# Selling and Selling Short

Thank you to Swedbank and Kepler Cheuvreux Swedbank for releasing the material

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Mats Larsson, November 4, 2018

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- Ways to Handle the Difficulty
- A Sell-or-Hold Strategy


## Introduction

*"Almost all of the really big trouble that you're going to experience in the next year is in your portfolio right now; if you could reduce some of those really big problems, you would come out as a winner […]."* /Charles Ellis

When it comes to investing in portfolios of individual stocks, it doesn't matter if your benchmark is an index or an absolute return number; there are still two basic ways to beat that target. Either you succeed in holding winning stocks in sufficient numbers or you have fewer bad positions. Find the stars or avoid the dogs. If the largest mistakes can be avoided the portfolio is almost destined to outperform.

In any given year there are generally fewer stocks outperforming a long-only index than underperforming it – the median stock is an underperformer. Hence, having a clear, well-thought-out and actionable strategy for how and when to sell stocks in the portfolio seems like a pretty important thing.

Important but few gives it a thought

Still, in a survey made by Cabot Research in collaboration with the CFO Institute a few years ago, less than 15% of the respondents said they had a rigorous and calibrated method for identifying sell candidates in their portfolio. Investors who in great detail can discuss how they identify the stocks to buy usually describe their selling discipline in a few sentences. The problem is that selling is hard and emotional. The risk is that without a previously defined method to sell shares our passionate but not so rational psyche will take the decisions for us when we are under stress.

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Picture 7.1. Which are Next Year's Lemons in Your Portfolio?

*Source: businessinsider.com*

Winning by not losing

Start with shorting

In this text we will cover two intertwined topics in investing; selling and selling short. However, we will actually reverse the order and start with the area of shorting since this practice also gives valuable insights into what potentially should be sold on the long side.

Apart from drawing on own experiences the text has been inspired by the works and thoughts of amongst others James Chanos, Lee Freeman-Shor, John Heins / Whitney Tilson, Kathryn Stanley, Amit Kumar, Scott Fearon and, as almost always, Michael Mauboussin.

Selling when
- Proven right
- Proven wrong or
- Better alternatives

The standard description of when long-only investors choose to sell are 1) when their thesis for the stock has been realized, 2) when the fundamentals of the case change significantly or 3) when they can identify better uses of the capital. In other words they sell when they have been proven right, when subsequent developments have proven them wrong and/or when other investments look more interesting. Still, these tenants in themselves don't make a structured process obvious.

Not one size fits all

For example, since not all investors are alike they probably wouldn't use exactly the same criteria. The definition of being wrong varies between different investor types. For a momentum investor the investment case often builds on the share price trend, so when the trend is broken he is wrong and he therefore generally uses a stop-loss. A fundamental investor is instead wrong when his reasoning around the corporate fundamentals that he builds his investment case on are proven wrong and he therefore must redo the analysis to decide how to act.

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Investors and their investment methods could be divided and categorized in a myriad of ways but we have chosen to narrow them down to two trios.

- Time horizon and type of position: short-term contrarian (1-6 weeks), medium-term trend following (6-18 months) and long-term contrarian (3-7 years)
- Research tools used to gain an edge: technical, quantitative and fundamental

Categories
- Time horizon
- Research tools
- Fate of position

+ type of stock

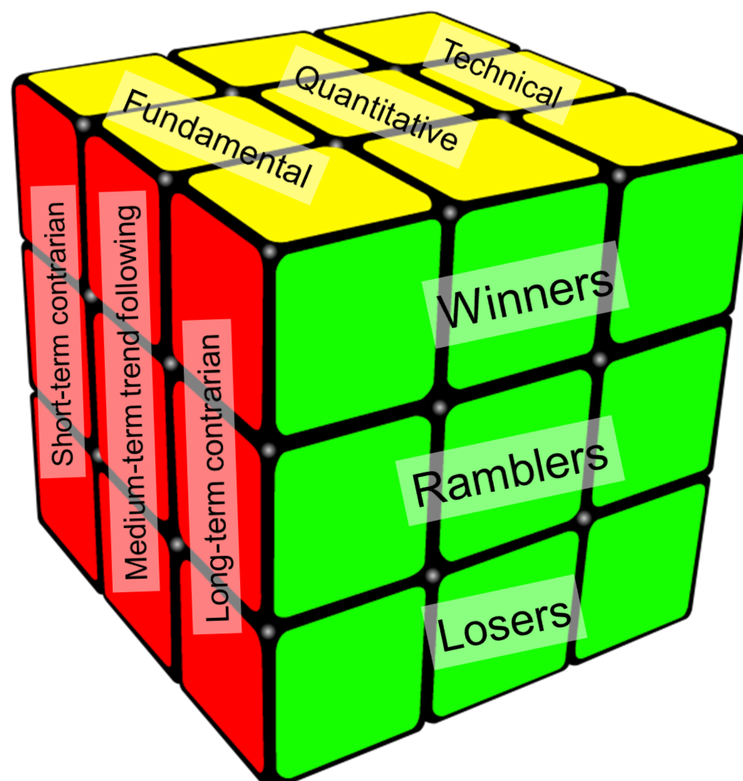
With different methods in building a portfolio, naturally the way selling is done will vary. Further, how selling is done, as we have seen above, also differ depending on the success of the position. Another angle to factor in is then:

- The selling of winning positions, of positions going nowhere and of losing positions

An additional important aspect to factor in is the character of the stock but we will leave this angle for later. Even with our narrowed down choices there are numerous scenarios that we have tried to illustrate with a Rubik's cube below. We have called the stocks going nowhere "ramblers".

27 combinations…!

**Picture 7.2. Selling Comes In Many Varieties**




*Source: learnhowtosolvearubikscube.com, the author*

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The easiest one to describe out of these groups with regards to selling is actually the quantitative investor. Irrespective of other aspects he will do a periodic rebalancing of the portfolio where he essentially starts with a blank sheet and buys a brand new portfolio of a fixed number of stocks that meets his investment criteria. Naturally, a stock that was included before and is to be included again isn't sold and bought back. In this case it's just a matter of rebalancing the position size. Thus, selling for a quant is simply a matter of removing those stocks that don't make the roaster in a new screening to make place for new stocks.

Quant selling is easy

This impassionate rules-based portfolio handling is noteworthy as it takes much of the stress and psychology out of the otherwise tough selling decisions. In many ways this use of a fixed number of positions (which we quite like) also resembles Peter Lynch's "pig-by-a-trough rule", i.e. the requirement that a new position must be good enough to force out another position to be worth contemplating. A rule he however didn't always live up to himself.

It is obviously important to understand the many varieties of investors and investment styles and what this means for their selling. We have touched on the stop-losses of momentum investors and the rules-based selling of quantitative investors but in the text that follows we have chosen to focus on the longer-term fundamental investor both when it comes to long-only investing and when it comes to shorting.

