IFB273: Banking Crisis Averted/Building a Portfolio/Performance Compared to the S&P500

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Dave

0:00

All right, folks, welcome to Investing for Beginners Podcast. Today we have episode 273. Before we dive into the show, I have a little quick message for everyone. We are doing a listener survey, which is to help us get to know you, our listeners, your interests, and what you guys think of the show. So please support us at the podcast by taking our short questionnaire, you can find it@surveymonkey.com backslash, our backslash airwave, it'll only take a few minutes, and your feedback will help us improve the show, and what we present to you as well as advertising and everything else.

For your time, we are willing to give out, we're going to be giving out a drawing for a 500 hour Amazon gift card. This will be through our podcast host airwave media. So please check out the surveymonkey.com backslash, our backslash, airwave, or you can check it out on the show notes. So with that done, let's go ahead and kind of dive into the show. So we're gonna answer some great listener questions that we got recently.

The first one is concerning the situation, the banking situation with Silicon Valley Bank, or SVB, and kind of what our thoughts are on that, as well as just the whole banking situation that's really dominated the news over the last few weeks. So, Andrew, I guess I'll let you take first wing sounds

Andrew

1:18

good. I mean, I feel that embedded in this question is a different question. I will answer the original question, don't worry. But I just want to say as a individual investor, you, Dave, we were talking about this before, you don't have to have an opinion on everything. And actually, the less opinions you have on things that are going around in the finance world, probably the better your performance will be.

And so to be a good investor, you don't have to know what's the Fed gonna do next month? Or are we going into a recession, or whatever the clickbait title is, because as long as you're investing in a group of companies, and the economy grows, your investments will grow along with them. And that's really what's important.

You know, I have a couple investments in a couple banks, I own Bank of America, I own JP Morgan. So obviously, I have thoughts on what's been going on lately. But I don't feel like I have anything that's a special insight. And it certainly hasn't changed my philosophy on owning those stocks. But I'm happy to share it. What about you,

Dave

2:25

I'm kind of of the same ilk. And I think the idea that you don't have to have an opinion or know everything about everything is really spot on. And it kind of goes to that idea of operating within your circle of competence, and operating around the areas that you feel comfortable and know something I didn't stay at a Holiday Inn Express. So I don't know everything. For those of you who remember that commercial from way back when I think having an opinion about things he has is great.

But you don't have to have an opinion about everything and know everything about everything, I have spent a fair amount of time playing around with the whole banking world and the finances, and financials, because it's something that interests me. And so I understand what happened at Silicon Valley Bank, to a certain extent, but I haven't really dived into it deeply, because it just It doesn't concern me.

And it's not something that really affects what I'm doing on a day to day basis, as well as the companies that I do invest in I own Ally Bank, I also own JP Morgan and I also own Wells Fargo, lots of Wells Fargo, unfortunately, but that's a whole other conversation. But the I guess my point with all that is that, even though you may understand the ins and outs of it, it's going to be very complicated. And if you're a newer investor, diving into something like that, unless you really, really, really want to know, is really going to take you down a very deep and very complicated rabbit hole.

Investing in banks and insurance companies. And other of that, like involves understanding accounting very deeply involves looking at the balance sheet very deeply. And it involves speaking a different language, because there are things like the the city ratio, and the efficiency ratios, which are things you do not have to worry about if you invest in Microsoft, for example. So that being said, I think it's important to understand these things and know these things. But as far as how it affects your overall performance in the stock market and your day to day life, it's just not something that's really you need to know. And I think to Andrew's point, you know, knowing what the Feds going to do, you know, understanding who's going to win the March Madness. I mean, those things don't really impact our investing on a day to day basis. And it's a lot of its clickbait. And a lot of it is really get you to react to something and make a decision one way or the other. And if you're really, really curious about these things, there are lots of other great financial podcasts out there.

