IFB307: Buy When There Is Blood in the Street

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Dave [00:00:00]:

Welcome to investing for Beginners Podcast. Today we have episode 307. Andrew and I thought we would talk about buying when there is blood in the street. So recently there has been some pretty extreme volatility and we thought we would talk about how this could be an opportunity to buy or sell particular companies and maybe kind of our thought process behind this and how you could utilize this in your own investing. So guess Andrew, let's maybe talk about some past and maybe talk about the banks and then we can kind of go from there.

Andrew [00:00:31]:

Let's do some post game film. Look at what happened with the Know. Some time has passed and I think it can be helpful because that was really the last time there was major blood in the streets. And I know it won't be the last, and it's something I think hopefully a lot of listeners have lived through and it's recent enough where we can draw some lessons from it. So maybe just to give a little bit of a context in case you're listening to this in the future, earlier in the year there were some banks that it was discovered, they had troubles, there were some problems, a couple of banks and a couple of them went bankrupt, they went bust. So as a result that whole industry, just all those stocks came down, they came down by a lot. And we're recording this maybe three, four, five months later and a lot of, well, at least the stronger banks have recovered and their stocks are doing a lot better and it would have been a great time to buy. But if you think about we lived through that, it was not an obvious time to buy, even though looking with hindsight it seems like, oh yeah, we shouldn't have all loaded up on banks. So, I mean, I missed it personally, what happened. We're value investors, why didn't we take advantage of this one?

Dave [00:01:44]:

For me, some of it was fear, some of it was maybe not having spent enough time really analyzing those particular companies. And so when they went through that period, I didn't feel like I had enough knowledge to take advantage of what was really going on. Some of it was a lot of noise, especially when the Silicon Valley Bank collapsed. And that whole period there was lots of noise, lots of news, lots of media, everybody and their brother covering it. And so it was very much in the face upfront and I guess I didn't feel like it was really impacting Morgan that much. But in hindsight it was a great opportunity because maybe it didn't directly impact them. But a rising tide raises all boats and so does a falling tide. It takes everything out to sea too. And that's know, fear in the market can impact a company like Morgan for example, that was not experiencing the same issues that were Silicon Valley Bank or First Republic for that matter. They were not going through the same issues that those two particular banks were, but the market was reacting like all banks were bad. And so that just kind of drew everything down and I just felt like I didn't have enough knowledge to really feel like I could pull the trigger and buy more Morgan if I owned it kind of thing. And that would have been the time to do it. And so I guess that was my reason. What was your reason?

Andrew [00:03:13]:

My reason was I felt like I was fully allocated already and so I didn't feel a pressing need to allocate anymore because I had a lot of banks in my portfolio already. So I guess the silver lining is as the banks in general recovered then I saw the recovery in my portfolio but then the flip side of that is like well I should have taken advantage and bought more and obviously I didn't. So does make the case for like when you wait for some stocks there can be a lot of payoff because if you're underexposed to expensive sector and then it becomes cheap then you can really load up and that can do really nice things for your portfolio. But it is interesting because for all we know this could age like spoil milk. I was looking at their tickers and a lot of those banks are starting to come down again and we have been seeing some pressure on stocks in so you know, will that blood in the streets period return? It would be interesting to see we're not completely out of the woods yet when it comes to all this stuff. But one of the things I do remember that stuck out during that time was how Warren Buffett who's been pretty big on banks for a while sold out of everything except for bank of America. So whether you want to admit it or not, that can sometimes have an impact on the way that a lot of investors think because he's such a respected thought leader that you wonder if oh man, are things for the banks really going to be bad for a know and it's hard to know.

