IFB369: How to Handle Stock Losses for Beginners

Alright folks, welcome to Investing for Beginners podcast. Today we have episode 369, so we are going to answer some great listener questions, but before we dive in, if you have any questions, please reach out to us at newsletter at investing for beginners.com. We'll be in the show notes. You can also send us questions on.

00:00:50 Dave

The Spotify app, if we're listening to the podcast via that or you can reach out to us on the social machines in particular.

00:00:57 Dave

The X machine or.

00:00:58 Dave

Twitter send us those questions and we'll be happy to read them on the air and help you out any way we can sue with that. Let's dive into the first question. This is from John, so hi. I enjoyed your podcast very much. Listen to all the episodes I can. I too purchased Disney stock a few years back and was up for a while, but now I'm down a bit for an extended period of time.

00:01:18 Dave

I've been reluctant to sell for not wanting to.

00:01:20 Dave

Lose money. But am I wrong? And should I just peel the Band-Aid off and move on? Or was I right in holding on and hope of recuperating my investment? I bought a lot of shares when they were in the 100 and 30s and I.

00:01:32 Dave

Doubt it will.

00:01:32 Dave

Ever get back to that yet? I can't.

00:01:35 Dave

Hit the sell.

00:01:35 Dave

Button left. Any advice would be much appreciated. Thanks for any info you can pass on to me.

00:01:41 Dave

And other listeners. So great question and I'll turn it over to you Sir Andrew for.

00:01:45 Dave

The first take on this.

00:01:47 Andrew

Sounds awesome. Well, let me make it short and sweet first. Thank you for listening. Second, this is a great, great question and I appreciate the honesty. And you know the feelings around it is very hard sometimes to sell a stock especially.

00:02:03 Andrew

At a loss.

00:02:04 Andrew

And I feel like we all go through this as investors, if you hold individual stocks.

00:02:09 Andrew

You're going to inevitably come up with this, and it happens whether you've been doing this for 10 years or 10 days. So my short answer is.

00:02:19 Andrew

It's different depending on what stock you're talking about. So you really have to look at Disney's kind of in a silo and think about, do I still believe in the fundamentals of this business or not? That's kind of where.

00:02:32 Andrew

For me, the the crux of the answer would.

00:02:35 Andrew

Be.

00:02:36 Andrew

That is, I think that that's the first part. And then the second part, you have to get over the psychology of ripping off the Band-Aid and we can talk about that later as well, but for me.

00:02:46 Andrew

The answer to the question is always.

00:02:49 Andrew

How do I feel about the business? What has changed and how do I feel about not the Business Today, but ten years down the line?

00:02:57 Dave

I'm of the same camp, so I bought Disney during the pandemic for my daughter, so I was starting out and I let her pick some of the companies that she invested in, so she chose Disney, Spotify, Roblox, and Amazon because those are the things that she uses. So ironically, she's probably destroying me. I haven't looked at her portfolio recently.

00:03:18 Dave

But between Spotify and Amazon, they've done quite well. So she we bought Disney at much lower price and then we bought a little more when it was a little higher price and since then it did not do well and we actually ended up selling our shares of Disney essay our only because I bought them. But it was really her invested in it.

00:03:40 Dave

So I ended up selling them for her because she didn't like.

00:03:43 Dave

A Disney movie.

00:03:44 Dave

And so she wanted to sell. So I let her. I let her make that decision. But like Andrew was saying, when you're in this situation, it's really hard, and it's probably the hardest.

00:03:56 Dave

This.

00:03:56 Dave

And buying is stressful, but selling is way more stressful. And because it's we feel the loss way more than we feel the win. And so the psychology around that is it really prevents us from maybe doing the right thing or hesitating way more than we probably should. The way that I would try to look at this.

00:04:17 Dave

Is.

00:04:19 Dave

If you have.