Focus on long-term fundamental

Short selling strategies and short cases for individual stocks can also be divided into a number of varieties including:

Short Selling Categories

- Tactical
- Paired
- Structural
- Cyclical

- Tactical shorts based on technical or quantitative indicators with a 1 week to 1 quarter outlook, b) paired shorts where the investor pair long-positions and short-positions of similar types of companies, c) structural shorts with a 1 to 2 year investment horizon, d) cyclical shorts based on the top-down view of a sector or the stock market

Again, we will generally focus on the structural shorts. Notice how the long-term investing of short selling uses an investment horizon that is shorter than the long-only long-term investing. This is partly due to a difference in risk level but also to the fact that stocks decline much faster than they rise. Also, borrowing shares incurs borrowing fees as long as the trade is on. Thus, short sellers have to recoup this investment hurdle and the fact that they "pay to wait" makes timing more critical.

Focusing on structural shorting

Okay, let's kick off.

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## Selling Short

*"Look for debt financed asset bubbles, technological obsolesce, accounting irregularities and consumer fads."* / James Chanos

Accounting warning flags in separate text

The section of short selling should be read in conjunction with *Those Other Pages* covering accounting warning flags in *The Companion 2015:4* from November 30, 2015. Detecting suspicious accounting is an important part of short selling but we will not describe it further here.

Profiting from declines

A short seller earns money when stocks go down. On average stocks go up over time but they occasionally have drawdowns that are much faster and more violent than the steady upward trend. An investor with the opportunity to short can as such benefit from all types of movements.

Having the ability to short stocks gives an investor the opportunity to be offensive when the markets are at their weakest. Psychologically it gives the investor a piece of mind to stay rational and to be able to make money when everybody else is panicking. An investor who includes shorting in his toolbox doesn't have to rely on prices going up to earn money, he "only" has to get the direction of price movements right.

Jim the king…

Never the same, the fact that pure short sellers without a long side are swimming against the tide makes generating positive absolute returns over time a tough task. James "Jim" Chanos who is the undisputed king of shorting, the short sellers' Warren Buffett, has in over 4 decades generated an annual return of about 3.5%. Considering that he is working against the stock market and starts each year on an average of about -8.5% this is quite an achievement.

**Picture 7.3. The King of Short Selling – James Chanos**

…shorted Enron

*Source: hurricanecapital.wordpress.com*

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It is a mistake to think that short sellers only short stocks indiscriminately into a falling market. Most shorting is done in rising equity markets simply because they go up most of the time. Also, the normal process among short sellers is to look to individual companies when searching for opportunities – they are bottom-up investors.

As is the case with activist investors people hold, often weakly supported negative views of short sellers as persons. We agree that many might be a bit special - but mostly in a positive way. Thus, we wanted to present a very subjective, short and possibly stereotype personality profile of how we view short sellers.

Short sellers are hard workers who enjoy going against the mainstream opinion. They are driven by curiosity and the pleasure of detecting the truth. They are often also driven by a sense of justice that gives them energy to dig into situations where the corporate insiders treat the company's, and by this the shareholders', money as a personal bank – often without owning many shares of their own.

Psychological Profile

- Hard working
- Contrarian
- Curious
- Truth seeking
- Ambitious
- Single-minded
- Anti-social
- Cynical
- Moralist
- Frugal
- Pain resilient
- Pigheaded
- Smartass

They are ambitious, driven, single-minded and sometimes anti-social persons who like to win against the odds. They get a kick out of being smarter and more independent than the ordinary investor. Often they have a cynical bent and quite enjoy a stock blowing up in the face of the easily fooled crowd.

In this one might say that there is a moralist aspect as well since short sellers enjoy exposing that the emperor is strutting around the stock market without clothes. This means that short sellers rarely are the most flamboyant spenders on luxury goods themselves.

Jim Chanos of Kynikos Associates, whose short sale of Enron has been called the market call of the decade, has claimed that a successful short seller must have the psychological constitution to withstand pain and keep a position in the face of the steady flow of news media and sell-side research (what he calls the muzak of the investment industry) that tells him that he is wrong. The short seller must withstand long periods of negative reinforcement.

One common problem with this profile is pride and pigheadedness. Short sellers like to know better, to be smarter. This unfortunately can make them stubbornly resistant to admitting that they invested in the wrong position.

In taking group decisions it is often pointed out that diversity and especially diverse viewpoints of an issue leads to better conclusions. We view short sellers as important to the pricing formation of the equity markets precisely as they bring another point of view to the party.

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**Learning From History**

New on the job…

Let me share a personal anecdote on shorting. About a decade ago I ran a European TMT-portfolio. My then new employer graciously gave its portfolio managers a great degree of freedom on how to structure their portfolios and instead steered us on targets for information ratios.

…managing a 140/40 portfolio

I chose to structure my portfolio as a so-called 130/30 portfolio (i.e. 130% long and 30% short), although the position sizes rather made it a 140/40 portfolio. The leveraged long 40% part selected positions from a screen combining high ROIC, strong share price momentum and low EV/EBIT. The short 40% part selected positions from a screen combining low ROIC, weak share price momentum, high EV/EBIT and high NetDebt/EBITDA. I then met with analysts and companies plus researched further material to make the final choice of a fixed number of decently concentrated positions. Hence, you could say it was a "quantamental" type of stock selection.

The 100% long base of the portfolio was indexed. I rebalanced the portfolio with a fixed regularity that I can't really remember right now (quarterly?). Why this setup? It was specifically tailored to the sectors under management, since TMT and especially Technology stocks respond well to "quality-momentum" strategies and I had also picked up on the fact that leverage was a more important factor on the short side than on the long side.

It started out well…

With a 140/40 setup a PM view on stocks gets amplified and especially so when it comes to the stocks on which he has a negative view. It's basically a hedge fund stacked on top of a long-only portfolio. If you are negative on a stock with a 0.2% weight in the index, the long-only manager cannot do more than to not own it and if he is right and the share price in an extreme case goes to 0 he has earned… well, 0.2% compared to the index. If he instead can take a -5% position by shorting the stock the correct stock call pays off in a totally different way. Since I thought myself a good PM I naturally wanted to amplify my view.

And it worked like a charm! I stepped in from one employer to another and if my selective memory serves me right I immediately became the best performing portfolio manager the first year (there could have been someone else with similar returns as well but in that case I have repressed this). Then the GFC came, the global financial crisis that is, and things changed.

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**Picture 7.4. It Worked Like a Charm**

*Source: linkedin.com*

…thanks to my brilliance…

My overlay 40/40 portfolio had the same number of longs and shorts and the long exposure was of equal size as the short exposure in terms of market capitalization. Since the volatility of short positons are much larger than of long positions this means that the portfolio was not market neutral in terms of volatility. I knew this from start and it didn't disturb me much but with the GFC the volatility of all positions, and especially the short ones, now climbed to a different level.

…but then costs skyrocketed…

Although this hurt my information ratio (and by this my potential bonus) and I still today feel bad about not having set up a procedure for scaling my portfolio positions to handle different risk environments it probably in the end didn't cost me any actual money. Something else did. The cost of lending stocks shot through the roof and this literally ate up the profitability of my otherwise, despite the rough times, fairly decent stock selections.

…which cannot be blamed on me?!

