they fast growers or slow growers? And then you can compare, okay, maybe this industry is more like Pepsi and Coca Cola, that's more matured. And there's only a few big players.

Or maybe this is like the cloud industry where there's 1015 companies all around the same small size, all growing crazy fast. And that's very different from Coke and Pepsi. So it doesn't give you all the answers. But it kind of helps me to understand what are the some of the dynamics in this industry. And I think something that can help a lot is if you start to see somebody taking a lot of market share. So I guess a good example would be Airbnb. So you see kind of the hotels, all their revenues, and then you compare it to Airbnb and Airbnb is growing, like a weed and all these other ones are growing more like Coca Cola or Pepsi, right? That's another obvious one to people. Yeah, Airbnb is is taken lot market share. But that's what you can visualize when you look at the numbers and start to see those things.

Dave

7:24

Yeah,I think that's a great insight, the thing that I noticed kind of using that I did my usual, you know, try to learn how different things work before I started looking at the numbers, but one of the things that I discovered when I was looking into solar panels, like the cons of solar panel industry, was that all the companies were growing really fast. But then if you started digging into the metrics, or just looking deeper into the income statements, you could also see that the vast majority of them were not profitable. For me, that was actually something I was like, Hey, okay, maybe this isn't the time to look at this industry for me, because the companies aren't making money. I don't see, in some cases, some of them were grossly negative in their profits and didn't look like they were trending in the right direction either.

So it made me think, Okay, well, maybe this isn't as much ado about nothing, like there's a lot of smoke here, but there's not much fire. And so it helped me actually kind of stopped my research on that, because I didn't think there will be anything there for me to what that I'd want to buy, just because of kind of the analysis of all the specific companies, it just didn't seem like it was anything that would be a good investment now, potentially somewhere down the road, possibly. But you know, as of right now, it didn't work, the economics for the industry, were all that great. That's

Andrew

8:42

a really good insight. And it's good that you were willing to get over the fact that you had invested some time in the industry, but understanding that, hey, this isn't what I'm looking for. So I'm just going to move on. Feels like a waste of time. But that's kind of required if you're gonna have some good insights, because having good insights means saying no to things,

Dave

9:05

right. Yeah, for sure.

Andrew

9:06

So I guess beyond looking at kind of the overview of the numbers, if you want to start, I guess, looking at some of the minutiae, then how do you go about trying to, I guess, kind of parse what you think is important, and what you don't think is important? Yeah, I guess, once you kind of have the big picture of the industry, and then you kind of know, okay, here's a company that's doing really, really well. And then maybe here's a company who's either the leader, or they're the best. And then maybe there's a number two, whatever that looks like you start to identify the key players in that industry. And then you I feel like that's the time to dive into those particular businesses.

And then that's where reading the annual report can give you a lot of information about if we're talking about shoes again, because I started with that. How does this company make money and then how do they differentiate themselves from a competitor, right and so we target In this particular type of customer, or we sell this particular type of shoe, you get into the real nitty gritty of that part. And then you can zoom in, zoom out, zoom in, zoom out and see, is this strategy that companies employing? Is it working for them? Or is it not? Because without the context, I could read about five different shoe companies, and they all sound like they're doing great. They all say, this part of our business is really, really smart.

Dave

10:28

Or one of the leading shoe producers in the world. Okay.

Andrew

10:31

You get a lot from kind of checking the facts fact checking these companies. And to me, like, I have to feel like I understand the logic of a company's but also see the evidence of a moat in order to say, Yeah, this is a better company than this company. And to me, I mean, I don't know, everybody can look at Industry Analysis differently, right. But when I'm, my purpose of industry analysis is to see what are the better investments inside of this industry? And then and then you try to kind of overlay that with is this industry good to invest in as a whole? That's my, that's my goal with looking at industries. I'm sure people do it for different reasons, too.

But if that's the goal, then the purpose is to see how are they doing compared to each other? And who's, who's the one that's going to do the best over the next 1015 years? Right?