00:04:20 Dave

A thesis, or if you've written down something of why you bought the company in the 1st place and then looking at that and realizing OK, these these ideas are the reason why I bought Disney are still in play, then it becomes a little easier to make a decision yay or nay.

00:04:41 Dave

If you unfortunately did not do something like that, this would be a good time to remind yourself. Note to self. Write down why.

00:04:48 Dave

The company, you can do it anywhere and it doesn't have to be anything fancy. It can literally be a notes.

00:04:52 Dave

App on your phone or.

00:04:54 Dave

A sticky note if you want and post it to your wall, whatever works for you. Low key, high key, low tech, high tech, whatever works. Anyway, once you have an idea of why you bought a company and you look at the reasons why it may or may not be a reason to hold.

00:05:12 Dave

Not, I think, then it becomes an easier way to do it and I guess to to think on it. And so that's I guess really how I try to think about it and it doesn't make it any easier for sure. So you mentioned the psychology of it. What are your thoughts on kind of how to work around you know the the mental aspect of selling?

00:05:34 Andrew

There is something about the way we are wired where we just really don't want to take a loss. We've talked before about how taking a loss kind of.

00:05:45 Andrew

Is a way of waving the white flag to say I made a mistake and that's hard and painful to do on its own. But there is something about I've come across it I I feel it myself. I've seen it in family.

00:05:56 Andrew

Numbers.

00:05:57 Andrew

You hear about it, we get questions about it. You just don't want to take a loss, right? And it feels better to say I'm going to wait for this to recover.

00:06:06 Andrew

Before I sell so you know, at least sell. Break even. I didn't lose any money and then I can buy something else. And so trust me, I understand the logic behind that. I understand the feelings behind that. The one thing that I try to hammer home.

00:06:21 Andrew

And probably not as successful as I would like of a message, but it's like.

00:06:21

It's.

00:06:26

Yeah.

00:06:26 Andrew

Yes, you can wait until that comes break even and you didn't lose any money. I'm playing this in air.

00:06:33 Andrew

Quotes.

00:06:34 Andrew

But what are you losing out on by not selling? So what else could you have bought in that time that you're waiting for it to break? Even that you're just going to completely miss out on because?

00:06:46 Andrew

You're scared to take a loss, so if it takes Disney four years to break even.

00:06:54 Andrew

Maybe you earn. I don't know. I'm just throwing random numbers out there. Maybe it takes four years for them to break even. The stock finally recovers. You're up 30% in four years. What if the markets tripled in that same time frame? Well, then now you're not feeling as smart. Because if you would have taken the loss in Disney RIP the Band-Aid off.

00:07:15 Andrew

And then bought something else that's done much better. You're at the end of the day.

00:07:19 Andrew

And in a.

00:07:19 Andrew

Better spot. That's how I would try to frame the reason why you want to pull the Band-Aid out. Try not to think of.

00:07:26 Speaker 1

If.

00:07:27 Andrew

Your when you bought and when you sold, but try to have a longer term horizon of like in five to 10 years, I'm going to have a better outcome because I found a better opportunity for a business that's maybe not struggling.

00:07:41 Andrew

Maybe a a stock that's a better deal. So it all depends on what your other options are and that's.

00:07:48 Andrew

That's kind of investing stock picking. At least that's the that's the game of.

00:07:52 Dave

It and that's the hard game of it.

00:07:56 Dave

How would you feel if?

00:07:58 Dave

Let's say the position sizing for example, let's say that that this company was, you know, 0.25% of your portfolio versus 7%. Would that influence your decision on?

00:08:12 Dave

Selling.

00:08:13 Andrew

Yeah, I think that's a great point. You're really trying to. It's different, right? Because you could be doing this part time, you could be doing as a hobby for me, somebody who approaches this from like a full time mindset. I'm trying to allocate my time to what's best for the portfolio. So in that kind of a scenario, it makes a lot more sense.

00:08:33 Andrew

For me to spend time.