I was too shell-shocked by the environment to gather the mental strength and flexibility to change the setup and due to this, in the bad times I gave away the alpha that I had earned in the good times. To be frank, pride due to the strong start of the portfolio might have had something to do with the lack of flexibility as well. I mean, hadn't that flying start proved that the setup was brilliant and that I was a genius? How could I back away from that?

After the GFC had bottomed out the majority of the equity PMs were sacked and we who remained got orders to refrain from any type of "financial engineering", not that it had lost us any money but back to basics was the sign of the times. After some reshufflings I ended up as one of three global long-only equity managers and that, for then, ended my efforts shorting stocks.

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Humbling Lessons

- Robust portfolio construction
- Factor in liquidity
- High demand + low supply = high prices
- Financial engineering builds fair weather strategies

What lessons can be learnt? First, portfolio construction really matters and it's hard to be flexible when things turn sour so it is better to think ahead planning for various scenarios. Secondly, in considering short positions one cannot only look at corporate performance and valuation but factors like companies' market capitalization, stock liquidity and free float must at least be factored in. Thirdly, given the higher volatility of short positions it might be a good idea to diversify the short side more than the long side.

Also, the lesson is that there are few free lunches out there; when the market tanks and shorting should be like shooting fish in a barrel, asset managers curl up in fetal positon and stop doing exotic things like lending shares. Plus, when the market heads south a lot of people want to short. Hence, the supply for lending stock goes down and the demand goes up with the predictable result that the cost to borrow and short goes up.

Perhaps the general lesson is that all financial engineering works smoothly in markets with ample liquidity but not so much in those where people are scared and counterparty risk reveals its ugly head.

**Practicalities of Shorting**

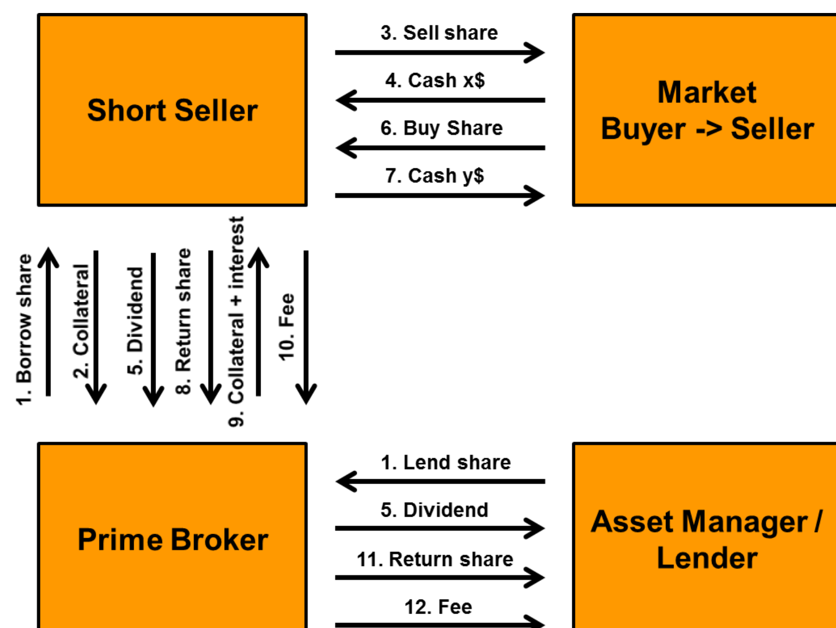
*"I have seen more stocks go to zero than infinity."* / Jim Chanos

Just like in traditional investing short selling tries to buy low and sell high to make a profit. It's just that the order of the transactions is reversed as the short seller first sells and then buys later. To be able to do this the short seller must borrow the shares to sell (or else it is called naked short selling which is mostly forbidden in equity markets).

Shorter Scheme

1. Borrow
2. Sell
3. Buy back
4. Return

Picture 7.5. The Process of Short Selling




*Source: The author*

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Borrow & collateral

Say that you expect a stock you don't own to go down in price. You can then contact your brokerage house and they will handle a short selling transaction. Investment banks have entered into deals with large asset managers which give them the right to lend some of the asset manager's shares to short sellers. Importantly, to protect the asset manager from losses the short seller will have to set aside a cash sum as collateral with the broker on a special account.

Sell & buy

The short seller can then sell these borrowed stocks to a third party and receive money in return. Now, if the price of the shares goes down as originally expected the short seller will later on be able to buy back an equivalent number of shares in the market at a lower price. Hence, some of the money received from the initial sale of shares will be left as profit. Score!

Return & fee

Since, all shares of the same class are the equivalent to each other these acquired ones are returned to the lending asset manager together with a fee taken out as a payment for being able to borrow the shares. The collateral is now released, minus a modest fee to the broker for arranging the transaction but plus any potential interest earned on the sum of money during the period.

Pass on the dividend

Legally, the ownership of the shares shifts from the asset manager to the short seller during the transaction. The asset manager instead gets a claim on the short seller.

If the shares happen to distribute dividends while the shares are lent the short seller must pay the asset manager a sum equivalent to this out of his own pocket – on the other hand the share price will probably decline by roughly the same amount giving a counterbalancing profit.

At any time the asset manager can terminate the lending transaction and call back the shares. This can for example be because they will be needed for attending and voting at an approaching annual general meeting.

Up = loss

Naturally, if the share price goes up instead of down, eventually the short seller will have to repurchase the shares at a higher price than he sold them for and the short seller will have made a loss. The broker will then use the collateral and fill up the number of shares to be able to return the same number of them to the original owner. The (hopefully) remaining collateral is released to the short seller.

More collateral or cover

Thus, the risk is then that the price moves up after the stock has been sold short, causing losses and even requiring more cash infusions on the broker account. If losses spiral out of control the position could in worst case have to be liquidated by necessity – probably only to create the peak prior to the downturn. We don't know the origin of the following quote but find it quite telling: "Shorting's easy. You short a

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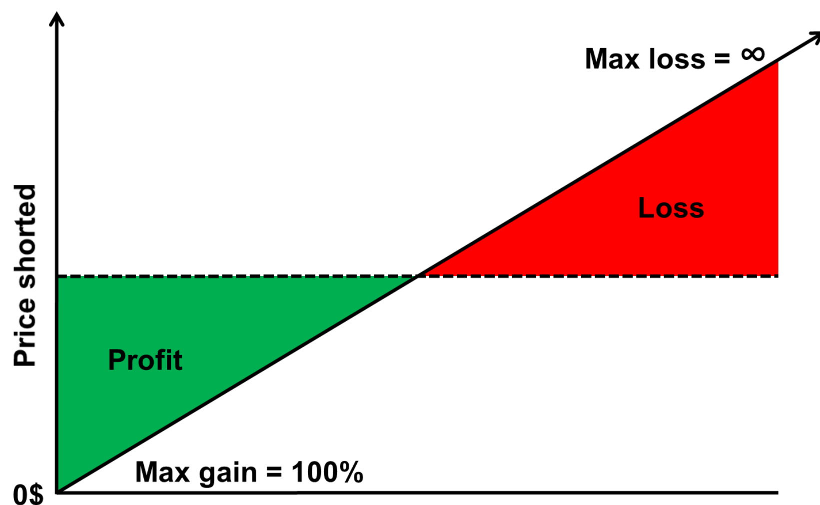
stock, watch it double, cover in panic, then wait for the inevitable bankruptcy."