Dave

11:24

Yeah, I like that. It kind of sounds like to me, like you kind of build up a shell, if you will, of this is what the industry kind of contains. And then you try to fill in the shell with information to tell you Okay, these are the companies that maybe I should look at. And these are the competitors. And these are the moats of these competitors, and how could they potentially overlap or even buttheads and compete against each other? Does that kind of sound like what you're trying to do? Yeah, I mean, I think that's a really smart way to do it.

And I think I've read that Michael Mobizen kind of does a similar thing, where he kind of builds a framework of this is what the financial situation. Yeah, a lot of people in the market like to refer to the TAM word. addressable market, it gets a little old because it gets overused, you know, Ubers, Ubers, Tam was 5 trillion or something crazy like that, when they first IPO. And so like, basically, every dollar spent in a world Uber was going after, that hasn't exactly panned out. But there could be some absurdity that but I think the framework, the way you do it, I think is probably a really smart way to do it. So let me ask you this question. Let's say that we wanted to investigate the semiconductor industry, and you kind of build that framework.

But if you don't understand, like, what semiconductors are, and maybe how they function? How would you kind of, is that something you attack? Or is that like, okay, maybe I don't quite get this, I can put this into too hard pile for now. Like, how do you kind of think about that? Because shoes or shoes? There's not a lot of tech involved in the shoes? I don't think but, you know, when you think about seven conductors, or there's a lot more moving parts, if you

Andrew

13:02

will, I feel like I will answer your question eventually. But I feel like you're the perfect person to answer that question. Okay, because I graduated electrical engineering, engineering for a few years in my career. You have a couple of semiconductor companies in your portfolio, but you had no background in the industry. So how did you get over the intimidation of something as complex as semiconductors, in order to be comfortable investing in them?

Dave

13:29

Well, I did my usual hoard a whole bunch of information to try to read through and just try to learn it as best I could. I went to, I looked for people that were considered industry experts, if you will, and try to read through the information that they presented some of it, I went to more of the semiconductor for Dummies, you know, realm to just basically get a grasp on what do they actually do? And then how do they make them? And then trying to figure out, what are the different moving parts of how they're made, you know, there's the design, and there's actual physical making of them.

And then there's the actual use of them. And so just trying to figure out how those different components in, you know, also I had you who has sort of worked in the industry, and so I could, you know, pick your brain about different things, because you had, you know, not inside knowledge, but you had worked in the industry. So you understood, you know, some of the technical questions that maybe I would ask about, you know, the differences in the sizes of the, you know, nanometers, you know, what's the difference between seven and five and, you know, understanding, you know, origins, you know, law and some of those things that once I started to kind of get my head around those, then it was a lot easier to understand the different businesses.

That's really how I did it, but it took me I mean, it wasn't something I did in a weekend. It took me months to kind of you know, keep picking at it and just staying at it until I got up. To a place I couldn't understand. And I also spent a lot of time reading the financial reports reading the 10 ks of Taiwan Semiconductor and Texas Instruments and Intel and AMD and Nvidia and on and on and on, when that helped start to give me a framework, but I went to YouTube and look for videos on how they're made. I looked at infographics start to create some of my own to some of those things.

And then I spent some time writing about it too, because I think that helps formulate, it helps you think better when you have to write because when you write, you're trying to put down ideas and try to clarify and for the reader. And if you can do that well enough, that means you understand something

Andrew

15:33

totally did you take a similar approach with payments, everything, pretty much

Dave

15:37

everything I've ever done. I did the same thing with payments, tried to do the same thing with the electric industry, whether that's solar or whether it's batteries, did the same thing with with the cloud, any of those kinds of things. That's what I've done.

Andrew

15:53

Did you know that's a big difference in the way you had to investigate, let's say payments versus semiconductors,

Dave

16:01

they were a little different. The semiconductor for me was far more technical. And it was way more outside of my circle of competence, because I just didn't understand what a wafer was and what a chip was, it just I didn't get that. So I had to figure that out. With the payments, part of it, it was more about the ACH and how the business use the tech. But once the tech part of it was kind of uncovered, the basic gist of it is they're moving money around. And that's not a whole lot different than banks.