00:08:36 Andrew

Research time on like to your point, the bigger position portfolio and not worry so much about little small positions. So yeah, I I totally see the logic in that, but I I know it's not always it's not as simple and I I fall to it, I fall victim to it too because when you have all your stock tickers on the spreadsheet.

00:08:58 Andrew

Human nature is to look at the ones that are doing the worst, and those are going to be the ones that drive you insane. So yes, logically we should all be caring more and spending more time on our biggest positions. Some of my best positions are my biggest positions and I spend not nearly enough time on them because they do. They do pretty good and it's like so.

00:09:18 Andrew

Logically counterintuitive, but that's the way we are wired as stock pickers. Yeah, for sure. The last question I kind of have is how do you, how do you feel about?

00:09:28 Dave

So.

00:09:30 Dave

This was some advice I got, you know, to kind of put it in perspective, so.

00:09:35 Dave

I had bought PayPal, which we've talked about at at Infinitum, and I won't go into all the details of that, but I bought a bigger position in PayPal and I bought a very small position in talent here. It's literally 100 bucks. And so I'd seen. So that was more of a psychology experiment than anything.

00:09:52 Dave

Because it was down for a year and a half or something like that. And I never questioned selling it because to me it wasn't. I don't want to say it wasn't a serious investment, but it really wasn't. And so it was $100. I was willing to basically gamble to see how it feel about investing in a company like that. And now it's, you know.

00:10:12 Dave

Thou.

00:10:13 Dave

5070% something stupid like that and it's interesting how my perception has changed about that positions because of the psychology of a being down and then being up.

00:10:24 Dave

A lot. So then you have that and then I have PayPal, which was down a lot, but it was because it was a much bigger position. To your point, it occupied way more of my time thinking about, you know, what do I do with this? What do I do this? And I got some advice from our friend Brian Withers, who suggested that I trim.

00:10:43 Dave

Instead of selling it out right, was trimming it. And so that's what I ended up.

00:10:46 Dave

Doing is I sold about half of what?

00:10:48 Dave

I owned and I feel better about the position. Also it it reduced my cost basis too. So it's closer now to where the original investment where it's trading at now. So it I feel I feel better about the position than I did before. So what are your thoughts about that like maybe trimming some of the position and then?

00:11:09 Dave

Seeing if it will recovers or something along those lines.

00:11:13 Andrew

Do you have a long-term mindset searching for safe compounders? So am I and I'm investing my entire life savings with the picks from valuespotlight.com.

00:11:24 Andrew

Yeah, I like that. That kind of mindset shift. So was there something about PayPal itself where?

00:11:32 Andrew

Maybe your conviction was lower than when you bought it, and so that kind of.

00:11:37 Andrew

Play this self out in the trim.

00:11:39 Dave

Yeah, for sure. I definitely felt that, you know, management wasn't taking the company in the right direction and it seemed like it just was underperforming compared to what the potential was. And so it's a little bit like watching, you know, a baseball player who you could see has all the talent in the.

00:11:52 Dave

Gold, but only hits 240 instead of heading 280. And you know lots of home runs. So that's the way PayPal felt to me. And so I guess at the the higher portfolio size, it felt like it was underperforming and now that it doesn't, now that it's not as big of a size 5-6 percent, 7% range and now it's one.

00:12:13 Dave

So it feels better if that makes.

00:12:15

Yeah.

00:12:16 Andrew

You, I mean, I did something similar to I had Starbucks as a 10% position. And so that's like putting it up there in one of my top biggest positions.

00:12:27 Andrew

And then out of nowhere, here comes Alphabet as a wonderful opportunity. So I was.

00:12:33 Andrew

Like.

00:12:34 Andrew

I was so frustrated. I was like, man, why didn't I wait to load up in the Starbucks?

00:12:40 Andrew

Wait, you know, wait to see if there be another opportunity. Felt like I, like, used up all of my opportunity on Starbucks. And then it's like, well, actually you can just trim it back. And if I feel like I did that Starbucks and alphabets opportunity was equal.