Unlimited damages

Theoretically, as stocks cannot go below zero in price, profits for a short seller are limited to 100%, while the loss is unlimited since there is no equivalent ceiling on how high a share price can move up. In real life few short sellers work without some kind of risk management strategy often including some sort of stop-losses so, although extremely painful, losses are seldom unlimited (but don't tell those who were shorting VW in October 2008 we said that).

Risk management vital

Picture 7.6. The Risk-Reward Asymmetry of Shorting




*Source: The author*

In some cases the problem that the downside is unlimited when selling short can be handled through using derivatives. Instead of selling a stock short an investor could by a CDS and risk less capital. Derivatives such as a CDS are however not always available for all companies and they come with counterparty risks that could blow up in a credit contraction.

Mounting problems

There is another related asymmetry in shorting stocks. If a position goes wrong on the long-side it, and the problem it causes, becomes smaller as the share price declines and the portfolio position with it. A short position going astray instead becomes larger as the share price goes up. Hence, the potential future problem is increased. Hence, short portfolios are diversified to limit the risks and in quantitative long-short portfolios it is common to have a more diversified (or smaller) short portfolio than the long portfolio to better balance the volatility of the two sides.

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Due to the higher risk level short sellers seldom make a killing (or lose their shirt) on a case since they cannot bet the farm on one isolated situation. The position sizing is still a function of the portfolio manager's character. Trade size is a huge emotional amplifier and an investor should only take positions he is mentally comfortable with. Some hold relatively large positions for years while others set up rules limiting position sizes according to risk/reward metrics. The above-mentioned Jim Chanos tries to have about 50 positions where about 10 of these account for max half the weights of the portfolio.

Diversification

Some formalize the position sizing's role in their risk management into various types of rules. The 2% rule is one example. The distance from entry price to the stop level defines the risk to the portfolio and max 2% of the portfolio value can be risked by one position. For example, if you have USD 100,000 in the portfolio then USD 2,000 is the max risk allowed from one position. If the entry price for the short position is USD10.98 and the stop level is USD 12.48, then the risk per share is USD 1.5 and the maximum number of allowed shorted shares in the position are 2,000/1.5= 1,333. That is, keep the position to around 1,300 shares or less.

2% max loss

Famed activist investor Bill Ackman of Pershing Square calculates what he calls a "ceiling on valuation", i.e. a bull case valuation for the stock which then is the worst-case for someone who's short. This allows him to get a feeling for the risk in potential positions. For some companies like a fast growing Internet company it is very hard to establish this ceiling so they don't qualify as a good short case. In profiting from short selling Pershing Square looks for companies that can go to zero and disappear or companies that they think are breaking the law and thus risk closure by regulators.

Worst case bull valuation

When the equity of a company is wiped out short sellers don't have to cover their positions. They make a 100% return. If the risk/reward of the ceiling vs. the probability of going to zero is attractive Ackman's firm can consider the stock as a short.

**The Short Seller's Checklist**

*"'How did you go bankrupt?' Bill asked. 'Two ways' Mike said. 'Gradually and then suddenly.'"* / Ernest Hemingway, The Sun Also Rises

The question of whether a stock should be shorted and the subsequent position sizing is down to the investor's conviction about the risk/reward of the case. For the non-quantitative investor shorting stocks isn't the opposite of buying stocks since the character of the positions are different. Therefore, finding short selling candidates requires a separate process than just choosing those that rank the lowest among the long candidates.

Finding shorting candidates by…

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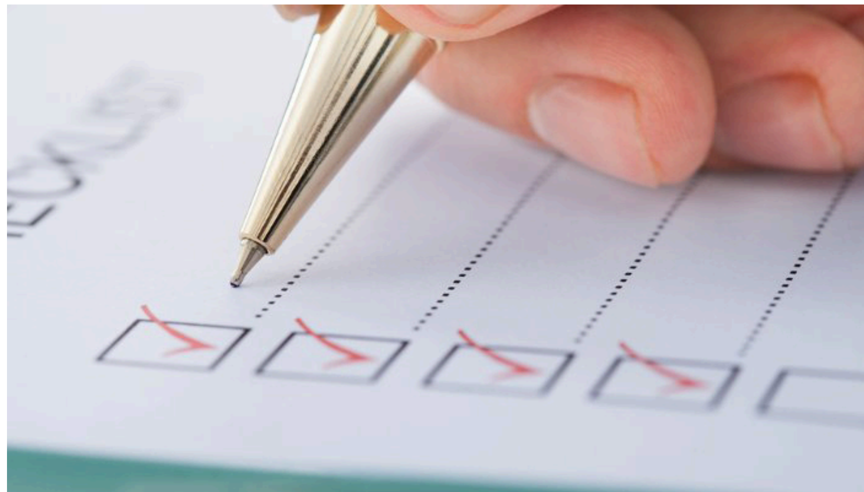
…ticking boxes..

Below we suggest a checklist logging a number of characteristics of a good short case. The more of the boxes that can be ticked the higher conviction. Still, fundamental shorting cannot be done mechanically as not all companies that tick the short seller's boxes are good short cases and the actual position taking will always require a leap of faith hopefully based on previous experience.

…plus some judgement

**Picture 7.7. Checking All the Boxes**



*Source: meadescontractors.co.uk*

Hard work attracts few

Because the risk is higher than on the long side and short sellers are swimming against the tide since the stock market goes up over time, they must have a confidently researched investment case to backup the position - and the potential of the case must be sufficiently large to motivate the hazard. This is oddly one of the attractions of the fundamental shorting area. It often entails too much manual work to attract significant competition.

The nature of successful short selling is searching for non-consensus information that is not priced and not well distributed by sell-side research. As such the research often takes more time and work than the research performed on the long side. Nevertheless, the optimistic case of a company is more often already priced in and in a way it might be simpler to spot companies with looming troubles ahead since the signs will be there for those looking, even if the investment public is still optimistic. Short sellers try to look for the first tremors of an approaching earthquake.

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Since the corporate management generally will be of less help and sell-side research generally focuses more on the positive case, the short seller focuses more on the financial disclosures from companies and ideally work their way through several years of annual and quarterly reports. This not only gives insights into the accounting but also into the management's attitudes towards their shareholders and if the story the management tries to spin changes as they have to abandon previous goals and strategies. Many short sellers don't even try to meet with management.

Management not helping

When short selling cases are discussed in general there is often a focus on insider selling and accounting issues such as companies with rising inventories or a strong appetite for using up cash. Typically, when presenting how to screen for shorts James Montier, currently of GMO, advised to look for "a growing difference between net income and cash flow from operations, increasing DSO, growing DSI, growing other current assets to revenues, declining depreciation relative to gross property, plant and equipment and a total asset growth greater than 10 percent. And then add to that a P/S higher than 2x."

