IFB305: Evaluating Investments Beyond Stock Prices: A Deep Dive into Business Performance

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Dave [00:00:00]:

All right, folks, welcome to Investing for Beginners podcast. Today we have episode 305. Today we are going to read two great listener questions and answer them. One is going to be a two parter, so that'll be a little bit longer. But without any further ado, let's go ahead and dive in and take on the first one. So we got how would you suggest to monitor the performance of your investments? Maybe specific company performance? Key metrics, technical fundamental analysis in order to determine whether to sell, hold, or buy? So this is from Neil. This is a really great question, something we've not really talked about much before.

Andrew [00:00:34]:

My answer is all of the above. What's your answer?

Dave [00:00:38]:

My answer is the same. No, mine's a little more specific than that. Is yours a little more specific than that?

Andrew [00:00:44]:

Yeah.

Dave [00:00:45]:

Okay. You want to take first dab?

Andrew [00:00:48]:

Sure. I guess the biggest thing with monitoring the performance of the investments, I feel like the way that's worded maybe needs to change a little bit. What's the performance of the business. Because the stock market is going to move in so many different ways because it's so emotional. So if you bought a stock and it's down and the market's up, don't worry, it happens to me all the time. It happens to all of us all the time. It doesn't mean you were wrong. It means that that's the way investing in the stock market is now. You could start to see after a year, two years maybe, the market's onto something and you want to dig deeper. But when it comes to figuring out, do I want to keep holding this stock? Do I want to sell it, move on, you want to look at what's the business itself doing and then try to make a determination based on how it's doing. Do I want to continue holding this business for ten years, or do I feel like something has happened and I want to sell, try to cut those losses short and move on to a new opportunity. So I've definitely done all of the above when it comes to those. And sometimes you do want to cut it short, and sometimes you want to let it ride and let the market catch up with how the business is doing. So that's kind of the first way I would try to frame it. Don't look so much at the performance of the investments, look at the business and then make a determination from there.

Dave [00:02:05]:

Yes, that's a great way to do that. So how do you monitor, I guess, the performance of the business? Do you keep, like, a thesis book or do you have an idea of why you bought the business and maybe what is driving the business? And then how often do you kind of try to update that?

Andrew [00:02:23]:

Those are good questions. I guess I have the benefit that I've been writing about my investments for almost a decade. So luckily, or unluckily. There is a public record of all my great ideas and all my dumb ideas. So I can very easily go back to those and see why I bought a business and if those things are still true or not. I know that's something that you've suggested that people do. It doesn't need to be some grand report that guys on Wall Street are going to read, but it can be as simple as writing down your ideas. And I think that's very helpful because you'll forget sometimes it's easy to look at maybe headline numbers, and then obviously, if you're on a website like Seeking Alpha where people are making comments, your mind can go a completely different place than the actual reason why you bought a business in the first place. So to have those thoughts, to have that analysis documented somewhere, can really help you bring that conversation to where it needs to be, which is, why did I buy a business? Why do I think that this is an important driver for the business? And why do I think that that's continuing or not continuing? So I would say that's probably a good way to start. Do you do something similar?

Dave [00:03:35]:

I do. I've written a little on seeking Alpha. I've written a little on our blog, and we talked to Jake Taylor a while back and talked to us about this fantastic app that's free. It's called journalytic. And that's something that I try to use whenever I do buy something, is to make a post on there about why I bought it. What are the reasons why I bought this business? There's a technique that I've seen some people use. It's called a one pager, where they basically just take one piece of paper or one page of a document, however you want to use that, and they write down their thesis or their reason why they bought the company. Is it they have an industry leading technology? Is it you love the management or you think the product is so superior to anything else? Any of those kinds of things can all go in there. Warren Buffett actually created a one pager for Geico back in the it's out on the interweb, and it's really cool. It's maybe five or 600 words, not super long, but it goes into depth on why he bought Geico. And if you look at it now and kind of compare it, you can see why he's continued to hold the company all these years. Or I guess he's been in and out, but he currently owns it. And so I think that's a great way to do it. And the other reason why that's really helpful is I'll give you an example today. Ajin reported a Dutch payments company that I own, reported earnings today, and they are less than favorable. And the stock market absolutely hammered them. The last time I looked, it was down 38% today, so it was down big. But if you didn't know why you bought it and you saw that number, you'd freak. Anybody would I don't care who you are, you'd freak. But because I wrote it down, because I'm very familiar with the company, I'm not freaking. I'm actually probably thinking about buying more. But anyway, those are kinds of the ways that it can help you to monitor the situation. Because if you're just trying to go by memory and you see Netflix go down by 20%, that could be a pretty harrowing thing to try to live through for a few days until it starts to rebound. So that's how I do it. Do you look at numbers too? Is that something that you pay attention to? Do you have maybe company specific metrics or KPIs, I guess is the best way of putting it. How do you kind of look at that?