Dave [00:04:45]:

Yeah, it's very hard to you know, my crystal ball is very fuzzy and so it is hard to know. But that's a great point that Buffett is probably one of the best bank investors out there and he certainly knows the industry in and out and it's a little telling that he's not in any of them other than bank of America. So that logically you could look at that and go well maybe he sees something that we don't that is preventing him from being in that sector. And I think it really goes back to trying to know what you own and understanding what it is that's driving the returns for those particular companies. And like you said you felt like you were allocated pretty heavily to that sector and I do too. Even though I'm not in banks at the moment, particularly, I have a lot of payments companies which are financial companies which are tied to the banks to a certain extent. And so being exposed to that sector, I didn't feel like I needed to run out and try to do some quick analysis to decide whether US. Bank or JPMorgan was a right fit for my portfolio. And hindsight is always to 2020, right? It's always easy to look back and go, well, yeah, duh, you should have bought that. But when you're in the moment, sometimes it's hard to justify it or realize it, especially if it's something that is kind of falling outside of your circle or it's not really something that you know a lot about.

Andrew [00:06:14]:

So let's talk about this idea that someone who's very well respected or I think we all assume Warren Buffett's probably smarter than us. When you see an investor do something like that, would that prevent somebody like you or I from investing in a sector where there's blood in it or an industry? How do you get past that as an investor? Because that's a tough hurdle to get over. And a lot of times when there is blood in the streets, you do see a lot of big names that.

Dave [00:06:42]:

Do stuff like that.

Andrew [00:06:42]:

Either they'll make a comment in the news about an industry or they'll vote with their feet and their money like Buffett did. How does an investor even have a chance to get past that?

Dave [00:06:52]:

Right? That's a really hard question and that's a tough question for me. That's something that I guess I obviously respect Buffett and Munger and all those great investors. And the way that I try to work around that is by trying to understand the companies that I own and trying to do the best that I can do and not worry too much about whether Warren or Tom Gaynor or pick investor and insert here doesn't or doesn't own this particular company. For me, I'm going to do the research and work that I feel like I need to do to buy Visa. And I'm not going to worry too much about who else owns it simply because they're not me and I'm not them. I mean, it's a nice confirmation when you find out that Bill Ackman owns the same company you do. Like, okay, hey, a smart guy owns the same company I do. All right, maybe I did make a good choice. But the ultimate decision to buy Visa or Ajin or Texas Instruments did not come back to whether Warren and Charlie owned it. It came back to I thought this was a great investment for Dave. And that's, I guess, how I try to view it. You and I own many of the same companies, but I didn't buy them just because you recommended know I bought Texas Instruments because you showed me how great it was. And then the more research I did, I realized that you were right, and it was a great you know, then I made the decision to buy it, but not because Andrew told me to buy it. I did it because it was something I felt like was a good choice for me.

Andrew [00:08:29]:

So, I guess how would you react? Mean we could take TSMC because Berkshire had a position in TSMC that's in semiconductors. We both own that.

Dave [00:08:38]:

Yep.

Andrew [00:08:38]:

And shortly after I bought TSMC, Berkshire got how that's a very direct parallel with that one because I think you still own TSMC.

Dave [00:08:48]:

I do. And I actually bought it after he.

Andrew [00:08:50]:

Sold out of that's how you got over yeah.

Dave [00:08:53]:

Yeah, I got over it partly because I felt like that was maybe not necessarily his decision to buy the company. I wondered if it was Ted and know his underlings, if they were the ones who made the decision to buy the company or if it was Buffett, irrespective of whoever chose to make that decision. You introduced me to how great a company it was, and then after I did some more work on it and read about it and tried to learn about it for my own, then it led me to go, okay, yeah, this is a good investment. At least I think it's a good investment. So time will tell whether I'm right or wrong. But for me, it's trying to be, I guess, my own person. I have two choices. I can do it myself and try to figure it out on my own, or I can just literally just follow Buffett and every investment he you know, to me, I can't do that. So that's how I move past it, is by trying to make my own decisions, because what drives him to do it? I'm not in his head. Likewise, he's not in my head. So certainly not saying I'm better than him. No stretch. Not implying that at all. But that's what works for me, is I'm trying to be, I guess, independent. Thinker, if you will, if I can be.

Andrew [00:09:57]:

Makes sense.

Dave [00:09:58]:

Yeah. That's kind of what it comes back to for me. So how do you think about that? How do you move past the blood in the street and how do you move past opportunities that you may or may not miss? And how do you try to if something does walk into your wheelhouse, how do you react to that?