Like our friends, Braden Simone at the Canadian investor podcast recently did an episode about what happened at Silicon Valley Bank and so that if you really want to know, well, you can listen to them and they'll talk more deeply about it. But to date for Andrew and I, it's just not we'd rather just focus on things that we can control and things that are going to be useful for us. What's up Let's move on to the next question. Let's move beyond banks. By the way, Braden, and Simone did a great job with breaking that down. So just an FYI. Here's the next question.

I found you online and listen to your podcast. It is very enlightening. I am about to embark on the dividend journey following your recipe. I am wondering when you realize that you have invested enough in one particular stock before moving on to another as you build your portfolio? This is a great question. So Andrew, what are your thoughts on this?

Andrew

5:26

So when you're building a portfolio, I think it's important to have a couple of key principles, we can all build our own personal portfolio look at all look many different ways. But when you build a portfolio, take it back to the basics, what's important. Remember, we're building this for the long term, because nobody can guess what the stock market's going to do tomorrow.

But we know the economy is going to grow. That's what we believe in. So over the long term, our investments will do good. So you're going to put these investments, you're going to hold them for a long time. That's the goal. Number two, you're going to diversify, which means I might love my Apple iPhone, and think Apple is the greatest thing ever. But I'm not going to put all of my money in Apple stock.

Because even if I'm right, that was bad risk management, you don't want to put all your eggs in one basket, because no company, no single company is immune from the realities of capitalism. No single person's immune from the realities of living on this earth. So you spread it out. So if you're doing these things, right, you're the last thing would be dollar cost averaging, tried to put the same amount every single month, because that's how you get around the whole problem of trying to market time, it's impossible to time the market. And so if you're not dollar cost averaging, that's basically what you are doing. So instead, if you dollar cost average, you're putting money into the market all the time, over the long term.

That's how you beat market timing. So with those three kind of pillars in place, diversification, long term investing, and dollar cost averaging, ask yourself, Okay, how do I do that? So for the individual investor, probably the easiest way I can think of is to build a portfolio, whether it's 1520 2530, whatever you're comfortable with, of stocks. And how do you do that? Well, I kind of go back to how I did it with the E leather, when I first started that out, and there was just a new stock every month.

And then as the months go on, you give it like a couple of years, and you're basically have full diversification. So that's one way you can do it. You could just buy an index fund and get instant diversification in that way. But if you're buying individual stocks, buy until you're fully diversified. And then you can obsess endlessly about how to optimize after that. But I would start by getting diversified, but not necessarily doing it too fast to like, I liked the idea. And the reason I say that, and I've said this a lot.

But the reason I say that is like let's say I wanted to diversify today, right, I just wanted to buy 20 stocks? Well, I can't tell you what great opportunities are and 20 stocks, it's hard enough to find one at any given time, just to say this is the best opportunity today. Oh, that's why, you know, to me, it's build this over time. Because if you're gonna be investing for 20 years, what's the two year ramp to build up your diversification? That's how I see it?

Dave

8:25

Yeah, that's how I see it too. Can we back up for just a second? And maybe people that are newer to the show kind of explain the idea of diversification? What exactly that is?

Andrew

8:34

Yeah,basically, diversification, I guess the easiest way to think of it is you're splitting your money up, whether that's equally or in chunks, but you're buying multiple stocks. So that again, if anything bad happens to any one company, you're not absolutely crushed by that happening. I've heard people recommend 10 stocks, I've heard people recommend 20 stocks. 25 to 30 is another common range, as long as you're, you know, splitting it up. So you're not all in one industry or all in one company, then that's how you get diversification. And so it helps you more depend on the growth of the economy instead of the growth of any one company because companies do fail. And so you try to avoid against that.

Dave

9:20

Yeah, and the different sectors in different industries can struggle from time to time. Like right now. For example, software as a service type companies have been on the struggle bus over the last year plus, whereas a few years ago, they were the cat's meow, everybody wanted them so it can go in spurts and having a splitting up your portfolio into different buckets can help you mitigate that risk and reduce the long term effects of some of those things.