Andrew [00:05:40]:

Yes, I feel like that's a perfect lead into what I wanted to say. Anyway, to give an example know a situation where you see things change and you don't decide to hold a company. I'll talk about Target for the millionth time. If I look back at why I bought Target, it was partially you talk about the key performance numbers. Part of that was having a decent amount of same store sales. It was never going to beat GDP, but it was going to be at least what it's been in the past. And so when you think about Target's business, it's not like if you were to put them in a industry comparison, you would use Walmart and Costco. But the Target story is not really a low price story as much as it is a discretionary spending kind of story. And so when I saw developments where their customers who are making discretionary purchases weren't doing it like they used to, but then you look at a competitor like TJ. Maxx where that customer is still doing it, then you start to see, okay, maybe this isn't an economic we're going into a recession story. Maybe this is a targets losing their ideal customer. And they just came out with earnings, I think, yesterday, and comparable sales were down like 6% or something. There's a lot of drama that's been going around with that company lately. But even before that data point yesterday, I had started to see a trend that did not fit with what my original thesis was. And so it's really hard to cut bait with a stock, especially if you're down like I was. I don't know if I had lost money on that company, but I'd certainly underperformed the market in the time I held that company. And so that's really hard to lock in. But sometimes that's the decision you have to make when you have that kind of KPI that you're watching same star sales, if that's really important for them and they're not executing, you have to think about, is this short term or is this long term and what does it say about their future? So I feel like we've kind of danced around some of the question, but I do feel like it is dependent on the company. So I might look at same store sales and that portion of a revenue driver for Target, but that might not be the same for a different company, particularly if it's like a margin story or a buyback story or something like that. So you kind of have to take it on a case by case basis. And that's why you can't just say, oh yeah, this is how you want to monitor. Because there's different ways to monitor different companies.

Dave [00:08:06]:

Yeah, exactly. I think your Target example is a perfect example of why you need to have some way of documenting why you bought the company and what the things are that you need to monitor for the company. Because like Andrew said, it's going to be company by company. And if you start getting into the 15, 2025, 50 holdings and you want to monitor all those, if you don't have some sort of system, whether it could be as simple as a Word document or an Excel document or even just writing something on a notepad, it doesn't have to be super complicated. There's lots of programs out there that allow you to do that, to monitor all those things, because it has to be company by company, because you can't compare Visa's performance, business performance, to Targets because they're two different businesses. And so the things that are important to Target, like Andrew said, same store sales mean nothing to Visa. Likewise, Visa is all about payments and it's all about the amount of transactions that they're enabling because that's how they make money. And that doesn't mean much, if anything, to Target. So you have to kind of, once you understand each business better, how many coffee drinks Starbucks sells means nothing to Visa. Well, maybe does a little bit, but not directly. So I think just understanding the differences and then having some way of documenting that so that you can track like a quarterly or annual basis I think is very important.

Andrew [00:09:28]:

Yeah, agree.

Dave [00:09:28]:

I think the last thing I want to kind of touch on with this is one of the things that I don't track is the price. And I think that's one thing that when you have seeking Alpha has, you have the ability in stratosphere as well. You have the ability to kind of track your portfolio and see how it's doing versus its stock price. And that's not something I pay much attention to.

Andrew [00:09:49]:

Do you do you're better than me?

Dave [00:09:54]:

I haven't looked today. The only reason I know about Ajin is because of what's going on on Twitter. But beyond that, I have no idea whether anything else is up or down. I just don't look very often.