00:12:57

Hmm.

00:12:58 Andrew

Then.

00:13:00 Andrew

Trim the Starbucks and put them equally in in Alphabet and Starbucks and so that psychology for sure that.

00:13:08 Andrew

That helped my psychology of like worrying a lot less about Starbucks itself. I can't remember who the investor was. I don't want to say it was George Soros, but something's like whispering in my ear that maybe it was. It was in the bulk.

00:13:23 Andrew

And maybe this was a I don't think it was juggling green, but but somebody had written about this investor, he basically said.

00:13:31 Andrew

His gut would tell him when he had too much money in the position, or like if he couldn't eat or couldn't sleep or something.

00:13:41 Andrew

Like his body was physically telling.

00:13:43 Andrew

And.

00:13:44 Andrew

You're not making the right choice. That's why I thought that was very a very interesting thing.

00:13:49 Dave

Yeah, it is. It's funny, you know, we spend, we spend so much time obsessing about numbers and financials and all that stuff, but we're really drives our investment decisions and our returns is our brain and our stomach. Yeah. Yeah.

00:14:04 Andrew

Yeah. You know, there is wisdom to that.

00:14:09 Andrew

Like.

00:14:09

MHM.

00:14:10 Andrew

We all have strong convictions on the different stocks we buy. That doesn't make us right. If we're right 60% of the time, we're really.

00:14:17 Andrew

Good stock pickers, right?

00:14:19 Andrew

So to have these things where you're.

00:14:24 Andrew

Doing things in your portfolio to reduce the stress level, I think it's beneficial.

00:14:29 Dave

Yep, I totally agree. We'll agree. All right, so let's move on to the next question. So we got dear Andrew and Dave, love your show. Thank you for teaching me so much and giving me the confidence to be patient. I have two follow up questions about two of your favorite themes, Buffett and dividends. And he's got that right.

00:14:46 Dave

I read the Warren Buffett is committed to giving most of his fortune to charities and is supposed to be used relatively quickly. As much as I understand his fortune, as in Berkshire Hathaway stock, what does this mean for the price of the stock the day after? So that's the.

00:15:00 Dave

Question. The second question is I created a small dividend portfolio in order to learn more how it works for me. I wonder if I should use an auto reinvestment option or invest the dividends myself in stocks that are cheaper or more promising at the time regardless of the stock that it distributes. So this is a great question from offer. So let's let's tackle.

00:15:19 Dave

The the Buffett.

00:15:21 Dave

Question first, So what are your thoughts on the buffet question?

00:15:25 Andrew

I guess I'll kind of punt on it a little bit in that.

00:15:28 Andrew

I'm I haven't closely followed what Buffett's giving. I'm sure he's he's. I know he's publicized in the past, what he plans to do with his shares, what he is doing with the shares when it comes to his philanthropy. So I don't want to comment on the specifics because there could be short term. There could be short term movements that I'm just not.

00:15:48 Andrew

Aware of because of whatever he has said. But.

00:15:53 Andrew

Berkshire and probably Berkshire, more than even other.

00:15:56 Andrew

Stocks, but stocks businesses in general that are valued rationally in the market.

00:16:02 Andrew

The long term value of Berkshire stock is going to be based on the core Berkshire business, how Berkshires business does over the long term, so.

00:16:13 Andrew

Yeah, I mean, we could speculate about what what's going to happen with Warren Buffett and and all of this where the price is going to go in any given day.

00:16:22 Andrew

But you know, some billionaire could stub his toe tomorrow and decide to sell a bunch of his stock and something else.

00:16:30 Andrew

And you know, we can't predict any of that either. So I understand the question. I think it's good to think about a lot of these different factors. But to me this is one of.

00:16:37 Andrew

Those.

00:16:37 Andrew

Kind of short term, more than the short term bucket versus the long term bucket. So if you're holding Berkshire or you're thinking about Berkshire?