Andrew [00:10:14]:

So I guess coming back to the banks and why did I not sell bank of America or Morgan, which I own both of those when I heard that Buffett has. And like you said, Buffett's been a really well respected investor in the banks, and he's made big splashy moves with the banks from time to time over the last decade. Plus longer. Obviously longer, but especially in the last decade. And so for me, it was my understanding of why I own Morgan and bank of America and the reason why I own it. It comes down to as simple as I believe they have a moat and I believe that banking will continue to be important and they will continue to as the economy rises, so do banks. And I think that sounds really obvious. Like, oh yeah, when the economy rises, companies go up with the economy. That sounds obvious, but that's actually not the case. You'd be surprised how many companies that might not apply to, but banks are one of them and they don't have to do much to participate in that tide rising. So that's one reason why I own banks. And then the second one, as far as the two bank of America and JP. Morgan in particular, is because of the way I feel about their deposit moat. And so it's very possible that maybe Buffett's view, maybe he sees a different moat in those banks and maybe it's not centered around deposits. Or if it is because people have talked about this whole deposits thing ad nauseam during this whole crisis, it's very possible that him and I just have a different opinion on whether those deposits are sticky or not. And that could come from our own differences in personal experiences of the way we've interacted with people. Different spheres. It could be a million different you know, Buffett said he's wrong a lot and I know I've been wrong a lot. So you figure, okay, maybe I'm wrong this time or maybe I'm right this time. At the end of the day, it kind of comes back to what you're saying. If you can understand about the company and why you own it, then you can kind of ride or die with that decision. And as long as you have the information, you can feel good about it. And the fact of the matter is, if you're going to chase the higher returns that come when you buy, when there's blood in the streets, you better know why you're buying and you better know why there's blood. I think for the banks in particular, I think a lot of it was around deposits, because deposits have always been thought of as so sticky that they stick around longer than a lot of people's wives might. And that seemed to have changed because of how fast a couple of the banks had collapsed. What the verdict of that is, we'll see, but that's the question you have to ask yourself is, all right, if that's why I own a bank, do I still feel that way? And hopefully you're able to have that conversation with yourself before there's blood in the streets, so you can react right away. But that's going to look differently for every company. We got a couple of companies today and this past week that have dropped a lot blood in the streets. And there's definitely other reasons why people are running for the exits. And it does make you puts that mirror up to your face like, okay, why am I holding this? And is everything I'm hearing in the media really going to be the future of this company, or is it going to be something else?

Dave [00:13:34]:

Right, yeah, exactly. I mean, Odjin is one of the companies that I own, and they dropped 40% in one day. News came out that they were slowing in sales. Their margins were contracting, and the market reacted. It's always been viewed as a very expensive stock. And when the market saw that the growth wasn't as big as it has been in the past, the market reacted very negatively to it. And it dropped over 40% in one day. And the next day, I think it dropped another 10%. So it was down almost 50%. It erased three years of gains in basically a day just gone. And so it was a pretty drastic drop. And there was lots and lots of chatter on Twitter about why that happened and why there was so much blood in the street related to this company. It didn't just affect Ajin. Too. PayPal dropped 10% in the same day, and it had nothing to do with Ajin. But just because the tide was going out on Ajin. It kind of pulled other companies in the same sphere kind of down with them, and they partially recovered the next day. But I had a question that I had to ask myself. Okay, do I believe in this investment or not? Do I believe in this company and what they're doing or not? And for me, who was in the company, fairly big, over 10%, 12% of my portfolio was in this company. I had a choice to make. Do I want to double down or do I want to run for the hills? And after thinking about why I bought the company, all the reasons that I bought the company, and are those still intact? And they are, then I decided to put more in the company. And there are varying opinions on Twitter, for example, about whether it's time to run for the hills or not. And a lot of people were piling into the company now because it's cheaper. And some of the people that owned it ran for the hills because they just felt like there was no way it could ever recover from this. And I don't believe that's the case. And so that's why I still believe in the manager, in the management, and I still believe in what they're trying to do in their platform and in their moat. And just the opportunity that they have in front of them, I think, is really big. And the other thing is that all these things that they were supposedly falling for, that were being viewed as negative were all things that the company had been broadcasting that they were going to do for over a year. And so the big drawdown was that the thing everybody was complaining about, the majority of people were complaining about was the fact that their margins contracted. And the reason their margins contracted was the company went on a hiring spree. And they've been doing that over the last year or so, and they broadcasted that they were going to do this. They expected their margins to contract, and they knew this was coming. But they did it strategically because several years ago, when prices were sky high and employees could demand the world, especially in tech, it was really expensive to hire people. And so Ajin's. Like, they held off. And then when the market started to turn, and then when the employment market started to turn and people couldn't necessarily demand the highest prices for their jobs, then Ajin. Went after talent. When other companies like PayPal and Stripe and some of the others in their industry started weighing off people because they overhired, then Ajin. Swooped in to hire these great employees to help spur more business in the future. And so they've done this in the past. They did this three years ago and went through the same contraction, and then they came out better on the other side. And so I expect this to happen again, but I knew that it was coming. It wasn't a surprise. And so the market reacting as negatively as it did was a surprise. But the reason why ajin Was doing what they were doing was no shock to me. And so to me, it was not an easy decision. It's never easy. When you see a company drop that much, you certainly are going to have doubts and think that you made a mistake. And time will tell. I may have made a mistake. It's entirely possible. I have to realize that and understand that I could have made a mistake. But at this point, I don't feel like I have. But again, time will tell. And that's what investing is all about, is trying to make informed decisions as best as you can with the information you have in front of you. And then if you make a mistake, try to learn from it. So that's, I guess, kind of why I did what I did.

Andrew [00:18:14]:

There's a lot in there. I mean, I see a lot of parallels with the stock I'm wrestling with right now where they have a and I don't feel comfortable talking about it yet because the decision is still up in the air. But it's definitely been bouncing around the last few days. Similar story, big drop over a day, and the different headlines and the different changes in the business which were telegraphed beforehand and talked about. Yeah, it is interesting. Maybe let's talk about a time when buying when there was one in the streets did not work out well for people. So one that was kind of near and dear to my heart was when the airlines came down during the pandemic, because I own Southwest Airlines and I had a pretty big stake in that and that was definitely a blood in the streets situation when all those airline stocks came down. And so in contrast to the banks I ended up selling out of Southwest during that time. And in hindsight, again the verdict is still out because we're talking about three years and not ten years. And that applies to the bank, it applies to the airlines, applies to Ajin. The verdict is still out but in hindsight it appears like that was actually a pretty decent move to not buy in the streets. So my question to you then would be what are times where you determine that there's blood in the streets and I'm going to avoid it and it ends up being a good thing.

Dave [00:19:39]:

Yeah, that's a good one. I think it comes down to understanding the business, understanding the industry that is experiencing this downturn and understanding what is really driving the downturn. And if there are structural changes or if there are some sort of changes that are happening to the industry or the particular company that they're not reacting well to and they're falling behind, then it can be a situation where is this is the time not to dive in. And an example that kind of springs to mind is kind of the situation with Nokia and Apple. When the iPhone came out and when Nokia realized that they were now behind the eight ball and their stock was dropping, you could have had the opportunity to buy into that company for a lot cheaper than when it was writing its highs. But if you understood what was really going on that the technology was changing and what Apple was introducing was revolutionary and was taking the world by storm, then investing in Nokia would have been a mistake because the company reacted late, they reacted poorly and they were never able to really come back from that. And that's one of the things that I struggle with intel is I don't know if they're going to be able to recover from getting behind in the tech. And I'm not an expert in the semiconductor space, but at the moment, I have not doubled down on intel just because I'm not sure if they're going to be recovered. I haven't seen signs that that's going to happen and I don't get too bent out of shape about, okay, I missed the bottom and maybe I catch it more on the rebound. It's still a great return. You can't time everything perfectly. So I guess that's kind of one of the ways I think about it. What about you?

