Back to Basics: Essential Portfolio Maintenance For Investors

Dave [00:00:00]:

All right, folks, welcome to Investing for Beginners podcast. Today we are going to do one of our back to the Basics series. Today we're going to talk about portfolio maintenance, if you want to check back every Thursday. And we'll talk about different aspects of back to the basics as we try to help you become a better investor. So as I mentioned earlier, portfolio maintenance will be the topic for today. So maybe, Andrew, we can start and talk about maybe what is a portfolio and how do you maintain it?

Andrew [00:00:28]:

Yeah, I mean, stock pickers, that's the never ending struggle is to try to figure out what stocks are you going to place in your portfolio and what place do they have in your portfolio and how are you going to use those choices to define how your results are going to turn out? How are you going to be able to achieve what you're trying to achieve? And so it is hard because in the process of being a stock picker, you have to figure out what kind of stock picker do I want to be? And you might not know the right answer right off the bat, and then you might not be good at like figuring out which companies actually work best, which portfolio buys and sells work best for that strategy. So it can be difficult.

Dave [00:01:14]:

Yeah, it totally can. When you're building the portfolio, you kind of have to think about where do I want this to take me, how do I want to get there? And it's not just about trying to decide whether Verizon or Nvidia are the best choices for your portfolio. You also have to think about how does this impact my goals and why am I investing? And picking stocks can be a challenge for sure. It's hard. And there's a, there's a lot of moving parts that go into it. And so determining what you're going to put into your portfolio and then how you're going to maintain it, I think is probably an under discussed skill or activity when you are investing. I think most people focus so much on what companies do I want to buy that they dont really think about a building the portfolio b does this fit my dreams and goals and see how Im going to make sure that what Im buying today is going to fit that priorities 510, 15 years from now. So I guess kind of thinking through that, how would you suggest a newer or even an intermediate investor can start thinking about those ideas and how they can start trying to build the portfolio?

Andrew [00:02:30]:

Robert, I don't know. That's a hard one to answer because the, I feel like we've talked about before the types of investors and different goals you might have can be so different. So what do you think?

Dave [00:02:41]:

Yeah, I think the first thing you have to decide is, what are my goals? What am I doing this for? And then once you have an idea of what those are, then I think need to start finding companies that fit your needs. In other words, if you're somebody that's looking to buy and hold great companies for a long period of time, I think that's going to be a different mindset or a different goal set than if you're trying to find something that is going to try to. If youre a trader or if youre somebody thats looking for more short term goals than long term goals. And it can also depend on what your time horizon is. If youre 56 and closer to the end versus 27 and closer to the beginning, I think your setup of the portfolio is going to be a different beast.

Andrew [00:03:34]:

So can you give some examples of walking through somebody making some of those decisions?

Dave [00:03:40]:

Yeah. So I guess the way I would think about it is if I have a longer time horizon, then when I'm picking companies, I'm going to look for companies that have a longer horizon, but they also may be a little earlier in their journey as far as a business. So maybe they have a long Runway to go, but maybe they're early on the Runway. And so you could look for companies that may have a little more volatility in them in the early stages. And understanding that if you have a longer time horizon, you can withstand some of the ups and downs of that company and still earn a good return because you have long enough time for it to recover from a potential drawdown. If there was a recession or if there's some sort of economic news that comes out or any sort of just natural volatility, volatility that you see in the stock market. And so if you're younger, that's kind of how you can learn to maintain a portfolio is by having a longer term mindset and giving yourself more time to recover from potential downturns or things that could potentially bad happen. Black swan events like Covid, those are all things that when you're investing, you have to not necessarily account for, but you have to keep in your mind that could happen.