00:16:46 Andrew

I would just to me the longer term view is easier and more reliable way to try to think about analyzing the stock. Whether your thoughts on the whole Buffett, Berkshire kind of thing.

00:17:00 Dave

Well, I don't remember the specifics.

00:17:04 Dave

But he has said in the meetings.

00:17:07 Dave

Many times that he is going to give the vast majority of his wealth away to charities.

00:17:13 Dave

And he's going to leave a small amount for some of his family, but the vast majority is going to go to charities that I think. I think it was a large part of it, was to the Bill Gates Foundation, the Bill and Melinda Gates Foundation. But because of their divorce, I think that some of that might have changed again.

00:17:33 Dave

I don't remember the specifics of that. I also seem to remember.

00:17:38 Dave

That he was.

00:17:39 Dave

Going.

00:17:39 Dave

To.

00:17:40 Dave

Recommend that they sell the Berkshire stock and put it in S&P 500 index until the money is used for the specific charities and I believe some of the charities were already designated how much they were going to get and and whatnot, and I think his thinking was that.

00:17:59 Dave

By putting it in SP500 stock, it could try to remove some of the volatility that he probably is anticipating after he's no longer in charge of Berkshire. After you know, after he.

00:18:12 Dave

Passes questionably. There will be a drop. I don't know how big you know, it's anybody's guess, but I wouldn't say for certainty that I predicted that there will be a drop. But I think there would be a drop if there's a. What's the word? I'm looking for? A founder LED company that's driven by somebody's reputation more than Berkshire.

00:18:32 Dave

Other than Elon Musk and maybe Jeff Bezos at Amazon, I'm struggling to think of somebody that really, you know, helps drive some of the value just by the buffet.

00:18:41 Dave

Name and when he's no longer there, I think it will have an impact on the price of the stock. But the Anders point if.

00:18:49 Dave

The people that are taking over are as good as Buffett thinks they are, and we think they are. Then I'm comfortable owning personally. Berkshire after Warren is no longer there because the core businesses are intact. What he set up should can and should last for a long, long time. Really the.

00:19:08 Dave

The I guess the unknown is the whole equity portfolio, the stocks that he has bought over the years, you know the apples and American Express the Cokes and so on. But one of the things there's been some commentary on on Twitter recently that they some people think that he's reducing some of his positions in these companies to give.

00:19:28 Dave

Greg Abel, who he's anointed as his. His success.

00:19:31 Dave

Other the optionality to be able to do other things and not have to carry that burden of having 50% position in Apple. We were talking about stomachs earlier. That's a strong stomach kind of position for a company that size. And so I I think he wisely is probably reducing his exposure to that company to give Greg Abel more optionality and not have to deal with.

00:19:52 Dave

That that big of a headache taking over Berkshire, but that that's all speculation. He's not said that in words. I don't know that that's just other people saying it and me parroting it back. So take that for what it's worth. I guess that's kind of my thought on what I think he's going to do, what's going to happen and how he's planning on.

00:20:12 Dave

Using as well, which is awesome that he's going to do something like that instead of just giving to the the family and having them blow it in a couple of generations. It's actually going to go to use for.

00:20:21 Dave

Something good which is awesome.

00:20:24

What's the?

00:20:24 Speaker 5

Biggest problem? Most investors.

00:20:26 Speaker 5

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00:20:46 Speaker 5

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00:20:54 Andrew

Yeah, yeah, totally. What are your thoughts on the second part of the question?

00:20:58 Dave

My take is and this is what I do for myself personally, and I like it because it it removes me from the equation is that I just automatically renewed them. So if I own Google, which I do and they.

00:21:12 Dave

Pay dividend, which they now do. Yay. Then that dividend gets reinvested in more Google stock and I have 0 problems with that. I can see the logic of having the cash put in your account and then you can invest it in something else. I I see the logic of that, but I also know that the.