And so once I kind of understood that, then it was a lot easier. Like, really, I started with Visa and MasterCard. And once I figured out how Visa and MasterCard work, it really gave me a good really good sense of the whole value chain, if you will, of how payments work. And so once understood the value chain and where visa sits in that, then it was a lot easier to understand a company like by server FIS, and Odgen, or Pay Pal because of where they sit in the payment architecture, or the flow, if you will, once you understand that, then it becomes a whole lot easier to understand the whole industry

Andrew

17:06

value chain, that's super, super important. Because it can be so easy to get caught up in this company competes directly against that company. But there's companies up and down that chain, customers, vendors, suppliers that play a key role in and also help you understand. Because you could be the best shiniest herd but you're still a turd and parts of value fans can be like that. Were not a big part of the profits go there was a small part of the chain and everybody else kind of has to feed off the scraps. Yeah, yeah, exactly.

Dave

17:41

In essence, that's what I was trying to do with the electrics with the electrical industry. Just I'm lumping a whole bunch of stuff. And so yeah, right. So when I couldn't find solar panel companies that I thought would be potentially a good investment that tried to start working back down the value chain to see if there was some other place in the chain, whether it was people that actually produce the silicone for the solar panels, or the chips or the wiring that's used not only from the solar panels, but to get from the solar panels to the conducting stations or the conducting stations themselves or the utilities.

And there's just there's a whole other chain of businesses that you can look at. And along the way. And same applies with semiconductor if Intel isn't your thing, you can look at TSMC who produces a lot of chips are and if that isn't your thing, you can look at, you know, design companies like Broadcom and Nvidia, there's so many different kinds of parts of the value chain that you can look at. And I think that a lot of times can be better opportunities than the thing you first originally thought was going to be the thing. So

Andrew

18:53

how did you since you're talking about semiconductors, how'd you decide on Texas Instruments?

Dave

18:58

That's an interesting question. I think probably because I was so wrong about Intel, that it led me to look at the business model for Texas Instruments and decide that in large part because of the write up that you did about the company really kind of helped spur my curiosity to learn more about the business. And then once I started to learn more about the business, I realized that their value proposition and what they create is a lot stronger and maybe less volatile in the long run.

Then an AMD Nvidia, Intel, Broadcom, Qualcomm, any, any of those other companies, which are not denigrating those companies at all are saying they're bad investments, but they're far more volatile than Dave likes to deal with. So, you know, Texas Instruments to me seemed like a safer bet. And I just felt like that their capital allocation, but just the business was stellar, but just the business model and what they do and how they do it. I just thought was sustainable for a lot longer than I probably originally thought.

Andrew

20:06

I feel like I already know the answer this, but what metrics confirm that this is for you with Texas Instruments?

Dave

20:11

Oh, boy, well, of course you got to look at the ROIC of the company, you have to look at the revenue growth and you have to look at the free cash flow growth. And I guess the last one is the share buybacks that they do, I think all four of those kind of general financial ideas kind of all correlate with how well they do what they do. They grow revenue, they're not super, you know, they're not going to grow at 30% a year, it's on the more mature side of the thing of the equation.

But because they do it so profitably, they generate so much cash flow that they can use to reinvest in the business, as well as buy back shares and pay a dividend. And they're very, very disciplined about their capital allocation. And if you read their 10k, they spend a lot of time talking about free cash flow and their capital allocation and how important it is. And they end every conference call with a little statement about how important shareholders are as well as free cash flow, so that it tells you if nothing else, that this is something they feel is very important to them. And, you know, it shows me that they care about us, you and I if we buy the company, so that was kind of my thought,

Andrew

21:19

there, they have a really great track record of doing that. So as you go through this, analyzing the industry and wrapping your head around how it works, what the businesses are, who the better performers are, what's next, because you don't just learn about an industry and then drop it all if you do end up investing in it. And I think this is timely because we had earnings last night. And Texas Instruments one of those big stock move after earnings, and a lot of the semiconductor names. So how do you deal with continuing to hold something in an industry and continuing to analyze that industry?

Dave

21:58

For me, it's maintaining my knowledge and continuing to try to learn more about what it is you're investing. I mean, we have to know what we own. And because I own Texas Instruments, when they have a quarterly call like they did a day or so ago, I listened to the call and I read through it and I think about what's going on with the company. And if it calls for it, I try to write something about it. And that all helps me maintain my knowledge of what's going on with that company and keeping me refreshed. On that idea. It also keeps my eyes open for other opportunities in the industry.