Andrew [00:10:03]:

That's one of my advices.

Dave [00:10:04]:

I guess the upside is that you don't react to negative news. So it's not like that. So I think that's one thing that I think is important, especially for new investors, it's okay to look, and it's natural to look. We're all curious.

We want to know, and especially if it's something new, you want to see how it's doing, but try really hard to create a lot of speed bumps in front of yourself, to not pull the trigger just because you bought Amazon and it's down 2% today. That's not really what we're trying to teach here. And so I think any way that you can prevent yourself from either looking if, you know, you can't handle it or if you can handle it, but preventing yourself from reacting to it, I think, will go a long long ways and it's just not something I pay much attention to as far as, like, tracking, it's more about the business performance, because that's really what's going to drive your returns over the next 510, 20 years.

Andrew [00:10:56]:

Yeah, if you're going to watch a train wreck in slow motion, put some eye protection on.

Dave [00:11:01]:

Right? Yeah, that's good advice. All right, let's move on to the next question. Now, this one's a two parter, so we'll go ahead and talk about the first part, and then we'll kind of go from there. So here we go. I have recently been trying to expand my portfolio into the shipping industry and came across a very bizarre company that I can't seem to figure out. It's the Yang Ming Marine Transport Corporation. It has a fairly large market cap and what I would consider an excellent balance sheet with an ROIC of 54%, as well as a healthy profit margin. It also increased revenue significantly over the last ten years. However, they have a massive dividend at $20, around 30%, but it's only around 50% payout ratio. I can't understand why a company that seems healthy and is a larger player in the global shipping market would seem so undervalued, and he's wondering if we could help sort that out. So, Andrew, do you want to kind of touch on the first part here and talk a little bit about Yang Ming and the kind of the shipping industry? I know you had some thoughts on that.

Andrew [00:12:01]:

Yeah, let's dive into some of this. So I'm not necessarily like, a shipping expert. I do have a logistics company in my portfolio, so a little bit familiar with that, I'll say, you know, shipping, and particularly if you're talking about on boats. So there's a company I'm blanking on the name right now, but there's a couple companies that deal with shipping containers and kind of shipping stuff from China to US. US. To China. Going internationally, that industry has just been historically very cyclical, and that might even be an understatement to say that when it rains, hurricanes, and when there's no rain, it's complete drought. Like, these profits you'll see are just crazy up and down. And that's just the nature of this coast to coast, if you will, shipping logistics. And so that could be why you mentioned having a dividend yield of, like, 30%. And all the metrics look great is because if it's a season where all the profits are piling in, but then next year it's a slowdown and you're losing money, then are those years profits really going to last for ten years? Which is how long we're trying to buy a company. And so that's why you'll see a lot of the metrics. It's like, wow, this looks too good to be true. And there could be a very good reason for that. And in this industry in particular, I've noticed that that's a very common theme of these companies, super low price to earnings when times are good, and it most likely will also result in a high dividend yield. And so that's why you kind of get these numbers that look really different. There's some other characteristics about this company in particular, too, but that's kind of the first observation I would try to think about. If the numbers look too good to be true, maybe it's an industry thing. And I know from studying some of the companies in this chain that that's how it is in this particular industry. Can you think of other industries that are kind of like that?

Dave [00:14:03]:

Oh, yeah. Well, I mean, the first one that really jumps out to me is the semiconductor industry can be maybe not quite as fast feast or famine, but it's definitely cyclical, and there's definitely ups and downs to different seasons of that industry, for sure. There's some consumer goods that can be very cyclical. Commodities can be very cyclical. And so those are some of the ones that kind of jump out to me. So if you're trying to look at some of these more, I guess, seasonal, cyclical kinds of businesses, like in particular, maybe the shipping industry, what would be a way that you could kind of try to, I guess, begin to analyze? I guess the first thing I would think of would be you don't want to look at just the first, like, one year of any sort of financials you'd want to look at a longer period. Right?