00:21:29 Dave

Way to continue compounding is to not interrupt it, and so if a company like Google is growing and then they're giving me dividends that I can reinvest in a growing company without me having to do anything, then to me that's kind of a no brainer. And again, it takes me out of the equation. It's it's one less decision I have to make and if I like the company enough to own it and continue owning it.

00:21:50 Dave

To me, that's that's an easy decision because that Google stock is gonna be more valuable than if I obsess about something for the next four months and spend $0.42 on buying, you know, a portion of that company, it's, you know.

00:22:04 Dave

Just not. I don't think that's the best use of your time and and effort. For me, I would do that. I see the logic, but that's how I would do it with I.

00:22:11 Dave

Think I know how you would respond.

00:22:16 Andrew

Alright, I love that. Like how you describe that like the last decisions you can make in theory, the better decision making you will make. So reinvesting to your point reduces the number of decisions you have to.

00:22:35 Andrew

And it's like you're going to handicap some of your best ideas because you're trying to always find new ones. There's there's a lot that could go wrong. And yeah, I mean, you'll get some stocks where I'm glad I did that, but you'll get others where you're like.

00:22:50 Andrew

Google, why didn't I just leave it in?

00:22:51

Right.

00:22:52 Andrew

There, you know. Right. So yeah, like how many?

00:22:56 Dave

Times. How many times have all of us raise our hand? Look at something and we didn't buy it. And then you look six months a year, two years later and it's up 72 percent or something crazy like that. And you didn't have the chance to buy it. I'm such an idiot. I mean, it's the same feeling with reinvesting the dividends. At least that's the way I look at.

00:23:14 Andrew

It. Yeah, I mean.

00:23:16 Andrew

Some of my best stocks are the ones I pay no attention to, so yeah, like.

00:23:22 Andrew

Is there some inverse correlation between like how excited we get about the stock and like I'll go, how well it performs possibly so all that Moe's too simple.

00:23:26 Dave

Yes.

00:23:29 Dave

Right.

00:23:34 Dave

The less I look, the better it does. OK that. All right, stop looking so much correlation. Causation. Let's move on to the next one. So we have. Hi, Andrew. This has been a really interesting and I think I've got my first DCF working. So Congrats, I have run a sensitivity analysis on the first company I've valued. As I am aware.

00:23:36

Yeah, yeah.

00:23:54 Dave

Changes in inputs can significantly alter the valuation.

00:23:58 Dave

Do you have any guidance on comparing the DCF valuation to the current share price in terms of a decision on whether to buy or not? For example, I have valued a company whose fundamentals look good to me, but my valuation is around 25% below the current price. Many thanks, Joe. So fantastic question, Joe. And what are your thoughts on this?

00:24:17 Andrew

Do you want to break down DCF?

00:24:19 Andrew

Real quick for somebody who's yes.

00:24:21 Dave

So to jargon aware everybody DCF stands for discounted cash flow and it's a valuation model that you can use to help value a company and it it basically what it does is it takes.

00:24:36 Dave

Free cash flow that the company earns and IT projects it into the future and then it discounts it back to the present value for today, basically accounting for any impacts on on inflation on the cost of money and the basic premise is a dollar today is worth less than a dollar five years from now because of the impact of something like inflation.

00:24:58 Dave

So when you run a DCF, what you're doing is you're trying to find determine the value of a company 10 years in the future, but valuing it as today's prices and trying to determine whether it's, you know, a good price or not. Kind of like buying a car or shoes. Same kind of idea.

00:25:13 Andrew

Yeah, like if you put 100 bucks into a savings.

00:25:15 Andrew

Account you.

00:25:16 Andrew

Can you can assume where you think they'll be in 10 years? And yeah, you just get some simple compounding from that and then you can assume this probably won't buy me a Big Mac.

00:25:22 Dave

Yeah, exactly.

00:25:25 Andrew

In 10 years either.

00:25:26 Dave

Probably not.

00:25:29 Dave

No.