Dave [00:05:08]:

And so if that does happen and you are investing in maybe younger or riskier stocks, that you have to kind of understand that that's part of the game. And sometimes you may see downturns in companies that you don't expect, maybe in the short term, but in long term they can do better. Likewise, if you are closer to the end of your journey as far as investing and you're looking to have maybe more stable investments or things that maybe don't experience as much volatility, and you can use those to help you get into retirement and with the understanding that when you have these older, maybe more mature companies that maybe aren't as experiencing as much volatility as a younger company. So if you're looking at, you know, I'll just pick out two that may be appropriate. So if you're thinking about a company like Nvidia, which is not a young company, but right now the industry they're in is kind of new, then they may experience more volatility in the short term, and we'll see what happens in the long term. But a company like, let's say UnitedHealth is a more mature business. They're in insurance, and youre not going to see maybe as much volatility from them as you would in Nvidia just because of the nature of their business. And so if you are at the end of your investing journey, a company like UnitedHealth might be a better fit because you wont experience as much volatility and downturn in economic times of struggle, whereas something like Nvidia may experience more of that just because of the nature of what it is they do.

Dave [00:06:56]:

I guess thats how I look at. What are your thoughts?

Andrew [00:07:00]:

I think thats a pretty good way for a beginner to start to think about the different ways you can categorize stocks.

Dave [00:07:07]:

Yeah. So what would you say would be a good way for an investor to start to, once they have a portfolio kind of put together, how do they kind of maintain that, depending on where they are in their journey, I guess, yeah.

Andrew [00:07:23]:

I think the easiest answer to that is the closer to retirement, you get more risk you want to take off of the table. And so for a lot of people, I think that means reducing the amount of stocks you might have and adding stuff to that can be less volatile, less risky, like bonds, but, you know, there's tax implications there. So you'd want to talk to a financial professional as far as, like, figuring out what types of businesses you want to have in your portfolio. I think it's really hard. I think we all have different opinions on what we think is going to be successful and what we think has a good chance of being successful and what doesn't. And so, you know, as you start to figure that out, some lessons in some industries won't work as well as lessons and others. And then generally, the younger the industry, the more risk can be involved, and the less of a chance that you're going to be able to forecast who the eventual winners will be. I like the example of Google.

Andrew [00:08:19]:

I heard this recently on the podcast. They were the last search engine. Everybody likes to talk about being the first adopter, and that's supposed to be the magic sauce in tech. Google was the last search engine, and now they are the only search engine as far as dominant market share. So it can be hard. I think tech's especially hard. I think, for me, one example I can throw out there that I felt useful is I feel like I've talked a lot about American Eagle and the many lessons I learned from that position. But one of them was, in the process of owning that stock, I realized that I don't want to be involved with a stock where I feel like, uh, it can go out of fashion very, very quickly.

Andrew [00:09:09]:

And so, even though I made good money on the stock, I don't want to make that mistake again. And so, for me, knowing that I don't want to have to be on top of fashion trends helps me make decisions on what kind of companies I want in my portfolio. And so, for me, that means I'm not looking at. And again, I reserve the right to change my mind. But, you know, I'm not looking at Lululemon, I'm not looking at Amber crimean pitch, I'm not looking at even some of the luxury stuff, because I just don't understand it. And so, for me, it took owning a fashion company and seeing how volatile those are to learn that. What kind of lessons have you learned in your journey?

Dave [00:09:49]:

So many. How much time do we got? I think one of the things I've learned is what I don't want to invest in or maybe things that I would probably, at this point, prefer to stay away from. And bringing up Google Lemon is a good example for me because it's something that I am the last person that anybody would ask about fashion. And so my ability to judge the popularity of a trend or the staying power of a trend, I guess, is maybe a better way of putting it. I am the last person to that I would ask, and nobody's going to ask me, if you see how I dress, nobody would ever think, oh, this guy is going to know everything about Lululemon. No, not the case. And so I think, hopefully, I can be aware enough that I can try to stay away from those kinds of companies because they don't fit. They don't fit the way that I want to invest or feel comfortable doing.

Dave [00:10:48]:

To your point, I don't want to be looking over my shoulder all the time worrying about if the train has left the station on a company like Google Lemon. I'm not saying it has by any stretch, because again, I don't know enough to say yes or no, but when I'm faced with those kinds of decisions with companies, I don't want to have to be, I don't know, kind of question. And so it's something like that, or let's say it's something like oil. Like I understand that oil is necessary, but I also understand there's a lot of uncertainty about its place in the world. And therefore, and then you take into the account that it's a commodity and you have futures. And the pricing I don't necessarily understand, per se. I've not really dived into it much, but it's never really been something I've been super interested in either. And so I guess when you combine those two factors, I just don't invest in it.

