Finding Long-term Investment Opportunities During The Current COVID-19 Crisis

By Chong Ser Jing
thegoodinvestors.sg

Disclaimer:

All information is provided by Chong Ser Jing. Any information, commentary, advices or statements of opinion provided here are for general information and educational purposes only. It is not intended to be any form of investment advice or a solicitation for the purchase or sale of securities. Before purchasing any discussed securities, please be sure actions are in line with your investment objectives, financial situation and particular needs. International investors may be subject to additional risks arising from currency fluctuations and/ or local taxes or restrictions. The information contained in this publication are obtained from, or based upon publicly available sources that we believe to reliable, but we make no warranty as to their accuracy or usefulness of the information provided, and accepts no liability for losses incurred by readers using research. Content, information, commentary and opinions are subject to change without notice. Please remember that investments can go up and down, including the possibility a stock could lose all of its value. Past performance is not indicative of future results.

Presentation format for today

- Section 1: Introductions
- Section 2: Understanding what the stock market is
- Section 3: The right mindset to have for successful investing
- Section 4: My investment framework and how it can be used to build a portfolio
- Section 5: How to find investment opportunities during this COVID-19 crisis
- Section 6: Q&A

Brief introduction of myself and Jeremy Chia

Myself

- Invest in US stocks since Oct 2010

- Graduated from NUS Engineering in 2012

- Joined Motley Fool Singapore as investment writer in Jan 2013

- Became co-leader of Motley Fool Singapore's investing team in May 2016 and left in Oct 2019

Jeremy Chia

- Graduated with MBBS degree in 2014

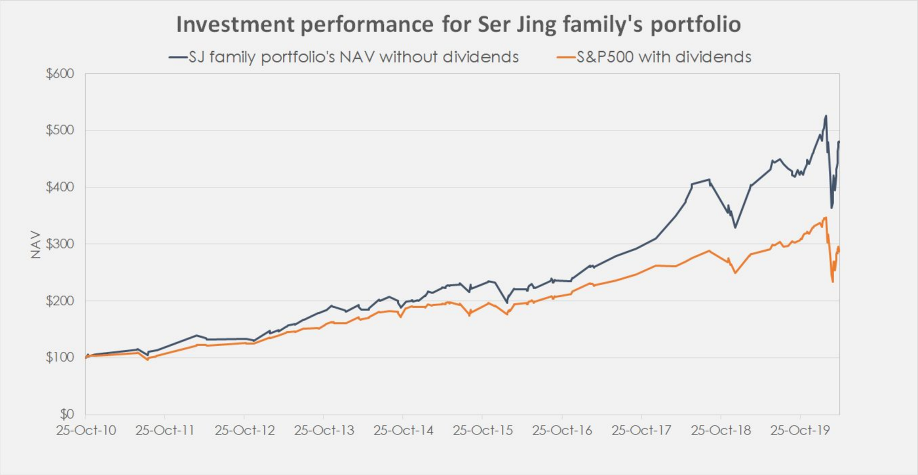
- Joined Motley Fool Singapore as investment writer in June 2017

- Has over 1,000 bylines under his name

- Has attained his CFA level 2 badge

My investing experience

Family's portfolio, Oct 2010 - today (unaudited)



With the Motley Fool Singapore

Flagship investment newsletter, *Stock Advisor Gold* (SAG), launched in May 2016

SAG return (May 2016 - Oct 2019)	Global stocks return (May 2016 - Oct 2019)
30.6%	16.4%

What we're working on

- ***The Good Investors*** (thegoodinvestors.sg): Jeremy Chia and myself

- **Compounder Fund**: Jeremy Chia and myself

COMPOUNDER FUND
GROWING YOUR WEALTH AND ENRICHING SOCIETY

Understanding the stock market

- First stock market appeared in the 1600s in Amsterdam

- Things have changed, but **the stock market is still a place to buy and sell pieces of a business → A stock will do well if the underlying business does well**

Understanding the stock market



- **The stock market lets us be silent partners with the best business leaders in the world!** (Above: Warren Buffett, Mark Zuckerberg, and Jeff Bezos)

Understanding the stock market

- Warren Buffett's Berkshire Hathaway shows how a stock will do well if its business does well

Berkshire **book value per share** (1965 - 2018)	Berkshire **share price** (1965 - 2018)
18.7%	20.5%