00:25:30 Andrew

I mean, we joke, but that's kind of how DCF works is you are accounting for inflation and everything.

00:25:35 Andrew

So to me, I think it's telling that.

00:25:39 Andrew

You like the fundamentals, but then the DCF is telling you maybe this thing's 25% too expensive. I think that's a good thing. I think one of the values of a DCF tool for me personally is that if I'm really excited about the stock, the DCF can kind of.

00:25:56 Dave

He like breaks on.

00:25:57 Andrew

Hey, yeah, like put the brakes. Like maybe this thing's a little expensive. And so then now you can relook at the fundamentals and like, do I still think that these fundamentals are really great or not? Not to say that they're bad, but you take a second look, you try to be more rational and then maybe that can help you decide whether it's.

00:26:17 Andrew

That's a buy or not, but the DCF kind of puts that barrier there to.

00:26:22 Andrew

Or see the thing.

00:26:24 Andrew

Deeply think again and kind of put put some time between like your excitement and the final buy decision.

00:26:32 Andrew

I think it's good that DCF came up like that because now you have, you can go back and reevaluate.

00:26:38 Dave

Yep, I agree. I agree. The the power of the the DCF or using any kind of model is the thought process that goes into determining what the inputs are going to be.

00:26:50 Dave

And.

00:26:51 Dave

Yeah, you can plug in numbers and just, you know, see what it spits out and that's easy. But if you're trying to be a thoughtful investor, then you have to think deeply about the inputs and their impacts on the valuation. You have to always remember too that evaluation using a DCF in particular is sensitive to the inputs that we put in.

00:27:14 Dave

And bottom line is they're.

00:27:16 Dave

Passes. I mean, we do not know for sure how much Google will grow tomorrow. We just don't. And to think otherwise is foolhardy. And so when you are valuing the company, really the the power of it comes into analyzing the fundamentals like Andrew was talking about determining what is the.

00:27:36 Dave

What is the mode of the company and how does that impact the growth in the future of the company? And you take a company like Google, which appears to have a really strong mode.

00:27:46 Dave

In a growing mode, and that indicates that maybe the growth that you could anticipate could be good for a long period of time, but if you don't really understand the fundamentals of the business, it's really hard to assess that. And so when you're using a DCF, it's really it's not a tool to help you figure out exactly what it is you're going to pay.

00:28:06 Dave

It's a tool to figure out if you're in a ballpark of whether you think this company is fairly valued or has an opportunity for it to be good.

00:28:14 Dave

Investment. Some people can mistake them as like I'm I'm looking for the exact value I'm willing.

00:28:20 Dave

To buy at.

00:28:21 Dave

You know, I run the DCF and the the the value comes up at let's say 50 bucks and you know I will buy if it's at 4892, but you know a penny over that. I'm out and that is missing the forest for the trees.

00:28:35 Dave

And so you need to try to make sure that when you're using any of these kinds of models, it doesn't matter where it's a DCF or reverse DCF dividend, discount model Shoals, Black Scholes model, any of those kinds of things.

00:28:48 Dave

That your.

00:28:49

Or.

00:28:50 Dave

Understanding the inputs that you're putting in and you have a good good handle on the business and all the different components of the business and that's really what a DCF helps you do is because it forces you to confront those fundamentals and understand if you have a good handle on the company and this is a great question to ask yourself.

00:29:11 Dave

You know, as Andrew was saying, if it if it comes up as overvalued, then it it really forces you to go back and look at the fundamentals that go. It was that right, you know, is this is the balance sheet really that strong? Are they really investing?

00:29:23 Dave

Yeah. Well, I mean, those are core questions to ask and we all make mistakes and the DCF can help you catch those. And that's one of the things I love about using a DCF.

00:29:34 Andrew

Well, actually yesterday in our evaluation of Hackathon Gilbert, you know, we were doing the evaluation for JP Morgan Chase with the the aftermath of the election and everything Gilbert said like.

00:29:41 Dave

Yeah.