Because I've done enough work on Texas Instruments and Taiwan, semiconductor and Intel, I feel like I have a working knowledge of how the industry works. And so if something comes along, that catches my eye, it's a lot easier to switch and learn more about, for example, Qualcomm or AMD, for example, the learning curve isn't as steep because I've already learned and tried to maintain the knowledge of that industry going forward, and just try to keep my foot in the door, if you will,

Andrew

23:04

what kinds of things do you listen for in the earnings calls?

Dave

23:08

I think I tried to I use Texas Instruments as an example. So one of the things that I know, over the last, you know, I've owned the company, not quite a year, but I've listened to plus years of earnings calls for them and read four or five years of annual reports. And so because of that I know what the company is trying to do. And I know what their goals are and kind of their culture. And so one of the I guess the big overarching things is I try to keep in mind is what is the company trying to do? And are they veering from that. And so just to kind of a case in point with Texas Instruments, they're spending a lot of money trying to build out, expand their capacity, we're building out a new factory, and it's costing them a lot of money.

But they were upfront about that, over a year ago, two years ago that was going to happen, this was coming, they were going to spend the money. And all these things, were going to change revenue would potentially slow down. Margins would potentially contract and free cash flow potentially contract, which is all logical when you think about it, because they're like us, we we all of a sudden we go out and buy a car that we can't quite afford, then until we get a raise, then we have to kind of bite the bullet and except that you know, our money is going to contract a little bit. Well, that's what's happening with Texas Instruments. I know this because I know something about the business and where and they told us this was coming, but analysts don't like it. And they're pushing back on it and the market is pushing back on it a little bit.

But I know as an investor that coming on the other side of this is but a lot of potential for a lot of revenue growth and a lot of expansion of margins and all those great things that Texas is interested in is known for. So I'm okay with that as an investor because I know I got to go through a little bit of short term pain to get to the other side. Whether the grass is greener, if you will, so when I'm listening to their call, I want to make sure they're staying on that path that they said they're going to stay on that path. And if they aren't, then that's something that's going to pick up my ears. I don't get too excited, oh, margin contracted by one basis point or, you know, 100 basis points. Okay, that doesn't get me excited. But if they're, if management is changing, you know, all of a sudden, they're like, No, we're going to start drop this and we're going to become a Pizza Hut or something, then it's like, uh, you know, so I guess that's kind of what I try to listen to what about you?

Andrew

25:31

Or me last? Try to absorb all of it. So I have more positions, then most people? I think, right now it's close to 30. So for me, it's more about being intentional about how am I going to spend my time. And I think, at different times different companies deserve deeper dives. And I think with Texas Instruments, it's a good example, where you're seeing some softness in that industry, that sentiment is starting to turn analysts are getting impatient. If you don't know what's going on in that business.

That's a good time to do a deep dive and figure out what's going on. And is the thesis still the same? So yeah, I like that idea. I think it goes hand in hand with our conversation with Paul about thinking about capital allocation and how his management execute on that.

Dave

26:22

Yep. Yep, I totally agree. All right, everyone. Well, with that, we will go ahead and wrap up our show for this week. Don't forget to subscribe to the show on your preferred podcast app. If you enjoyed our little show. If you would kindly consider giving us a review. It greatly helps our show. And don't forget to browse the incredible materials we've created for you e investing for beginners.com.

Lastly, continue growing your knowledge as in investing for beginners insider with insights and educational tips delivered right to your inbox for free sign up today. And with that, we will go ahead and sign us off you guys go out there and invest with a margin of safety emphasis on safety. Have a great week, and we'll talk to you all next week.

We hope you enjoyed this content. Seven steps to understanding the stock market shows you precisely how to break down the numbers in an engaging and readable way with real-life examples. Get access today@stockmarketpdf.com until next time have a prosperous day. The information contained just for general information and educational purposes. Only it is not intended as a substitute for legal, commercial, and or financial advice from a licensed professional review, our full disclaimer@einvestingforbeginners.com.