- 20.5% annual return for 53 years **turns $1,000 into $19.6 *million***

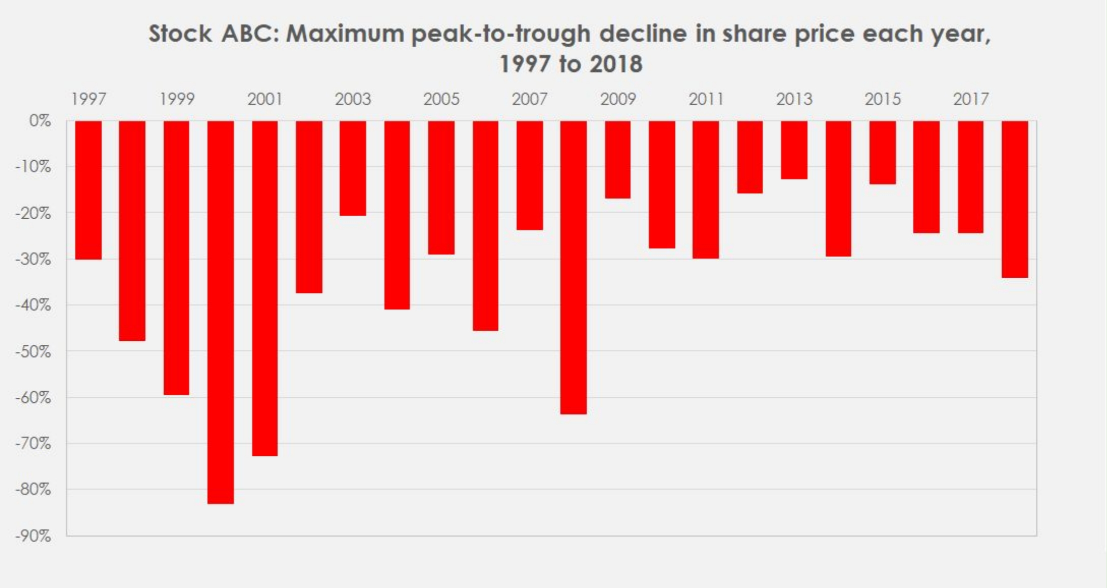
The first mindset

Which stock will you pick? Stock ABC or Stock DEF?

Stock ABC:

(a) Listed in 1997

(b) Top-to-bottom fall in share price for each year from 1997 to 2018 → 13% to 83%



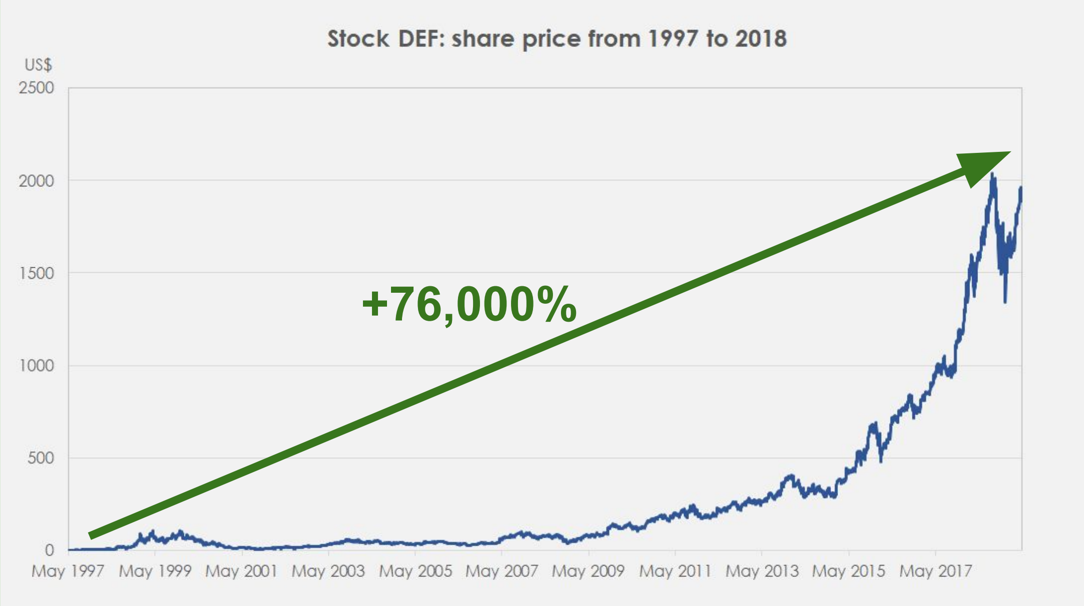
The first mindset

Which stock will you pick? Stock ABC or Stock DEF?

Stock DEF:

(a) Also listed in 1997

(b) Stock price from 1997 to 2018: US$1.96 --> US$1,501.97



The first mindset

Which stock will you pick? Stock ABC or Stock DEF?

- Which stock will you pick?

- Stock DEF is Jeff Bezos’s US e-commerce giant, Amazon

- Stock ABC is….

  also Amazon!!

The first mindset

- Peter Lynch: "In the stock market, the most important organ is the stomach. It's not the brain."

V.S.

- **Mindset No.1: Volatility in stocks is a *feature*, not a bug**

The first mindset

- Economist Hyman Minsky (1919 - 1996): largely ignored when he was alive, but gained popularity after the 2007-09 financial crisis

- Minsky theorised that stability is destabilising

- If stocks were guaranteed to rise 9% per year → Investors pay up for stocks → Stocks too expensive to return 9% per year, or market becomes fragile with debt (due to investors borrowing to invest) → When bad news happen, stocks fall

The second mindset

- When stocks fall, it hurts, and when it hurts, we make mistakes

	Peter Lynch	Average return for Peter Lynch's investors
Annual return (1977 to 1990)	29%	7%
What $100,000 would become	$2.7 million	$241,000