00:29:46 Andrew

Just that process as we were walking through as I was sharing my screen, he was like this helps me think about.

00:29:54 Andrew

Shareholders equity helps me think about the loan book like just by going through those steps, you are helping your brain walk down the path of analysis. And that's actually a hard thing to do. Like, it doesn't come naturally to just say, OK, I'm going to research this part of the business and then this part of the business and that part of business, I mean for me like maybe I take it to an extreme in my life.

00:30:15 Andrew

Like if I have to remember to grab my laundry, I'm putting the laundry basket in eyesight. Otherwise it's gonna stay in the dryer for three days. Right? So for me, I need those visual cues, but.

00:30:25 Andrew

As investors, I think that can also be the different types of queues. DCF valuation is a great way to queue your mind to look into these different parts of the business, to your point to look at the reinvestments and and really try to deeply think about what we're analyzing.

00:30:42 Dave

Yep. Yep. Exactly. Yep.

00:30:45 Andrew

Well, last thing I'll throw in with that is try to think about what the growth rate is too, like you might be OK.

00:30:54 Andrew

Paying 25% too much if you think the company is going to grow like 12% a year. If you have a.

00:31:00 Andrew

Good reason to think that.

00:31:03 Andrew

So the growth rate also matters. So I like to go and excel and like project out the growth rate and see you know, even though it's something's expensive, does the company grow into that?

00:31:15 Andrew

The numbers are going to kind of play out how they are, but that to me.

00:31:18 Andrew

That has also.

00:31:19 Andrew

Helped. It's actually been a game changer in.

00:31:22 Andrew

The way I picked socks as well, like, it's not just about how cheap or how expensive, it's how much growth am I going to get.

00:31:30 Andrew

And then and then you bake in how cheap or expensive? I mean something might be 25%.

00:31:36 Andrew

Cheap.

00:31:36 Andrew

But is that 25% cheap only going to grow like 3% a year?

00:31:41 Andrew

Maybe for something that's that's appealing, but for me, I'm looking for something different, so trying to think about growth too, not.

00:31:47 Andrew

Just if it's cheaper.

00:31:48 Dave

Expensive. Yeah, that's very, very good take away. It's super important to consider cuz that's that. That's baking in part of your returns, right? Yeah. So.

00:32:01 Andrew

Yeah, hopefully that answers the question. Hopefully it gives you more insights and you know the DCF.

00:32:07 Andrew

To him to like, beat the dead horse. It's part of the process. It's not the end destination. The valuation hackathons can be a great way to test your DCF in the wild. Work with Dave and I and do DCF's together. So that's part of value spotlight. If listeners out there haven't heard about that, we do regular.

00:32:27 Andrew

Valuation.

00:32:29 Andrew

We're on zoom. We're breaking down any company you want. We did. We did lululemon yesterday. And JP Morgan Chase, so no company was off limits. And that was that was pretty fun. So shout out to Gilbert for being there with us and giving us some ideas. And if you want to be a part of that, that's all inside.

00:32:36 Dave

Yeah.

00:32:38 Dave

No.

00:32:48 Dave

Spotlight. Yeah. Yeah, exactly. It's well worth the time. I know, I know. I learn a lot.

00:32:53 Dave

It's fun. All right. Well, with that, we'll go ahead and wrap up our show for today. I wanted to thank everybody for taking the time to send us a fantastic questions. Again, if you have any questions, you can send them to us at newsletter at investing for beginners.com. That is in the show notes. You can also send them to us via Spotify, the app that you would be probably listening to the show on, or you can reach out to us.

00:33:14 Dave

On socials, in particular on X or the Twitter machine.

00:33:18 Dave

So any of those places you can reach out and ask US questions and we'll go ahead and answer them on the air for you and help you out. So with that, we'll go ahead and sign us off. You guys go out and invest with the margin of safety emphasis on the safety.

00:33:29 Dave

Have a great week and we'll talk to you next week.