Andrew [00:14:51]:

Yeah. Well, start building your basic macro on Excel and pull that back 30 years and run a DCF on every year through your macro that's it all seriousness you can use. I know Braden's got this really cool Excel plugin, which I'm hoping he keeps that functionality because that plugin for Stratosphere allows you to go back 30 years or something crazy like that. So you can look at the company's history and very quickly see by looking at the numbers, oh, yeah, during 2008, 2009, the company lost a lot of money. And then you say, okay, well, if that company did did their competitor, who's in the same industry also do the same thing? And then you can see, okay, yeah. Whenever there's a recession, these companies really lose a lot of money, and then you're like, okay, this makes sense. So to your point, when something's really cyclical, if it's feast or famine, don't get too excited when there's a feast, but also don't get too depressed when there's a famine because you've understood, okay, this is just how that industry works. And that's something I think, as a beginner, I didn't necessarily understand fully. And what makes it interesting is every industry is a little bit different. And for this one, I mean, in our listener's defense, he wrote this last year, and I just saw it in my piled in my DMs. So the stock was doing really well last year as far as the company was making profits. But they're back to I don't know where they are now. This is old data, so sorry. Okay, in the listener's defense, he asked this question last year. So things may have changed a lot since then, but I can look back at the history of some of this, and there are a lot of waves, a lot of up and downs, and so I'll only have to take my word for it. You can actually look at the history as well and start to see some of those trends.

Dave [00:16:40]:

So how would you try to smooth that out, if you will? Would you look at a five or ten year period and maybe try to find some sort of normalized idea of maybe what the revenues could be? Like, just for example, okay, I really.

Andrew [00:16:55]:

Don'T want to overwhelm people because I just get crazy with it, but I'll say to keep it simple, one of the things I like to do as like, a basic screen is I like to look so QuickFS is another tool that's great for this. He also has an Excel plugin for this, so he'll let you do 20 years. So I like, 20 years, 30 years, anything that's long enough where I can see what happened during the last big recession, which the last big one was 2008, 2009. So I want to see data back to then, all the companies in the SP, and I looked at that 20 year period, what was their worst year and what was the drawdown to that? So the average revenue drawdown was somewhere like 15%, and the average operating income was something like 30%. So to translate that in layman's terms, at the worst point for a lot of the companies in the S and P 500, their operating income, basically their profits from their business dropped by 30% in the worst year. So now you can take that piece of information and when I look at, let's say paychecks, paychecks, their worst year where they saw operating profits drop was not nearly that bad. So I can say, okay, because of that, they're a lot less cyclical than your average company. And then I could take a company like a home builder or something like PHM it's like, all right, it went negative for a lot of years, so that's not as common, or they lost 80, 90% of their profits. So then you understand, okay, that's way more cyclical than your average company. So you want to pay a lot lower of a price for a company like that because you're basically saying whatever they're earning right now is too much. So I'm going to assume they're going to earn a lot less and then value the company based on that. I don't know. That's kind of to start where I would start to think about it.

Dave [00:18:47]:

Yeah, I like that. It kind of builds in a margin of safety because you're not taking the absolute enthusiastic high, and you're also not taking the absolute pessimistic low, and you're kind of working in between, which is probably a more air quote average or normal year for them. And then you can kind of base your performance on that, and then if the company continues to do way better than that, then awesome. And I think that's a really smart way to look at it because it automatically builds in a margin of safety when you're looking at any yeah, that's great.

Andrew [00:19:19]:

Last thing on this company, the other thing is I don't see it traded on the New York Stock Exchange, and it's also based in Taiwan. So you will naturally see stocks in other countries, particularly developing countries, that will usually trade at a lot lower price to earnings ratios. They'll probably have a higher dividend yield because of that. So stocks and other developing markets will look a lot cheaper. But there's a reason behind that because they don't have all the same rules as the companies that trade on the New York Stock Exchange. So I would keep that in mind, too. When you're looking at these companies, if you're only looking at numbers and you're not considering where are these companies traded, am I buying them over the counter? Am I buying them from the New York Stock Exchange? That can actually have a huge difference in the actual risk you're taking for this company and others. I would consider that as well.