Accounting warning flags not enough…

We don't want to downplay the accounting issue (and have written a full primer on accounting warning flags in in *The Companion 2015:4* from November 30, 2015) but we find that the key to shorting is instead the business operations of companies. Successful structural short positions are often found among companies with some type of operational troubles such as a faltering business model, a changing competitive landscape or other adverse changes in the industry.

…without operational troubles

High valuations, high leverage, accounting warning flags and other factors are complements that add to the opportunity. Accounting based indicators like DSO and DSI can alert the short seller to something to investigate but without a clear view of a stumbling business case the conviction will be small.

The rest is complementary

Thus, accounting warning flags are not a reason to short per se. Often they are signs of business problems that the management is trying to cover up. It is only by understanding these underlying issues that it is possible to decide if the stock is a good short. If there are no underlying business issues, new management can simply come in and correct the accounting.

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**Picture 7.8. The Short Seller's Checklist**

1. **Liquidity**
2. **A Bad Business**
3. **A Weakening Business Situation**
4. **High Leverage**
5. **High Valuation**
6. **Insider Selling**
7. **Accounting Warning Flags**
8. **A Trigger**

# 2 and # 3 are the foundations

*Source: The author*

Above we state what we think is a relevant checklist for short selling opportunities. Apart from the accounting warning flags we will briefly cover them one by one.

Liquidity

Sufficient liquidity is more of a pre-requisite than something that is actively searched for in a short selling case. Even for a good short idea it will not be practical or advisable to peruse it if it's not possible to borrow shares, if the borrowing is too expensive or if the risk of a short squeeze is to high. In some cases derivatives might be an alternative but they can also be similarly crowded and expensive.

If it can't be done, don't do it

A constant risk in short selling is that the lender asks for the stocks to be returned. If the prime broker cannot find other stocks to loan, the short seller will have to buy back the shares in the market and wind up the position irrespective of whether the timing suits him or not. For this reason alone it is advisable for short sellers to stay away from small cap stocks with poor liquidity.

A short squeeze will force a stop-loss and lock in losses

Another reason is the risk of a short squeeze. Wikipedia defines a short squeeze as *"a rapid increase in the price of a stock that occurs when there is a lack of supply and an excess of demand for the stock. Short squeezes result when short sellers cover their positions on a stock, resulting in buying volume that drives the stock price up."* Naturally the risk of a short squeeze is higher if the supply of stocks to trade is limited and the demand is large. This is the situation when the free float is small to start with but the short interest on top of this is high due to a crowding of shorting.

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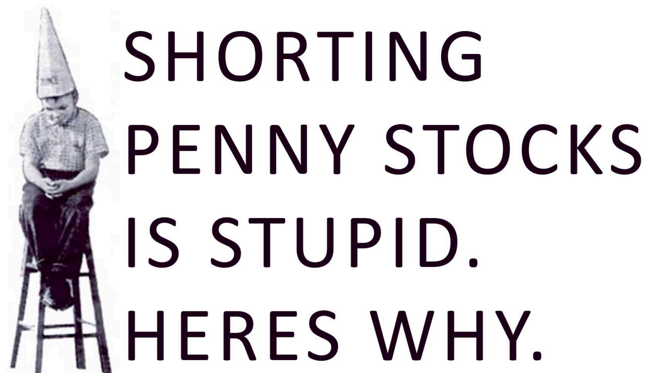
Short interest and DTC

The short interest compares the number of stocks shorted with the number of stocks in the free float. A short interest of up to 10% might be tolerable, while a number approaching 20% raises serious concerns. Days-to-cover (DTC) compares the number of shorted stocks with the daily trading volume. As such it shows how many days it would take for short sellers to cover their positions if they needed to get out. If the days-to-cover are 1 to 5 it will be easy and cheap to get out, if it is above 10 or 15 the risk of a short squeeze is high and the position could potentially lose a lot of short sellers massive amounts of money. Look to the two ratios in combination to estimate the crowding risk.

Blame no one but yourself

Short squeezes happen in relation to positive news and can be very violent in a narrowly traded stock. Ultimately, being caught in a short squeeze could many times, to some extent, be considered a calculated risk or a self-inflicted injury since the size of the short interest and the days-to-cover always must be considered when taking and keeping a short position.

**Picture 7.9. Short Selling Humor**




*Source: claytrader.com*

There are a number of short sellers that monitor which companies see rising short interest when they search for investment ideas. Since short sellers too often enter their positions too early, playing follow-the-leader can indeed be a profitable strategy. Still, it is important not to lay idle and pass on doing the necessary research homework or else the conviction will not be there when the position (temporarily) backfires.

Better search for less crowded positions

Also, well-publicized shorts are often exactly those that get crowded with plenty of investors shorting and covering in large volumes, resulting in increased borrowing costs and high share price volatility. Following the lead of other short sellers is too often just a lazy solution indicating a lack of ideas. Some of the opportunity will potentially be gone and the risk is definitely higher. As in all investing, to outcompete the competition you must do something different than the crowd.

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A Bad Business

More losers than frauds

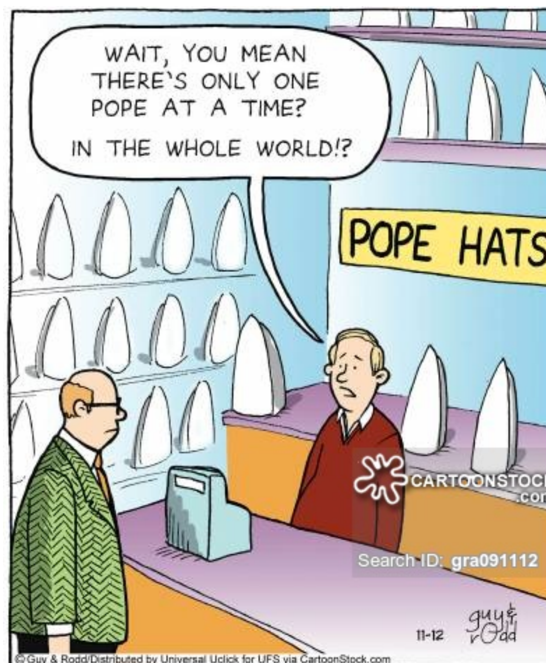
People tend to focus on the success stories but in business things go wrong more often than they go right. A fair number of stocks go bankrupt and zero-out their share price every now and then. Most of these are not frauds but plain business failures due to bad business ideas in a bad sector executed by bad management. Finding pure accounting frauds is a very complicated task and the success rate is probably higher when simply searching for bad businesses.

Will they create shareholder value…

Defining poor businesses is largely turning the search for successful, high quality companies on its head (see *The Companion 2015:1* from August 28, 2015 for a comprehensive checklist). Does the business model make sense? Is there sufficient demand for the products? If a company generates most of its revenue from one product or one client it is naturally more prone to fail. Can the expansion be funded? Is it a sector where companies earn good money? Or is it a sector where shorter product life cycles and swift changes in consumer trends make sustained business success hard?

…or not?

Picture 7.10. Misunderstanding Demand




*Source: cartoonstock.com*

The good company mistake

One of the most prevalent mistakes of short sellers is to focus on valuation first and short good companies. High quality, high ROE-companies with quality management as a general rule make very bad short cases even if the stock might be expensive. These companies can fund their expansion from internally generated means, sustain their operations indefinitely and by this grow into the high valuation. With capable managers temporary problems are also quickly solved.