The second mindset

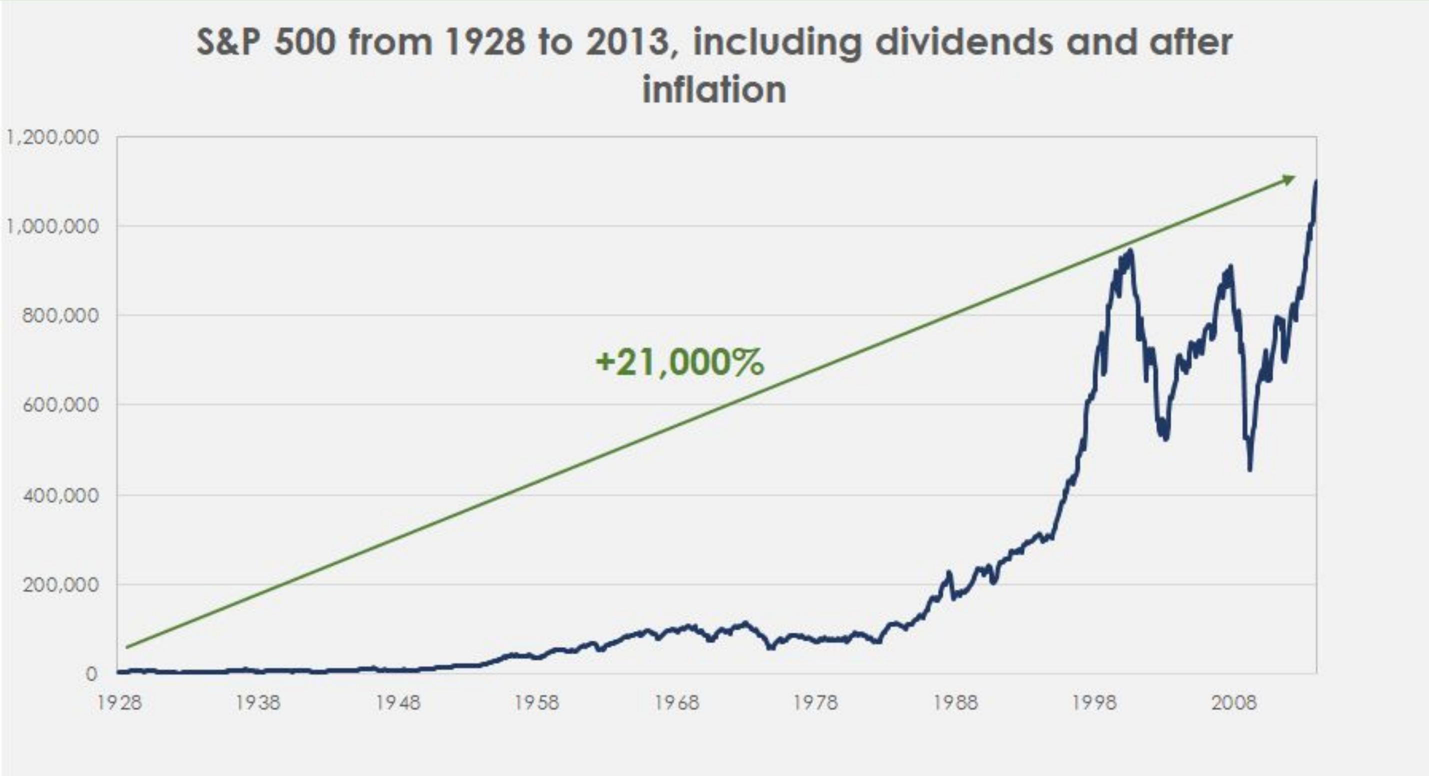
- Great way to think about volatility is to see them as a **FEE** and not a fine
- **Mindset No.2: Instead of seeing short-term volatility in the stock market as a fine, think of it as a fee for something worthwhile – great long-term returns**

The second mindset

Percentage decline in S&P 500 (from 1928 to 2013)	Historical frequency
10%	Every 11 months
20%	Every 24 months
30%	Every decade
50%	2-3 times per century

Source: [Morgan Housel]

The second mindset



Source: Robert Shiller data

The third mindset

Mindset No.3: What goes up, does not come down permanently

Source: [Credit Suisse]

The fourth mindset

- Factors for a single stock or single country's stock market to perform poorly for decades: (1) Devastation from war or natural disasters; (2) corrupt or useless leaders; (3) incredible overvaluation at the starting point