Dave [00:20:14]:

Yeah, that's a good consideration, for sure. All right, so kind of implied in Ryan's great question is kind of this concept of how do you identify companies? And when you look at their financials and you see that maybe everything looks great, but why is it so undervalued? Why does it seem so cheap? And he's talking about Yang Ming in particular in this question, but kind of implied in this question is that's not just for this company, it can be an industry wide thing. It can also be a global wide thing. And why do we find companies like that? When you look at the numbers, you're like, why is this so cheap? And I guess maybe I'll kind of throw that to you first to start, and maybe we could chat a little bit about that kind of concept.

Andrew [00:20:56]:

Yeah, I guess that was like a conversation we had a month or two ago, right? I guess two months ago when I was loading into that one stock. Why is this stock so cheap? And until you have a good answer to that, you probably don't know the whole story. If you can't find a reason why it's so cheap. I just think you don't understand the story because there's no free lunch on Wall Street and there's just so few opportunities that you'll find that if you find something that's really cheap, it's going to be because you understand the risks maybe better than the rest of the Wall Street does, or there's some other circumstance that's working in your favor. So you look back, even maybe Warren Buffett's most cheap, best cheap stock he ever bought was American Express. That was in the middle of one of the worst scandals they've ever had. And it wasn't so much that there was no risk to American Express. It was that Warren Buffett understood the risk, did the research to understand what's the real risk, and then took a risk with his capital because he understood that the risk was less than what the market thought it was. So I think you just have to continue digging, or if you're lucky like me, find something. You can bounce ideas back and forth until you say something that you're like, you know what? Actually, that's probably why the stock is hated right now. And then once you have that answer, then you can make the tough decision. Do I believe that that's true, or do I have a good reason to believe something else? And that's kind of how I would look at it. How about you?

Dave [00:22:21]:

Yeah, I think that's a fantastic way to look at it, and I wish I had known that when I bought intel, because I think in hindsight, it was cheap, and I thought, wrongly, that the market was missing it. And it really turned out in hindsight that I didn't know the company well enough and I didn't understand the semiconductor industry well enough, and I just didn't really understand. You looked at the numbers just from a numbers perspective, and it looked cheap, and it looked like it was profitable. It had great returns on capital. The revenues were growing. Well, they weren't awesome, but for a mature company that's one of the leaders in the industry, it was good. And all those things would lead you to go, wow, this is a great business. But then it's also trading at a 1416 PE or something in that range. And other companies that are as well regarded in the industry and in the markets were trading at much higher multiples. And so you would kind of think to yourself, okay, the markets missed on this, and the market didn't miss on it. They knew it better than I did, and they understood that maybe what was coming for intel hadn't quite hit yet. And the fact that they had gotten behind in semiconductor, the race for the smallest nanometer, they lost, and once they got behind, it becomes that much harder for them to catch back up. And those were things that I knew, but I didn't know. And so sometimes you can maybe be aware of information or data, but if you don't really understand that concept of once you get behind, you can't just skip two to catch up, you actually have to go through the effort of building the one that you're behind on to get to the next one. You can't just skip ahead. And so it just doesn't work that way. And when you don't understand that like I didn't, then it means that the company is not cheap. And so to Andrew's point, when you really understand the business, then you can really understand what is driving the value in the market. I'm not saying that the market is efficient, it's not. But I am saying that there are going to be times where the market's right a lot too. And so there's a reason why it's trading the way it is. And so I think really kind of understanding what you're buying and really knowing the business goes a long, long ways to understanding why it's so undervalued. So in the case of Yang Ming, if I was looking at it and I don't understand the shipping industry, I would have to do a lot of work to really get to what's going on with this industry. And why is this company in particular selling for so cheap? And before I would buy it, I would have to understand that idea. And after my experience with Intel, I now understand how important that really is. Before, I didn't really get that, but I do now.

Andrew [00:25:12]:

Yeah. In particular, that idea that you have to go down each node is so specific to that industry. I don't know if I can think of any other industries that function just like that. Makes it hard.