Dave [00:11:43]:

And I'm not saying you can't be successful. Others, like, there's tons of people that have been very successful at it, but it's not a game I want to play. And so I guess I try. I've been trying more and more and more to stick to games that maybe I have not necessarily an advantage in, but at least a competency or a potential to have a competency in that can give me a better chance of performing better over a longer period of time. And I think if you stick with that, I think you don't have to buy everything. And I think that's one thing that it's real easy to get caught up in the FOMO and it's real easy to think, oh my gosh, I missed out on Nvidia and I'm screwed. And I'm never going to get a good return just because I missed out on that stock. And while it has done awesome, it doesn't mean you can't have great returns, not investing in that.

Dave [00:12:31]:

Andrew has proven that with his portfolio right now. So I think that's why I tend to try to stick to my own lane, if you will, and hopefully that can help me. And that's one of the lessons I had to learn the hard way. I invested early in a company called National Oil well Varlo. I think that's how you say it. And I didn't really understand what it was. I didn't really understand what they did. It was in the oil industry, and I lost, I don't know, good 85 90% of my, of the value before I pulled the trigger and got rid of it.

Dave [00:13:02]:

But you know, it just shows that you can't buy everything and you can't know everything. And I think you should try to stick, to stick to your areas of competence if you can.

Andrew [00:13:12]:

Yeah, for sure. Have you made mistakes like in the time horizon realm?

Dave [00:13:19]:

Yeah, I think I have. Probably being too focused on in the past, being too focused on short term ism and getting frustrated because a company that I thought was a good business wasn't doing as well as I thought it should. And so then probably being impatient and pulling the trigger on something that, you know, ended up doing well over a long period of time. I've done that a few times for sure. Have you fallen for that?

Andrew [00:13:49]:

Yeah, I feel like I fall for it all the time. I think for me personally, I can, sometimes I get too excited for a company that's maybe more on the mature side and you dont see that impact. Well, you can see that impact anytime because the stock can do whatever it wants, but you wont generally see that impact until 510 years down the road. And so ive tried to implement a I want revenues growing at least as fast as the economy because if its growing less fast in the economy, thats going to be hard to outperform the market over like a ten year period, lets say. But, but you know, it's hard. There's some really good businesses out there that don't grow revenues that much, but they might be really profitable, for example, and be really good at becoming more and more profitable or there might be some maybe trends. A good word for. I was trying to think if there's another word but some sort of trend that's really like pushing the whole industry forward.

Andrew [00:14:51]:

I'm thinking about target, where after the pandemic it seemed like everybody went to target and then that kind of went away. So is that something that's more temporary rather than permanent? And that's where sometimes the nuggets of value can lie in determining whether the tailwinds that are pushing an industry, are they short term or long term? And if they're long term, you might have like a huge win, but if they're short term, you might be stuck in something that's more mature. Like I have had investments in. And over time you just start to realize, man, this thing's not going to beat the market. So that's kind of, I feel like that's a lesson I continue to learn. It's just something to be careful of.

Dave [00:15:35]:

It is. I mean, it's. It's easy to fall for. It's easy to fall in love with different businesses, right? And you kind of get a little bit of rose colored glasses about particular companies, and you don't see the forest for the trees sometimes, or you just choose to ignore, or the forest for the trees. And it's hard, it's really hard to overcome those mental biases or those blocks that cause us to think about those things. So here's an interesting question. We were kind of talking about tech a minute ago, and tech is now 25 28% of the s and P 500. And probably my guess is that that percentage will grow in the next 1520 years and tends to be maybe a little more volatile.

Dave [00:16:25]:

So as investors, do you think we need to get more comfortable with volatility as we age into our portfolios? Or do you think that's just going to become part of the, I guess, the game that we'll have to play as we invest for the next 1520 years because tech becomes a bigger part of our everyday life.