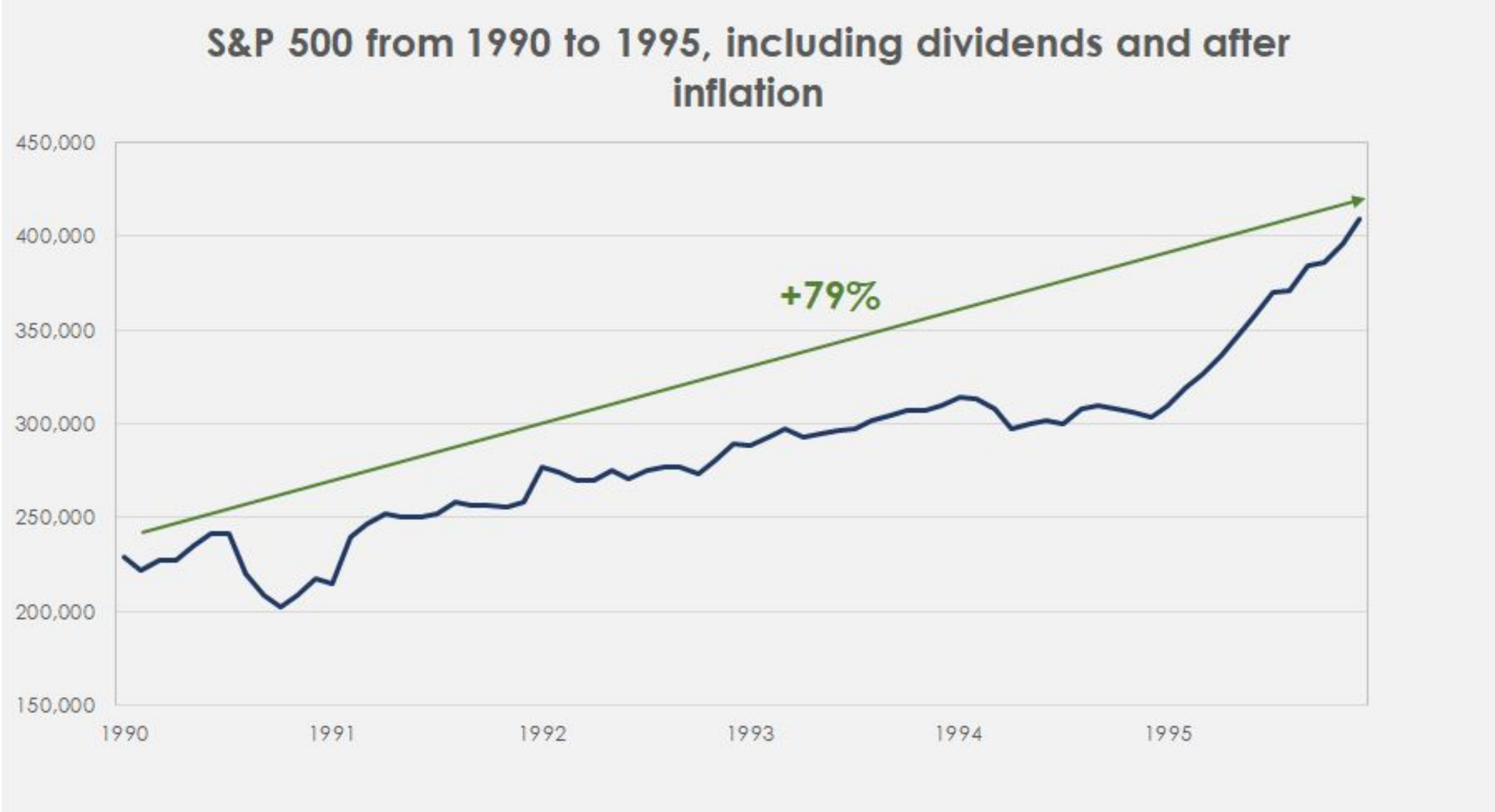
- **Mindset No.4: It is important to diversify across geographies and companies**

The fifth mindset

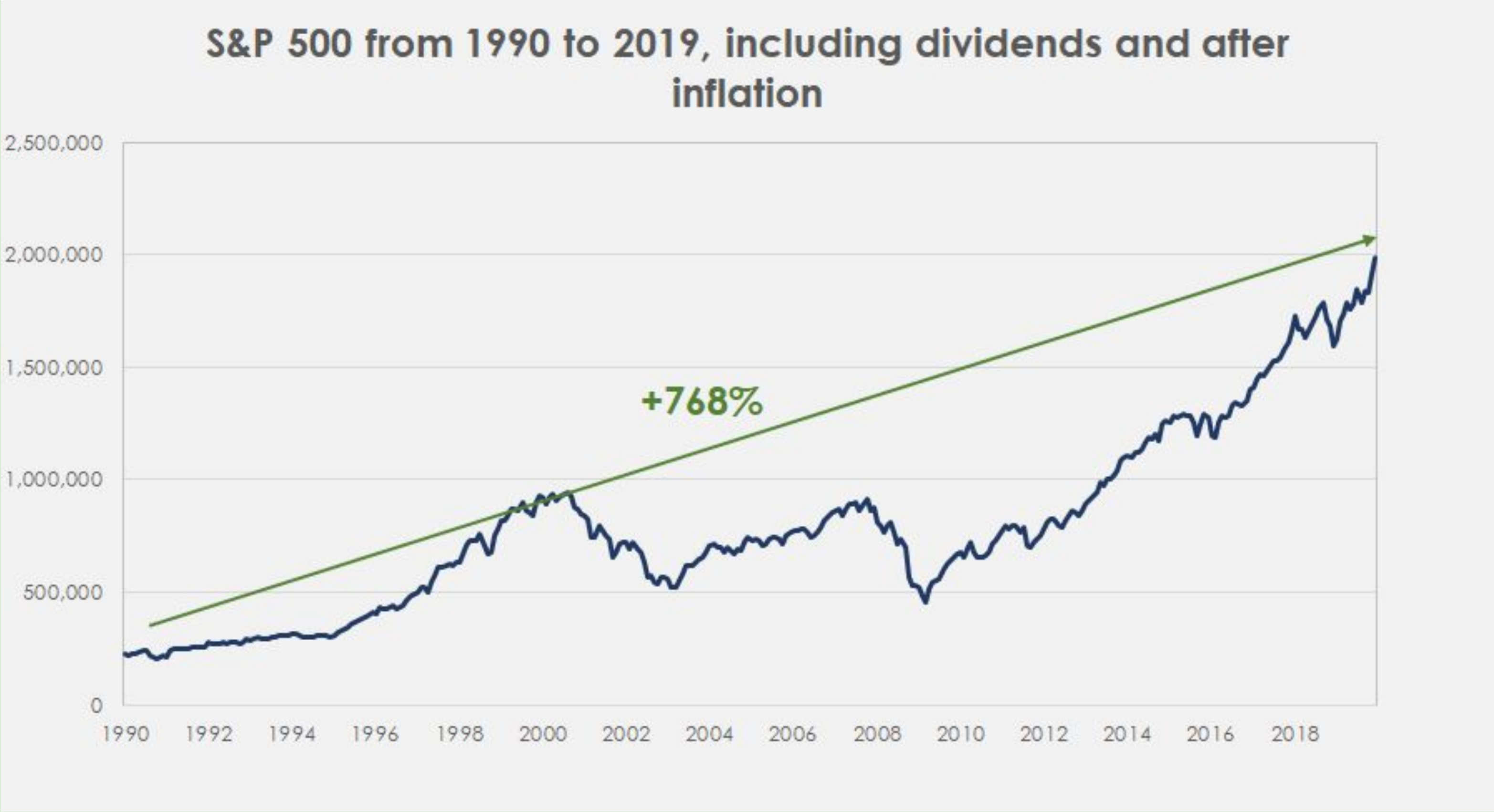
- In late 2019, COVID-19 emerged → Uncertain times!