And that's actually something that I'm struggling with right now with my portfolio is I got too concentrated into payments slash financials with different kinds of insurance company He's banks, fintechs, all those kinds of things. And so now I'm trying to work towards this kind of idea of diversifying my portfolio better.

And I'm actually using a lot of the picks that Andrew has worked through to help me do that, because his focus is not on those. And so because of that, he's found some great companies outside of that area that are great investments that I've been working in, it's something we were actually talking about off air earlier, was how can I kind of balance some of the great new ones he's taking, versus the ones I already have in a portfolio and make sure that I build them up enough. And so those are ongoing things and kind of like he said, you know, obsessing about the how you want to optimize your portfolio, you know, if you want to have 10%, in this one, and 4% in this one, and 6% in this one and 3% in this one, those are fun games that you can play, once you get to, you know, whatever you feel comfortable owning, for me, it's going to be in 20 to 25 range. That's what I feel like I can manage and keep track of. And right now I have about 17.

So I still have a little bit of ways to go. But it's going to be it's going to be fun, but it's a great question. I think a lot of people worry. Or sometimes they focus so much on the companies that they forget that they have to manage, you know, not having 25% and one and 2% and and other that they have to kind of meld that out a

little bit. I mean, to each his own, I guess is a good way of putting it. But for me, it's better to have a little more diversification a little more spread out.

But there is no hard and fast answer to this question. I think it depends on what your total amount of companies you want to own. And then once you get there, kind of endlessly obsessing about optimizing the percentages that you want to have a great rule of thumb that I came across recently, I can't remember if Andrew told me this little tidbit or if I read it somewhere, but let the winners decide what the portfolio percentage would be. So if you invest in a company, let's say it becomes 2% of your portfolio. And then because the company does so amazing that it becomes 10%. That's an awesome place to be because it's, you know, it's done so well that it's grown to be a bigger portion of your portfolio. And those are fun things to see.

So I hope that helps answer your question. And just remember, try to diversify as you get up to the total number you want. And then you can start worrying about percentages of allocation from there. And I think that'll get you a long ways to where you want to go. Alright, so the next question. So we have Hi, Andrew, I just purchased your monthly e letter. Thanks for all your insights and help as a beginner like me to get focused on retirement investing. One question I have is how you perceive your portfolio's performance against the s&p 500.

This stood out to me as yours is behind the index. I'm mainly asking because I want to be the most wise with my money to ensure it grows best. From what I'm seeing, shouldn't I invest in the s&p over your picks? I asked this with the utmost respect and just trying to better understand Kind regards, Noah. So Andrew, I'm gonna let you take first stab at this.

Andrew

13:05

Yeah, it's a great question. So to give context to the question, I started the newsletter in October 2014. And again, it's tracked a real money portfolio. And so throughout the years, it has outperformed the s&p 500 and underperformed the s&p 500. And so where we stand today, March 2023, if you were to start investing $150 a month at the inception of the newsletter, which was October 2014. And you were to do that in the s&p 500. And you're also to do it in the E leather, you would have more money in your s&p 500 than in the E leather today. So what happened there.

So I look at the evolution of the leather and the types of companies that were in there. And so starting out, if you look at the very beginning, it was very much a cigar butt kind of thing, trying to find stocks that were very,

very statistically cheap. And I did that for probably six years, pretty much up to the pandemic, trying to get the best of both worlds. Where, you know, you'd have the buffet approach of holding something for a very long time and picking something that's really statistically cheap.

And I found that I performed better when I would not hold for a long time, by itself quickly. But my psychology as investors, I feel better about holding something for a long time and letting the company do the work. So at a certain point, I realized that that's the way I want to go. And the portfolio started to change into better quality names and less statistically cheap names.

And so as Evolution has happened, the performance has improved. But there were some kind of talking about the diversification, again, the portfolio had some very concentrated positions 20% 25% statistically cheap companies that weren't the best companies that ended up really hurting the long term performance of the portfolio. So, obviously, I wouldn't be selling the newsletter if I thought that your money was better spent in the s&p versus the newsletter, but that's where the portfolio has been.

