

**Lynch, Peter with Rothchild, John - One Up On Wall Street***Fireside, 1989, [Equity Investing] Grade ★★★★★*

Peter Lynch who managed the Magellan Fund at Fidelity from 1977 to 1990 was the shining star on the 1980's equity heaven. Lynch's yearly outperformance was 14 percentage points and he succeeded in beating the S&P 11 years in a row. In this book the author reveals his investment beliefs and the process he used. Lynch was always of the opinion that the amateur could be a better investor than the portfolio manager working at an institution and this easy to read classic is his guide to how to pull this off.

The book is divided into three sections. In the first Lynch tries to depict the features of the equity market with long market cycles and corresponding waves of optimism and pessimism. He further covers the impossibility of making top down macro calls and the institutional handicap for the pro investor due to restrictive rules, need for clearance from committees and short term performance pressures. The market view also has to be complemented with a self-assessment by the investor on whether he is suited for the stock market. The second part deals with the basics of stock picking: how to find stocks, how to evaluate and how to monitor them. Lynch had a very labour intensive process and met with about 600 companies per year. The mantra was that you had to visit 10 companies to get one good investment idea. He had a preference for ideas generated in his immediate surroundings such as the hot new crowded retail outlet in the nearby mall and he also advised amateur investors to invest in companies in the sector where they worked. Invest in what you know and understand. Many have heard about Lynch search for tenbaggers, stocks that increase tenfold, but I think that one underestimated aspect of his process is the sectioning of stocks he does into six categories. This gives Lynch customized strategies for different types of stocks – the opposite of one size fits all. The categories were: 1) Slow Growers, 2) Stalwarts, 3) Fast Growers, 4) Cyclical, 5) Turnarounds and 6) Asset Plays.

Lynch himself, on average, had roughly 35 percent each in Fast Growers and Turnarounds and 15 percent each in Cyclical and Stalwarts.

Favourites were profitable, understandable companies with stable demand. Lynch often searched for the best companies in mundane sectors and he happily invested in small caps as long as they had profits. He rejected companies with extravagant offices as he thought that priorities here were on the wrong things and he avoided all companies in a bad financial state. Even if a company fulfilled the desired criteria the price of the stock also had to be appealing. Lynch generally looked to the p/e-ratio and had a rule that you shouldn't buy a stock with a p/e-ratio higher than the EPS growth rate the next two to three years. For each investment Lynch prepared a written investment case and he was of the opinion that an investor should be able to hold a two minute monologue on each of his holdings. After investing, Lynch redid the analysis every few months to see if the investment case was still valid. The third part of the book contains a mixed bag of portfolio design, advice on when to buy and sell plus general advice/opinions on derivatives, short selling, leverage etc.

I very much appreciate Lynch's scepticism towards forecasts. He preferred to analyse the opportunities for change and the changes that was already on the way. I also predominantly share his view that investors should focus on bottom-up analysis. However, I'm not as dogmatic as Lynch. I think the quote "That's not to say there's no such thing as an overvalued market, but there's no point worrying about it" reflects the times Lynch worked in. In my opinion it's possible to adjust investment processes according to the present market environment.

This is a classic must on every bottom-up equity investor's book shelf. Simply buy it.

Mats Larsson, March 11, 2012