Andrew [00:16:47]:

Well, that's a loaded question, isn't it? What makes you think tech's going to be a bigger percent of the s and p?

Dave [00:16:54]:

I don't know. I just wonder if technology will continue to take over more and more other parts of businesses that maybe we aren't even thinking about now. I'm not talking about like the AI revolution. I'm talking more about just technology taking over other parts of our lives that maybe it isn't quite yet at this point, but maybe it will become more so of our lives. And I just wonder how that will impact investment decisions compared to today.

Andrew [00:17:30]:

Yeah, I mean, I think something like this, we can really get down the path of splitting hairs. Part of the whole tech concentration now is we have this magnificent seven that make up so much of the index meta. Google, Apple, Microsoft, all those guys are all pretty much tech. And so they're both a combination of so big, and they've been the ones that have grown the fastest lately. I could see a world where if those businesses start to become more mature, I wonder if other industries have the chance to take some of the tech slice from the stock market. But I also don't think you can argue very well that there won't be more tech in the future. So you see how I'm splitting hairs?

Dave [00:18:21]:

Because I totally get it. I totally get it. I mean, your point about those companies being so large helps them take up a bigger part of the s and p. 500, for example, just because of the sheer size of their businesses, you think about the things that maybe tech is not touched so much yet, even just in our own homes, I think there is opportunity for other things to come in. But to your point, we're splitting hairs a little bit about that. I guess I'm thinking about this in the context of, let's say that you're 32 and you're building a portfolio and you want to earn money for your retirement someday. And how you allocate towards different companies can go a long ways towards what youre investing in. So if youre 32 and you have a fairly healthy risk tolerance, is investing in something like Verizon, which is maybe growing at GDP or maybe below, is that a good potential investment in your longer horizon or is it better to look at something like a Microsoft or an apple or something along those lines, which probably will grow faster than the GDP over the next ten or 15 years? And I guess that's kind of what I'm trying to envision, I guess.

Andrew [00:19:44]:

Yeah, I think you probably have better odds going for the faster grower. Let me care if I say that. Yeah, you have better odds if you go for somebody who's already growing faster than GDP, than somebody who's not. So if I was 32, I would try to put more companies that are growing at least GDP or higher than less.

Dave [00:20:06]:

Mm hmm. Yeah, I think that would not guarantee, but it would give you better odds that your portfolio would grow faster as well over that period of time.

Andrew [00:20:18]:

Well, assuming all those companies that you pick continue to execute.

Dave [00:20:21]:

Right, true. Good point.

Andrew [00:20:24]:

Dont have a crystal ball? No, just don't have people who are very flawed working in them. Nothing in the stock market's a sure thing. So that's why price matters. The price you pay on the stock matters because so many things can go wrong. But to your point, I would rather litter my portfolio with a bunch of GDP growers, pay a good price for them rather than get a bunch of, I don't know, the story about Verizon. I think you could argue different things. You know, 5G is very much in the bear market right now, but, you know, take a basket of like ten sub GDP growers. Yeah, I wouldn't, I would not want to leather my portfolio with those.

Andrew [00:21:07]:

Absolutely not.

Dave [00:21:08]:

No. It'd be harder. Now, I guess. A better question, another question then. Let's say you're 55 and you're investing at that point, do you think having maybe not sub GDP but more GDP like companies would be a better fit than some of the faster growers just because of the volatility that could be involved.

Andrew [00:21:30]:

I don't. Yeah, I mean, I'd be curious your thoughts? Cause I don't know if I necessarily subscribe to that idea.

Dave [00:21:36]:

I have not subscribed to that idea. And there's probably a big reason why that is, is because you read more and more reports about how our lives were living longer and a lot of the time worn advice about investing and morphing your portfolio as you get closer to retirement. I think some of that makes sense. But there's also the fact that 25, 30 years ago, the life expectancy was a lot shorter than it is now. If you're going to live, if you retire at 65 and you lived in 95, then thats 30 years that you have to live off of your retirement. And I think the expectations of getting to 95 are probably a lot higher than they were 25, 30, 40 years ago when a lot of these investment rules were established. I think you have to have maybe a little bit of a different mindset than maybe was originally established. At least thats the way I think.