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Avoid open ended growth

Also, avoid companies with a good growth track record and a long open ended runway of growth - irrespective of the stocks valuation. Even if this isn't necessarily a high quality company the open-endedness of the growth risks causing exactly those unlimited losses that is the bane of the short seller. Size up the potential market size and the competitive situation to determine the growth potential but don't act without a trigger. It could take years before the situation changes.

Apart from being present in a lousy sector and having developed a bad business model it is the failings and mistakes of poor executive managers that cause companies to flop. People in executive management are often wrong about their company's future since they almost always err on the side of over-optimism.

When trouble instead builds up some management teams go into denial. Failure terrifies people and some managers react by trying to wish it away and hope it will disappear by itself. The main sin of management is to not adjust when the world around them changes. If a business formula has built a successful company and the career of those in it, it will nevertheless psychologically be very hard for them to change the formula even though external events have made it ineffective.

It is not always that managers see the problems coming though. Myopia is a classical mistake in business. People assume the distant past is less relevant and only take learning's from the last few years instead from the larger, less frequent, cyclical patterns. When companies and managers only look to and learn from the recent past they are potentially setting themselves up for failure.

Many times poor executive managers simply misread their potential customers. There is a pervasive myth that it is the idiosyncratic visionary leaders like Steve Jobs, who don't care about customer feedback, that succeed. But at the same time it is a classical mistake to think that customers like the same things that oneself likes. CEOs are generally affluent and hypercompetitive. Average Joe doesn't necessarily appreciate the same goods as these groups. Further, too often managers get bogged down in data and rules of thumb but fail to truly understand how the real people in their customer group actually behave.

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Just like everybody else executive managers can occasionally fall victim to a mania. Unfortunately they also have the power to act on their belief. At the peak of the TMT-bubble in the year of 2000, 90% of US CFOs thought their shares were undervalued according to a survey by Duke University. People fall in love with stories, especially if these elevate as persons. They want the stories to be true and they work very hard to convince themselves (and others) that they are. Then they rush off and do things like acquiring AOL for USD 111b – later written down to a value of USD 12b.

In manias the investing crowd suppresses inconvenient facts like arithmetic. Often a simple top down analysis of addressable market volumes, reasonable prices at larger volumes and expected market shares after new competition comes reveals the absurdity of the estimates needed for the mania to be rational with regards to a company's share price.

A Weakening Business Situation

*"If the rate of change on the outside exceeds the rate of change on the inside, the end is near."* / Jack Welch

Bad turning worse – we like!

Share prices react to change. A bad business is a good initial condition with regards to short selling, but it is the worsening of business conditions that is the real kicker. Bad going worse is worth shorting.

Company issues

Any of numerous issues can arise; the loss of a key client, product or executive, successful products going out of fashion, declining prices as a competitor starts a price war, rising raw material costs, signs of market share losses, failed expensive acquisitions, the inability to roll over corporate bonds or even government investigation of business practices and fraud.

Sector issues

The change doesn't have to be tied to the company specifically. If the industry the company is in goes into a secular or cyclical downtrend this will surely affect the share price. Industries are affected by new disruptive technologies, changes in industry structures and the competitive changes this brings and by changes in industry regulation or subsidies. All have the power to destroy a business.

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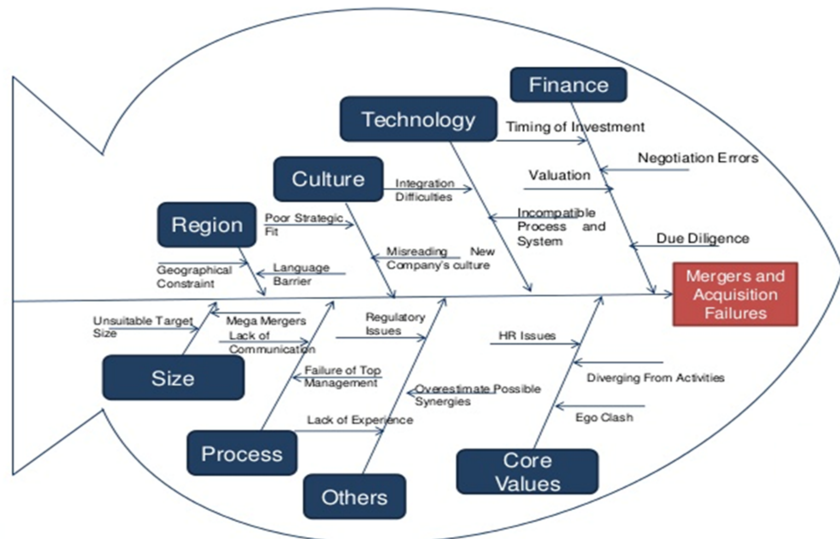
**Picture 7.11. The Failure Rate of M&A is Above 50%**

And it's a fish because…?




*Source: slideshare.net*

A favorite short selling target is the broken growth story. The reason is that they used to be market darlings and the share prices are often quite elevated with a long way to fall. It is important to wait until things start to crack before shorting. When something has started to break there will still be plenty of disagreement on the stock market keeping the price up.

Broken growth

Paradoxically fast growing companies showing losses can sometimes live on the general investors' hope and dreams longer than those that show profits. If there are no profits to start with, how can they weaken? At some point however comes the time when the company will have to ask for more money and these points can sometimes, but not always, act as negative triggers for the stock.

Product fads starting to top out can provide good short cases. The odds are with the short seller since failure rates of new businesses are far higher than the success rates. Often new products can grow as long as the pipeline is filled with the product for the first time. When all shelves of the value chain has been filled the product has reached the upper bend of the S-curve and growth slows down.

Product fads

The management's reaction to the changes will be key to a short case. The best situation is obviously if they fail to recognize that their industry has fundamentally and permanently changed. Sometimes changes are subtle but often they can be visible to everybody but the companies in the industry. Very few veteran managers in an industry are willing to revise their thinking and admit that they are now wrong. This would force them to remake their companies that are currently operating with maximum efficiency (but in accordance to an old business logic). The short seller wants them to stay wrong.

"To move from the old to the new is the only tradition worth preserving"

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In some instances managements respond to the decline of their core business by redeploying the corporate cash flow into businesses outside their circle of competence in what seems to be a desperate attempt to save their jobs. Some diversification efforts can obviously work but venturing outside one's core business is risky as it will leave you less experienced and generally with scale disadvantages compared to the companies that are already there.

"Diworsification"

The ability to understand and correctly react to change can be severely restricted if management is emotionally removed from their companies' operations. Corporate managers with lavish clothing and grand offices are no guarantee for failure but they obviously run the risk of not understanding what goes on in the ordinary day-to-day business of their companies.

What would Piketty say?

Especially in a commodity business, where the cost level is everything, outlandish executive remuneration can be a serious competitive impediment. And even when it's not, highly paid executives in striking offices carries a symbolism that is unlikely to foster a successful corporate culture where employees are willing to make sacrifices to succeed. Many corporate executives underestimate how important employee morale is.