Dave [00:25:24]:

Yeah, it makes it really hard. When you look at another company in the industry like Taiwan Semiconductor which is a fantastic business it's kind of the opposite end of the spectrum of intel where intel is kind of at this point has become a little bit more. They're behind the curve on being a leading edge, whereas Taiwan Semiconductor is infinitely the leader and is in the lead in what they do. They don't have a lot of competition and they have fantastic margins. It's just all around a great business. But then it still trades cheaply. But you understand that that's related more to a geographic risk than it is to a business risk per se. It's cyclical, just like all the other semiconductor. Companies are. So, I mean, there is that to consider, but just the kind of the opposite ends of the spectrum of the quality of the business and kind of where. They're going with their products and their services is vastly different. But understanding what's driving that can help too. It can help you decide how big a risk is China and how much do I really need to consider that? And I think those all things can help.

Andrew [00:26:31]:

Do you think seeing that with intel helped you better appreciate TSMC's Moat?

Dave [00:26:37]:

Yes. Unquestionably unquestionably. Yeah, for sure. Because I feel like it not only gives you insight into intel and kind of their place in the ecosphere, if you will, but also gives you a better appreciation for maybe a company like AMD and Nvidia and some of the other players that are all operating in the ecosystem. And to give you a sense for how great TSMC's Moat really is compared to what I thought possibly was Intel's Moat, which was wrong.

Andrew [00:27:10]:

So you still have a chance to redeem yourself then?

Dave [00:27:12]:

Yes. With one. Yes. Full disclosure, I own both. So, yeah, I could redeem myself with Conductor by learning from my mistakes. And I think that's the biggest thing that I try to take away from that is there's a whole myriad of reasons I can learn from that mistake. But I think it all goes back to determining what's driving the underperformance versus others in the industry or others in the really. But you really got to get to understanding why the company is because like Andrew said, there are no free lunches in the stock market. With so much information available and so many eyes looking at so many things, it's really hard to find something like, AHA, I figured it out and nobody else has.

Andrew [00:27:55]:

Yeah, well said. Should we do this last part of the question? Yeah. So we're going to move on to the last part of Ryan's question here related to what we've been talking about, but kind of a different problem in a way. He says, I find that when I branch in industries and companies I'm not as familiar with, that I come across these sort of companies that just puzzle me. So speaking to Ryan about companies that just don't make sense, the numbers don't make sense, or even maybe advice to your younger self, what kind of tools or takeaways could people have to dig into some of these industries and companies that are just kind of out there?

Dave [00:28:32]:

Yeah, I think for me, it all comes back to trying to learn as much as I can from the masters and how they think about different businesses and how they look at approaching specific not specific companies, but just in general companies. And then trying to read as much as I can from other people that I consider smart in the industry. And that can possibly help you understand why are people investing in Block or why aren't people investing in Snapchat? I don't get it. They puzzle me. I don't understand what people see in them. So if I'm going to go into that industry, in the advertising industry, then I want to learn as much as I can about

Google and Meta and trade desk and Snap and anybody else that's kind of operating in that industry to give you, I guess, a better sense of how the industry is and try to be curious. I want to be know for me, I'd want to understand why are people investing in this? I don't get it. I see this, and it doesn't make any sense to me, and ask questions, and I think that's what I would tell myself. And don't pull the trigger until you answer those questions. What about you?

Andrew [00:29:40]:

That's good. I would say that curious. I just put a spotlight on that word, curious. That's a big one. I think the longer you can stay curious, the more information you can compile both about a company and an industry and just your general knowledge. I think the more information that compiles, the better decisions you'll make. I would look to something like that, too.

Dave [00:30:04]:

Yeah, I think that's the best way. Staying curious, using all the resources you have available will definitely get you closer to having an answer. Sometimes you just may not. And I guess that's okay, too. And it's okay to pass. Don't have to swing at every pitch. We can let these go by. If you don't understand it, you don't have to buy it just because it's puzzling you. So I guess try to remember that too.

Andrew [00:30:24]:

Yeah, perfect.

Dave [00:30:26]:

All right, everyone. Well, with that, we will go ahead and wrap up our show for the week. Don't forget to subscribe to the show and your preferred podcast app. If you enjoyed our little show, if you would kindly consider giving us a five star review, it would greatly help our show. And don't forget to browse the incredible materials we've created for you@einvestingforbeganners.com. Lastly, continue growing your knowledge as an 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 the margin of safety, emphasis on the safety. Have a great week, and we'll talk to you all next week. Bye.

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