And that's where it's going. It's more focus on company moats, what's the best company to buy here, it's still going to be cheap, based on the number not cheap, not the right word, it's gonna be a fair price based on the numbers. But it's not gonna be about buying the most dirt cheap companies and trying to hold those for long term. Because that didn't end up well.

Dave

15:54

And I think the thing that I'm kind of hearing is that, like Warren Buffett, you kind of went through an evolution in how you kind of invest, value investing is still important. But it's more the way that Warren does it today, versus the way that he did it early on with Ben Graham. And his early investing was very much the cigar butt turn and burn, buy cheap, sell it when it gets to fair value and move on to the next thing.

And very statistically driven. And I guess it feels like to me, you've gone more the way of the numbers are very important still, but qualitative is becoming important as well, or even maybe not as important, but equally as important as the numbers were, whereas five, six years ago, we I don't think we could have said that. Yeah, that's very fair way to do it. So how was the portfolio done? Kind of since you've made the change? You know, to me, it looks like, you know, a completely different type of portfolio than it was even three years ago.

Andrew

16:59

Yeah. Well, from the behind the scenes standpoint, I got you involved, which has helped immensely, because we've sorted that there's so many big portfolio decisions together versus me having to do it myself. And so you could track that back to, to that period. And it has done, it has beaten the s&p on a one year and two year basis. And it's closing, and I'll be there on a three year basis. So, you know, it's just a couple of years. So you can't make any big conclusions from it. But it does appear to be working now, using this approach versus the strictly quant approach.

Dave

17:38

Exactly. But I think the moving away from the quant to more of a mix of qualities, I think also doesn't take away from the fact that you're still trying to find companies that are selling for a fair value or less than the fair value. The dividends are still important, critically important, you are not buying anything that doesn't have a dividend.

And trying to hold for a long time is still, the main focus of the portfolio is just that the quality of analysis has changed in our taking into more experience and more factors and that impact what you buy and what you sell. And that's exactly what Warren Buffett has done. And as someone who did not beat the s&p 500, the last two years. Personally, you know, I know what a feat that is to do. It's an easy thing to do. And I applaud you for all the changes that you've made. And I know it hasn't been easy.

Andrew

18:37

Data definitely hasn't. But I feel like investors have to figure out what are you most comfortable doing? And sticking to that if the numbers bring your comfort, maybe a quants feather if holding for the long term is better, maybe a little bit more quality. Those are good decisions to make. And you don't have to make them all at once. But I think moving in that direction over the long term, can do really great things for your results.

Dave

19:03

I totally agree. And I think the other thing that I take away from what I've seen of your evolution is that this is the idea that you're going to start investing one way and finish the game ending the same way, I don't think is

a realistic idea. Because the more people experience, the more wisdom they gather, the more times that they do something naturally things are going to morph and evolve.

And you'll find things that work really well and then you'll find things that won't work really well and you're able to more quickly sort through the poor choices versus the better choices and your selection process just gets a little bit better. And I think that it becomes not easier but it does becomes easier with more repetitions to find the good from the bad. And I think in any fear but particularly in investing and if you look at any The Great Investors through the years, all of them have kind of evolved through the years. And it's just I think it's just a natural process. And so I applaud you for doing that. I know again, I know it hasn't been easy.

Thanks. You're welcome. All right. Well, with that, we will go ahead and wrap up our conversation for today. wanted to thank everybody for taking the time to send us those fantastic questions. Those are great. Please keep them coming. We hope you guys enjoy our conversation and get some good information and takeaways from all this. Before I sign off, I need to remind you again, please support the podcast support us by taking a short listener questionnaire@surveymonkey.com backslash, our backslash airwave or click on the link in the episode show notes.

And with that, I will go ahead and wrap us up you guys go out there and invest toward the margin of safety. Emphasis on the safety. Have a great week, and we'll talk to y'all next week.

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