- What will happen to US stocks in the next 5 years and next 30 years if these all happened in one year: (1) A spike in the price of oil; (2) the US goes to war in the Middle East; and (3) the US experiences a recession?

The fifth mindset



The fifth mindset

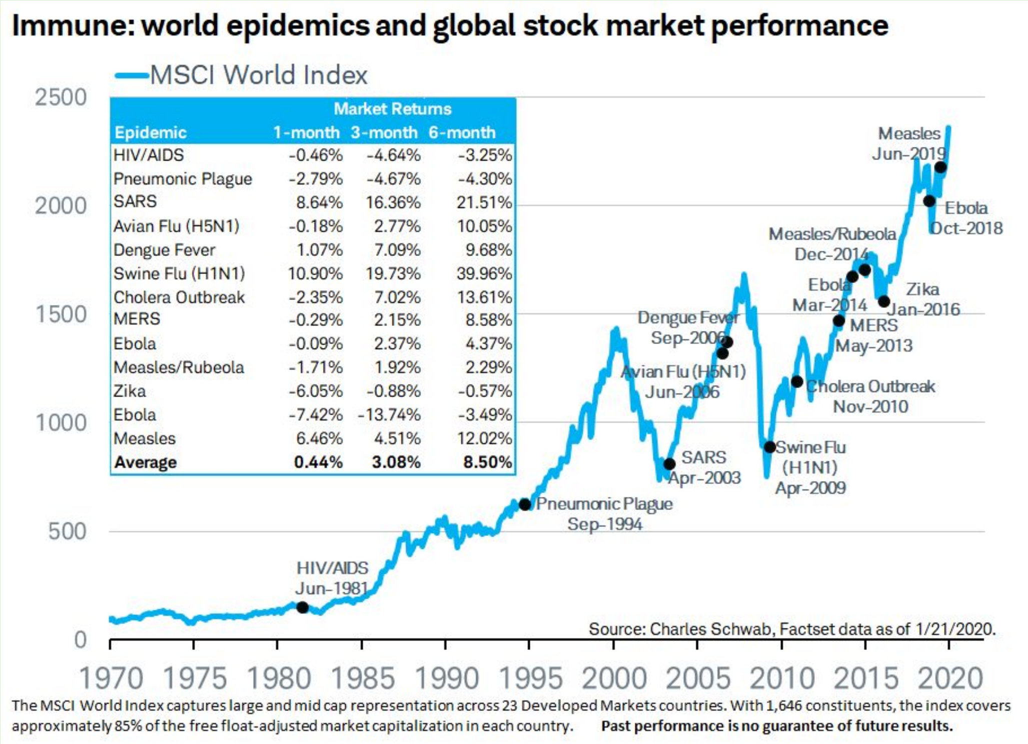


Year	Events	Year	Events	Year	Events	Year	Events
1990	Persian Gulf War; oil spike; US recession	1998	Russia defaults on debt; LTCM hedge fund meltdown; Clinton impeachment; Iraq bombing	2006	North Korea tests nuclear weapon; Mumbai train bombings; Israel-Lebanon conflict	2014	Oil prices collapse
1991	USSR breaks up; real estate down turn	1999	Y2K panic; NATO bombing of Yugoslavia	2007	Iraq war surge; beginning of financial crisis	2015	Euro currency crash against Swiss Franc; Greece defaults on loan to ECB
1992	Los Angeles riots; Hurricane Andrew	2000	Dot-com bubble pops; presidential election snafu; USS Cole bombed	2008	Oil spikes; Wall Street bailouts; Madoff scandal	2016	Brexit; Italy banking system crisis
1993	World Trade Centre bombing	2001	9/11 terrorist attacks; Afghanistan war; Enron bankrupt; Anthrax attacks	2009	Global economy nears collapse	2017	Bank of England hikes interest rates for first time in 10 years
1994	Rwandan genocide; Mexican peso crisis; Northridge quake strikes Los Angeles; Orange County defaults	2002	Post 9/11 fear; recession; WorldCom bankrupt; Bali bombings	2010	European debt crisis; BP oil spill; flash crash	2018	US-China trade war
1995	US government shuts down; Oklahoma City bombing; Kobe earthquake; Barings Bank collapse	2003	Iraq war; SARS panic	2011	Japan earthquake; Middle East uprising	2019	Australia bushfires; US president impeachment; COVID-19
1996	US government shuts down; Olympic park bombing	2004	Tsunami hits South Asia; Madrid train bombings	2012	Speculation of Greek exit from Euzorone; Hurricane Sandy		
1997	Asian financial crisis	2005	Hurricane Katrina; London terrorist attacks	2013	Cyprus bank bailouts; US government shuts down; Thai uprising		