Andrew [00:21:30]:

Well I guess taking it back to the airlines, you mentioned there's something structurally different about the industry and for the airlines at the time it definitely appeared like it was that there was something structurally different nobody was flying for and we didn't know how long that was going to last.

Dave [00:21:47]:

Right.

Andrew [00:21:47]:

So that definitely played a big role. Not to mention the fact that they were no longer profitable. And that's one of my no no's. So you wonder if that's one of the million dollar questions alongside know why you own a company and what the reason why you're trying to hold this company for a long time is. And the other flip side is that if there's blood in the streets, you know it's because people are doubting the future of this industry, and it's up to you as an investor to determine whether they're right or whether things are really not changed as much as people might think. So another saying that I think is really great to remember is the four most dangerous words in investing are this time is different.

Dave [00:22:30]:

Right.

Andrew [00:22:31]:

And so you do have to wonder when people start expressing that an industry has changed forever, is that really the case, or is it just one of those cycles that we see over and over and over again? Industry, industry, industry. One of the hot button topics right now is inventory shrink and a lot of the theft that's going around with retailers. But it was funny. I was curious, like, is this something that's brand new? Because it seems like it's really getting out of hand, especially if you watch the news. I saw an article from 1970 from the New York Times talking about, because of the tough times with the recession and high inflation, people losing, feeling, really crunched with their finances, that there was a lot more theft going on, a lot more organized crime and all of this. So you do have to ask yourself, if I want to be a retail investor, for example, in retail stores, am I worried about that, or is it something that's cyclical and predictable? Taking it back to the banks? Yes, bank earnings go down when there's a recession. Big shocker. But are they going to stay down forever, or is it just part of the cycle? So again, it's not always that easy, but sometimes it is. The airlines probably will recover one day and be fine, but for whatever reason, I've continued to avoid them. So we'll see how it all plays out. But sometimes you can get really complex, and sometimes things do change. And to your point, with Nokia, sometimes a company just goes away of the dodo bird, but a lot of times with good companies with good management to your point, cyclical things happen and things turn around and it's really easy to get caught up in the emotions of negative thoughts around an industry and you just wonder if that's the best time to unplug and dive into a ten k and just shut the rest of the world out, right?

Dave [00:24:15]:

Yeah, for sure. Think about this. I was listening to one of the latest Berkshire meetings the other day, and Warren was talking about how he and Charlie have experienced greater than 50% drawdowns on Berkshire Hathaway stock at least three times in the time that they've owned the company. And so it's not unusual to see drawdowns and to see blood in the street for Berkshire Hathaway and arguably one of the greatest companies ever. And so it comes back to you experience volatility. If you own individual stocks, you're going to see companies go down. I mean, Nvidia right now is on the run of the century. It's up 178%, I think when I last looked year to date, so far, but a few years ago, it wasn't doing so great. And so it's part and parcel of owning companies, owning individual stocks, and being involved in a complex system like a stock market, and you're going to see ups and downs. And if you skew in on a short time frame, you're going to see a lot of volatility, like the most extreme roller coaster you've ever dreamed of going on in your entire life. But if you zoom back over a longer period, you'll see less ups and downs, and you'll see more gradual up to the right, hopefully. And so I think it's part and parcel of the industry of investing, and I think that you just need to really understand what it is you own and why you own it. And if you can understand those things and really have a good grasp on why you own a particular company, then when there are drawdowns, you can consider taking advantage of those. But again, it comes back to doing some research, like Andrew said, unplugging and diving into a ten K and really understanding what's going on with intel. Is this just a market cycle and everything is down, or is this something that intel has done that has caused them to be the stock market is reacting the way they are with them. So I think that's great advice. Unplug and go read a ten K.

Andrew [00:26:17]:

Unplug and read a ten K. Yeah, that's unplugging.

Dave [00:26:19]:

Read a ten K. Moral of the story, right? All right, folks. 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 five star review, it greatly helps our show. And don't forget to browse the incredible materials we've created for you. Investingforbeganners.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.