Pride and suppression the short seller's best friend

The tendency to take credit for successes but blame everything and everyone else but themselves for troubles is a very sure sign of a company that will continue to struggle. Pride and suppression of facts don't make an agile company and the management is then more likely to "stay wrong".

High Leverage

Leverage, off and on the balance sheet, should always be judged in combination with the strength of the business operations of a company. A highly profitable business with stable demand and a cost mix with plenty of variable costs can withstand a higher debt level than the one with a less profitable and cyclical business with plenty of fixed costs.

Riskiness of company

Operational leverage can be estimated by the percent change in operating profit to the percent change in sales. In a downward spiral the blend of high operational leverage and high financial leverage could be deadly. The combination of a failing business and mounting debt very often leads to bankruptcy.

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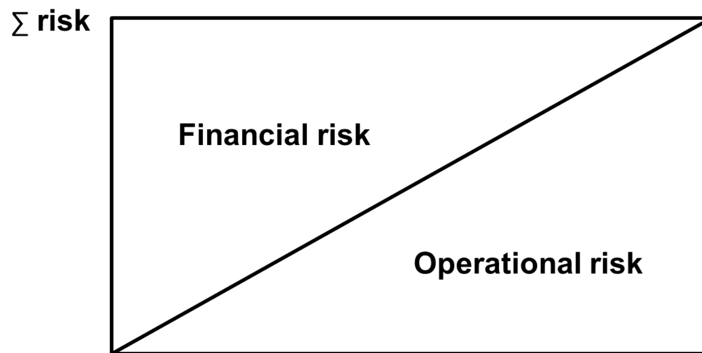
Picture 7.12. Operational Risk + Financial Risk = Total Risk




*Source: The author*

And then there is the "price risk" that comes with a really expensive share price

Target inability

The research of the short seller is not fundamentally different from that performed on the long-side but since it in this case targets the corporate inability to pay bills, it perhaps looks more closely at cash flows, the quality of earnings and the interaction between the balance sheet and the presented profits. If there are signs of a failing business then the level of debt is a huge positive for the short seller.

Debt vs equity and…

There are two ways that debt contributes to covenant breaches, credit downgrades and ultimately the demise of companies. The first is when the amount of debt in relation to the amount of equity becomes too large and the company eventually is forced in liquidation. In Sweden this process is initiated when half of the share capital has been exhausted. Thus, a company that cannot handle a reasonable decline in the value of assets, due to for example changing market prices or goodwill impairments without getting into financial troubles is unsustainably leveraged.

…debt payments vs cash flow

The other more common way that debt causes financial distress is when a company due to a lack of sufficient cash flow is unable to pay its bills, including the interest payments on its debt. Leverage effects aren't necessarily created only by debt. Contracts or commitments like leasing contracts that require regular payments over a long period of time have the same character as debt payments but don't necessarily show up as debt on the balance sheet. Instead of looking at interest coverage ratios, look at "fixed charge coverage" ratios. The inability to pay one's bills can lead to bankruptcy and a company that due to a high level of fixed payments cannot handle a reasonable cyclical decline in sales or an interest rate increase is unsustainably leveraged.

Poor debt structure

Apart from being too high in relation to the strength and stability of the business operations, debt can also be poorly structured. Often this is because the company has been greedy and chosen to finance itself as cheaply as possible. Banks call this maturity transformation but it is really a form of timing mismatch. A heavy dependence on short-term financing together with a tightening credit cycle can be a killer.

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Take Lehman as a case study. It wasn't the fact that the asset side of the balance sheet was loaded with faltering junk bonds that brought the firm to its knees (although this ultimately might have happened anyway), it was the fact that the funding of the firm consisted of very short-term bonds that suddenly turned out to be impossible to roll over. With a well balanced mix of bond maturities and back up credit facilities from banks the profits in the good times would have been marginally lower but the company would have been much better off in the bad times.

Like Lehman

**Picture 7.13. Without External Funding a Bank Cannot Exist**

*Source: prezi.com*

For companies with negative cash flow it is important for the short seller to understand for how long they can fund their operations and if they are likely to receive new money or not. Often there is a greater fool ready to fund the company another round and skilled investment bankers are always ready to assist in prolonging the death struggle. However, if the funding market has disappeared due to a worsening of the investment climate this is a stock that can go to zero.

When assessing the staying power of companies it is important to understand their reinvestment economics to apprehend their ability to grow in the long term. In all this the level of return on capital is crucial, as is the dividend. Companies that grow faster than they can afford and don't have any dividends to cut to improve their funding are potentially interesting short cases. The sustainable earnings growth rate is:

$$((\text{Net income} - \text{Dividends})/\text{Net Income}) * \text{ROE}$$

Target weak balance sheet, no dividend and low + declining ROE

For example a company that distributes half of its profits in dividends and has a ROE of 20% has a sustainable earnings growth rate of 10% and can swiftly increase this to 20% if dividends are cut. A company that doesn't distribute any dividends that generates a ROE of 5% has a sustainable growth rate of 5% and no flexibility. If the current growth is substantially higher than this it is generally due to an increase in leverage that cannot continue indefinitely.

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High Valuation

A fundamental short seller is the inverse of a long-only value investor. He shorts shares that are worth less than they cost. In the end the value of the company clearly matters and shares that are severely overvalued should eventually be shorted - but it is important to limit risk in shorting and the dominant risk in this case is the issue of timing.

Can you really invert an investor?

Expensive stocks with high valuation multiples often have good momentum and it will not be possible to stay short without considerable pain while waiting for the downturn. Especially in companies with open-ended growth the short seller cannot estimate when business fortunes will turn. Thus, valuation anomalies can last very long times and certainly longer than most short sellers are able to hold on to loosing positions. Hence, shorting on high valuation alone is often a recipe for disaster. Ask those who have shorted Tesla the last 4 years.

Again, avoid open ended growth…

The stock market expectations may well be unsustainable in the end but without a clear catalyst that will derail the corporate momentum, long-only investors will live on hope and take the stock even higher. There must be a fundamental change in outlook as a trigger or else the timing of the case could be wrong by years even. However, when the tide turns and companies face severe issues with their business model, then a high valuation is the icing on the cake.

…until the tide turns

A company doesn't have to have high valuation multiples to be overvalued. Companies in secular decline can sometimes have low multiples but with profits predictably melting away over time, the price is still too expensive compared to the worth of the company. This is a so-called value trap; a stock that may seem cheap on certain metrics, but in reality may not have the moats to protect its business or may face long-term chronic sector issues.

Value traps, a favorite of Chanos

The key issue for a short seller with regards to potential value traps is if the business model really has changed for the worse permanently. If so, cheap stocks can get cheaper as growth prospects disappear and profitability in core business units go down, until they eventually become worthless. The good thing for a short seller when it comes to sectors in secular decline is that the company will have a very hard time changing its fate given the sturdy headwind it faces.

Permanently worse

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**Picture 7.14. The Long and Short of It**

Taking a tall position?