Dave [00:22:43]:

So im not saying you shouldnt have more safer investments like fixed income kinds of bonds or money market accounts or things of that nature. I definitely think thats the case. But instead of maybe moving out of a company like a Microsoft thats growing at 10% a year into something like, I dont know, maybe Walmart, which is only growing at 5% a year, I probably would argue that its better to stay in Microsoft for as long as you can to ensure that you're continuing to grow your wealth as you are in retirement because you still want to generate income you don't want to. To me anyway, I'd rather have more at the end than not enough. And so I think that would be a better way to try to play it. But I'm not a licensed broker, and this is just kind of something I've been thinking about and how I want to do it. I wouldn't say that this is necessarily the established way to do it, but it's something I've been thinking a lot about, you know, because I'm 57, so I'm closer to the end than a lot of people. And so that's just kind of the way I'm approaching it.

Andrew [00:23:52]:

Yeah, I feel like the golden rule of don't have money in the market that you can't afford to lose would really apply there. So if you have money, that if it was me and I was, you know, five years of retirement and I have shares in a company that I want to use in retirement. I would just put that into something that I knows really low chance of losing money. So I'll just take it out of the stock market completely. But to kind of play like a middle game where you're trying to get with less aggressive stocks in air quotes, like less aggressive stocks, I don't think that's a good game to play at all. I don't. To your point, like, if you're going to have money in the market, you want that to grow in the best risk just the way that you can. And I don't care if you're Walmart or

Microsoft or UnitedHealth, if a market crash is coming, it's coming for all of them and so can't afford to wait for it to come back then.

Andrew [00:24:48]:

But whatever you can't afford to lose into bonds or cash or cds, whatever, is a lot less price volatility. That's kind of how I would look at it.

Dave [00:24:58]:

Yeah, for sure. You know, if I'm three years from retirement, I'm not looking to try to find the next. I'm not saying this is going to happen, but something more volatile like a crowd strike, I wouldn't, that would not be a company that I would probably put a lot of money into as I'm getting closer to retirement. Because to your point, if I can't afford to lose it and that company tanks for whatever reason, a high flyer like that, it's going to tank hard and it's probably going to tank harder than a company like Johnson and Johnson.

Andrew [00:25:31]:

So that it may never recover.

Dave [00:25:34]:

Yeah, it may never recover or it may never recover in your lifetime. And so there's that.

Andrew [00:25:38]:

Or just may never recover.

Dave [00:25:40]:

Yeah, true.

Andrew [00:25:41]:

Who's to say that? Like going back to the Google search example, you know, who are the other eleven Google competitors to Google search now?

Dave [00:25:51]:

Yeah, I could maybe name three. Right.

Andrew [00:25:57]:

So not to dig on crowdstrike, but those are the type of investments I think people should be very careful about because their odds of success are not guaranteed, especially in a young industry like cloud security, where anything very much wild, wild west there, I would think.

Dave [00:26:14]:

Right. It's still evolving market and you don't know who's where it's going to end up and probably a long ways away from where you're going to know what's going to end up. And even though Crowdstrike may be the leader now, there's no guarantee that they will be in five years.

Andrew [00:26:29]:

No.

Dave [00:26:31]:

Yeah. Okay. I guess so. To maybe kind of wrap this up. As people are building a portfolio and trying to get themselves ready for wherever stage they are, do you think they need to probably look at their age, time horizon and risk tolerance and compare those to kind of where they are in their investing journey?

Andrew [00:26:59]:

Yeah, I think that's a good idea. As a general rule, probably the longer time horizon you have, the more risk appetite you have. But theres a limit to that. And you want to make sure youre not gambling, but youre making intelligent investing decisions. What do you think?