Source: Morgan Housel (for 1990 to 2013)

The fifth mindset

Mindset No.5: Uncertainty is always around, but we should still invest



	Market Returns		
Epidemic	1-month	3-month	6-month
HIV/AIDS	-0.46%	-4.64%	-3.25%
Pneumonic Plague	-2.79%	-4.67%	-4.30%
SARS	8.64%	16.36%	21.51%
Avian Flu (H5N1)	-0.18%	2.77%	10.05%
Dengue Fever	1.07%	7.09%	9.68%
Swine Flu (H1N1)	10.90%	19.73%	39.96%
Cholera Outbreak	-2.35%	7.02%	13.61%
MERS	-0.29%	2.15%	8.58%
Ebola	-0.09%	2.37%	4.37%
Measles/Rubeola	-1.71%	1.92%	2.29%
Zika	-6.05%	-0.88%	-0.57%
Ebola	-7.42%	-13.74%	-3.49%
Measles	6.46%	4.51%	12.02%
Average	**0.44%**	**3.08%**	**8.50%**

Source: Marketwatch

The sixth mindset

- **Big** difference between *expecting* and *predicting*.

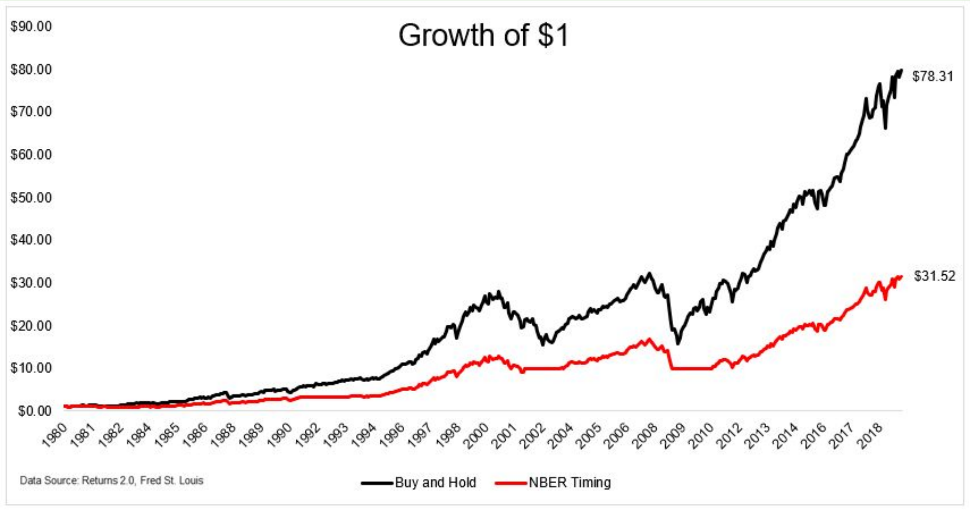
- **An expectation:** “If we invest for many years, things will get ugly a few times at least.” **A prediction**: “The US will have a recession in the third quarter of 2020.”

- If we have expectations only, we won’t be surprised with downturns. If we predict, we will be surprised.

The sixth mindset

- Timing the market based on recessions **don't** work.

- **Mindset No.6: Expect bad things to happen, but don't predict**



Source: *Michael Batnick*

All the mindsets together

- We need to be long-term investors to use the idea that a stock will typically do well if its underlying business does well too

- For us to be *comfortable* with long-term investing, we need the six mindsets

- **But we cannot invest for the long run blindly; investing in poor businesses for the long-term = poor results**

My investment framework

Can be found at thegoodinvestors.sg (under “Investing Knowledge Base”). There are six criteria:

1. Revenues that are small in relation to a large and/or growing market, or revenues that are large in a fast-growing market.
2. A strong balance sheet with minimal or reasonable levels of debt.
3. Management with integrity, capability, and an innovative mindset.
4. Revenue streams that are recurring in nature, either through contracts or customer-behaviour.
5. A proven ability to grow.
6. A high likelihood of generating a strong and growing stream of free cash flow in the future.