Dave [00:27:19]:

Yeah, I totally agree. I think depending on where you are in your lifecycle, I think that can go a long ways towards forming how you build and maintain your portfolio as you evolve as a person and as an investor. And the closer you get to your end goal, I think then you need to start adjusting your portfolio to meet those goals because I think when you're younger, you have different goals and when you're a little older, you have different goals. And so I think your portfolio needs to adjust with those goals and what you want as you get closer to your goal, whatever that may be, whether it's buying an island and drinking pina coladas or traveling the world or playing golf the rest of your life. I mean, whatever that may be. Yeah.

Andrew [00:28:06]:

And to kind of go back to the discussion about sub GDP, like if I'm envisioning a world where I own visa and, you know, if I'm in retirement and it changes from a GDP plus business and it matures into like a sub GDP, I might be fine with that.

Dave [00:28:24]:

Right.

Andrew [00:28:24]:

Because the tax implications of selling might be more bothersome than just taking the dividends and being okay with sub GDP growth.

Dave [00:28:34]:

Right.

Andrew [00:28:34]:

And depending on your life cycle, that might be a wonderful way to go about it.

Dave [00:28:39]:

Mm hmm. Yeah. Yeah, exactly. I mean, I think all those things, you have to kind of take all those variables and kind of run them through the calculator and decide if these are things that are going to work for you, where you are. And to your point, visa may eventually become that sub GDP grower, but if it's, you know, you've got a lot of money tied up to it, the taxes may eat into the profits that you could earn from selling it. It may just be better to continue to take the dividends from that as opposed to, as you said, the bother of dealing with the tax implications. Cause that's not a lot of fun and it could be a hard thing to deal with.

Andrew [00:29:20]:

Yeah. Then you gotta figure out where you're gonna put the money after you sell.

Dave [00:29:24]:

Right.

Andrew [00:29:26]:

You might have again, depending on how long you've held it. The tax implications can be tricky when you're putting money into something new, right?

Dave [00:29:37]:

Yep. I mean, bottom line, there's a lot of variables and there's a lot of moving parts to all of this. And when you're constructing your portfolio and you're maintaining it, I think you have to think about those things before you make rash decisions at any stage of your investing lifetime.

Andrew [00:29:55]:

So what advice would you give to somebody who maybe doesn't know exactly what kind of companies fit in their portfolio to fulfill their goals? Maybe they have the goal in mind, but they don't necessarily know, like what kind of companies fit with that. What would you say they should do?

Dave [00:30:11]:

Boy, that's a good question. I think they need to. The way I would try to approach it is I would try to figure out, okay, this is what I want, how am I going to get there? And then start looking around for either the individual companies that can help me or trying to find people that can help me. So if I don't feel like I have maybe the experience or the time to look for that, then I would turn to somebody like you who's already building a portfolio and looking at the service that you offer. Because I think that can be a great way to help hedge. Not hedge, but get you started, at the very least on building a portfolio, because you have somebody that has experience, somebody that is doing it, has done it, and then you can look to what they're doing, and those companies that you're investing in can be a great, I guess, guidepost or training wheels to help me figure out what it is that I want to do. And so that's, I mean, that's kind of how I started doing it to begin with, honestly. And in some respects, I still do that.

Dave [00:31:22]:

And I think that can be very helpful to, you know, lean on somebody else to help you. And that's one of the great things about the value spotlight, is that it can offer that ability to help people and act as guardrails or training wheels or whatever adjective you want to put on it. It'd be helpful to help you if you don't have that experience and you kind of don't know where to start.

Andrew [00:31:44]:

Yeah, that's cool. I would say, too, if you have the time, probably look into some investing classics and just try to broaden your horizons in general and understand it's like a lifelong game so you don't have to figure it out all at once. Stay curious like you always like to say, right?

Dave [00:32:01]:

Yeah. Stay curious. I mean, the more curious you are, the more you're going to learn. And the more you learn, the hopefully the smarter you'll get. All right. Well, with that, we will go ahead and wrap up our conversation for today on portfolio maintenance. Thanks for joining our back to the basics series. Again, we're going to do these every Thursday.

Dave [00:32:18]:

We have quite a few episodes scheduled to come, and these are all designed to kind of help you learn the basics of investing and help you become a better investor over the long term. So with that, we will 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 all next week.