My investment framework

1. Revenues that are small in relation to a large or growing marketing or revenues that are large in a fast growing market

- A shrinking market = uphill battle for a company to grow

- Example of shrinking market: Print-advertising declined by 2.3% from 2011 to US$98.1 billion in 2018

My investment framework

2. A strong balance sheet with minimal or a reasonable amount of debt

- Invest for growth easily
- Withstand tough business environments such as recessions
- Increase market share when competitors struggle during downturns
- Makes companies antifragile

My investment framework

3. A management team with integrity, capability, and an innovative mindset

- Management without integrity fatten themselves at shareholders’ expense

- Without capability and innovation, a company can’t grow

My investment framework

3. A management team with integrity, capability, and an innovative mindset

- On integrity, look at how management is paid and the amount of related-party transactions

- 4 of Haidilao's top 5 suppliers are linked to management, but Haidilao's profit margin is healthy (at least 9% going back to 2016)

My investment framework

3. A management team with integrity, capability, and an innovative mindset

- On capability and innovation, we can look at a company's past actions to grow

- Example: MercadoLibre, largest e-commerce company in Latin America (LA). Online marketplace in late 1990s → online payments service in early 2000s → Shipping solution in 2013

My investment framework

4. Revenue streams that are recurring in nature, either through contracts or customer-behaviour

- Recurring revenue means a company need not spend resources to recapture a past sale; the company can focus resources on winning new growth opportunities

My investment framework

4. Revenue streams that are recurring in nature, either through contracts or customer-behaviour

Intuitive Surgical

My investment framework

5. Proven ability to grow

- Companies with proven track record have higher chance of being able to grow in the future

- Ideally, a good history of growth in revenue, profit, and free cash flow

My investment framework

6. A high likelihood of generating a strong and growing stream of free cash flow in the future

- The more free cash flow a company can generate, the more valuable it is

- I tend to avoid project-based companies because of lumpy free cash flow

  Eg: Sembcorp Marine

Building our portfolios

- Companies that excel in all or most of the six criteria above could be worthwhile investments

- But such companies can still be poor investments (many big losers in my family's portfolio), **so diversification is important**

- 30 to 50 stocks, diversified across different industries and geographies, is right for me, but the answer will be different for each individual

Protecting our portfolios

- Investment framework is not meant to protect my portfolio from short-term declines in stock price

- Protects my portfolio by leading me to companies with:

Strong cash flow | **Robust balance sheet** | **High recurring income** | **Solid management**



Finding investment opportunities during the COVID-19 crisis

- I’m sticking to my investment framework

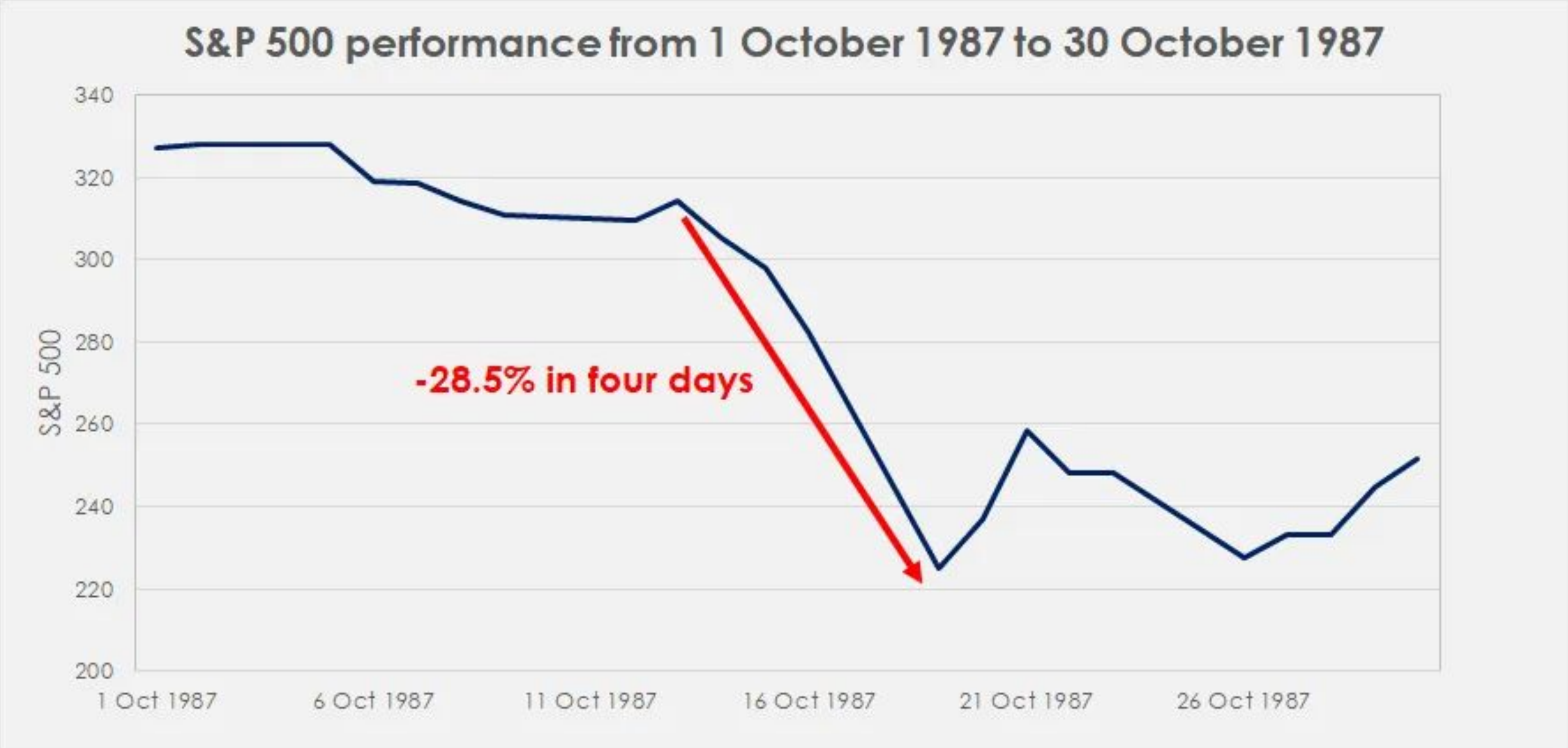
- COVID-19 does *not* change how the stock market works → Stocks will still do well over time if their businesses do well

- My investment framework is meant for finding companies that can potentially grow at high rates over a long period of time

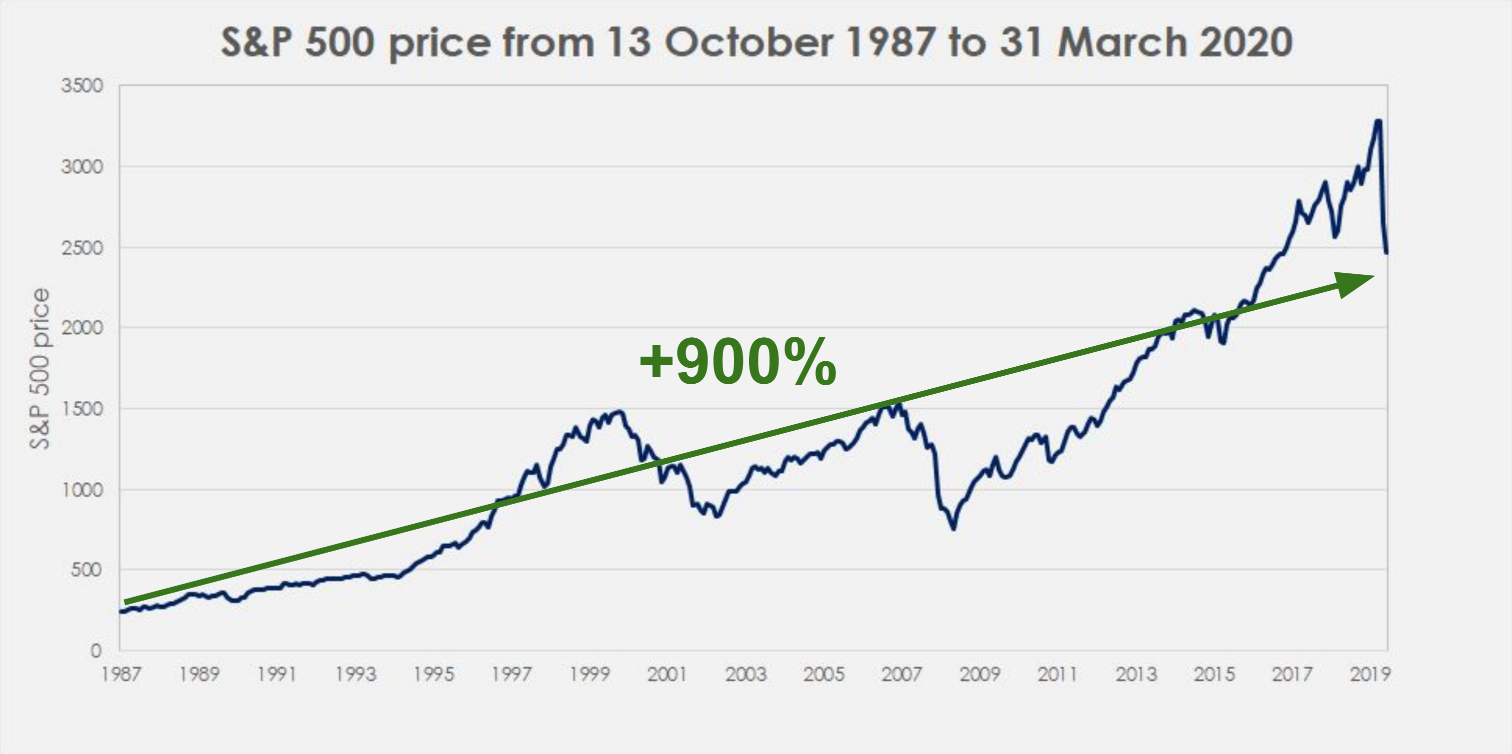
Finding investment opportunities during the COVID-19 crisis

- What about unprecedented volatility in financial markets during COVID-19?
- Markets have *always* been volatile
- Black Monday in 1987: US stocks fell by 20.5% in *one day* on 19 October 1987

Finding investment opportunities during the COVID-19 crisis



Finding investment opportunities during the COVID-19 crisis



Finding investment opportunities during the COVID-19 crisis

- Economic hardships in many countries are unavoidable, but they will pass

- 7.8 billion people in the world today; most will work hard to improve the world → This is the fuel for financial markets

- Miscreants and Mother Nature will occasionally wreak havoc, but humanity will prevail → Why I'm long-term optimistic on stocks

Thank you!

Q&A Time!

Blog: *The Good Investors*, thegoodinvestors.sg

Contact: thegoodinvestors@gmail.com