*Source: marcustoday.com.au*

Insider Selling

Clues from deserting insiders

The transactions of corporate insiders in the shares of the company in which they have privileged insights are closely monitored by short sellers as they search for signs that "the rats are leaving the ship" ahead of a pending disaster. It is important to pay attention not only to unusual trends in insider dealings but also to transactions by larger owners.

Normally contrarian

On average corporate insiders are a combination of long-term and short-term contrarian investors. They tend to buy in large volumes when the stock market crashes (a pattern not mirrored by the corporate buybacks of stocks in the companies they run). They also buy and sell in a contrary fashion in relation to the smaller wobbles during the larger stock market cycle.

Normally net sellers

Since managers receive most of the shares they own through various incentive schemes and as such don't have to buy them, insider selling is over time done in much larger volume than insider buying. Insider selling of stocks on average doesn't signal much as it is a natural way for a corporate insider to pay for his living expenses and diversify his financial risk. Insider buying carries a much more potent signal since this is only done when the insider thinks he can earn high returns from it.

Acting out of the ordinary? Take notice!

Still, if you see insiders going against their contrarian default mode and selling aggressively despite the stock being down this should definitely be a warning sign. In fact, in combination with checking other boxes on the short selling checklist any large insider sales transaction should add to the negative case.

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**Picture 7.15. Saving What Can Be Saved**

How short sellers view management?

*Source: ageofautism.com*

CFO leaving

Continuing on the rat analogy, short sellers also pay attention to other ways insiders may abandon their vessel. High turnover among corporate executives and other key employees or stakeholders sends a similar message and if the CFO leaves without having a much grander assignment ready, this waves a red flag for many. This might even act as a trigger for the short sellers to enter into their positions.

A Trigger

Need psychological shift

We have already given some examples of changing operational or industry fortunes in the text above on weakening business situations. Take the time to revisit them. To act as triggers for a short case they have to manifest themselves into tangible evidence of the change – single events that can change the investment psychology around the stock.

Enter too early?

The main weakness of short sellers is their inability to correctly time their positions. Just as most shareholders are too slow to sell when a company's future irrefutably looks bleak, short sellers generally enter too early into their positions – at times one or two years to early. Since they think they have solved the investment case puzzle they expect everybody else to see the same truth immediately.

Wait for first crack

To adjust for this many short sellers only act when there is a visible trigger to the case. The stock will tumble on a change in investor psychology, which can be triggered, by various company, industry or economic events. It is less risky to wait for the first clear evidence of changes in business fortunes.

Better risk/reward

The price to pay is that some of the downturn now has already happened when positions are opened. The impatience and the tendency to enter too early is therefore in a way natural since after the general public fully has understood the corporate difficulties the

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investment opportunity can be gone. Still, on balance the risk/reward is much better when the short seller first identifies the flaws in the business model and the exaggerated expectations and then waits until a catalyst is identifiable to short the stock.

Already prepared

Any development, as those mentioned above in the section on weakening business situations, that lowers the expectations of future sales and profits can act as a trigger. After the news the stock will be in a tug-of-war between pessimists and optimists and the bear scenario will not be fully priced. The short seller who has already a fully developed bearish investment case at hand will be able to be significantly more actionable than the up until recently optimistic owner of the stock.

Poor quarterly results and profit warnings

The main triggers are poor quarterly results or corporate profit warnings. The cockroach theory says that if you see one there are probably more, hence the saying that "there is no such thing as one bad quarter." Obviously there are instances with just one bad quarter, but generally - even if issues are temporarily - in the real world outside analysts' excel spreadsheets troubles take time, several quarters, to solve. And they could even be the first sign of the full demise of the company.

Technical triggers

Not all short sellers use fundamental triggers exclusively to handle the timing risk as they argue that borrowing stocks will be too expensive when the trigger is in place. One practice can be to take the short selling ideas from the fundamental research process and then use technical analysis or share price trends as a timing tool for when to execute the trade.

This is how Scott Fearon of Crown Capital works. He generally waits until a failing company has lost half of its value from the 52-week high before shorting it. This is because he wants the stock to have enough downward velocity to hit the bottom. Another way to handle the timing risk is to average up by taking several gradually larger add on positions over a period of time.

Short Seller's Checklist

1. Liquidity
2. A Bad Business
3. A Weakening Business Situation
4. High Leverage
5. High Valuation
6. Insider Selling
7. Accounting Warning Flags
8. A Trigger

**Picture 7.16. Ticked Enough Boxes? Then…**

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Shorting stocks is a risky and exhausting endeavor. Mental flexibility and open-mindedness is key to doing it successfully. A too ridged view on a position will hinder the short seller to correctly process new information and will stay in poor positions.

"You've got to know when to hold 'em
Know when to fold 'em
Know when to walk away
Know when to run"
/ Kenny Rogers, The Gambler

Some short sellers close positions if they move a certain percent against them. Others can hold on to their high-conviction ideas for a long time and rather increase the position size when it moves against them. All in all, positions should be covered if the investment thesis isn't playing out or when it is judged to take too long to play out.

**But Isn't Shorting Unethical?**

Illegal

The practice of selling stocks short has stirred up feelings for as long as there has been equity markets and on and off shorting has been outlawed or restricted in numerous countries. For example during the 2008/11 global financial crisis it was periodically forbidden to short US financial stocks and Greek stocks – not that that seems to have mattered much as the largest price declines came after the shorting bans.

Un-American

The first known example of short selling is from 1609 in the Netherlands, Napoleon Bonaparte was an early critic of the practice and in the Wall Street crash of 1929-32 Jesse Livermore was accused of having caused the calamities and he received numerous death threats. Selling stocks short was for a long time after the crash seen as "un-American" as it profited on the misfortunes of American companies and investors.

Just switching order

A profitable long-only investor buys low and sells high in two transactions. A profitable short seller also buys low and sells high, but he sells before he buys. The number of transactions is still two, balancing supply and demand over time exactly as in long-only investing. Frankly, we are at a loss to understand how switching the chronological order of buying and selling the same amount of stocks can cause such uproar.

Ban selling?!

If someone thinks banning short selling is a good idea, why isn't forbidding any selling of stocks an even better idea as long-only investors no doubt create most of the supply on the equity markets? To take it further, shouldn't all research analysts be obliged to only issue strong buy recommendations for all stocks (not that there would be any stocks to buy given the selling ban)? Anything else must surely be unethical?

Correct price, not the highest price

Taken to the extreme the arguments for prohibiting short selling just looks silly. The stock market isn't there to set the highest possible price for a stock in any given moment; it's there to set the approximately correct price given the underlying future economics of the business. Over time stock prices are set by the fundamentals.

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Stock markets generally crash since prices have become too removed from the underlying economics of the listed companies, not because of short selling.

Picture 7.17. The Core of Short Selling

*Source: investorsunderground.com*

In Arabic, reading from right to left, this would be long-only investing?

Still, short sellers are often accused of depressing share prices and accentuate stock declines. This no doubt can be true temporarily, but it doesn't need to be as it depends on the investment strategy used when shorting. Any investor with a trend following strategy (long or short) will amplify already ongoing movements, while a short seller who shorts overvalued stocks and covers his positions when the share prices have gone down too much will instead help cushion the price swings of the market.

Trend following amplify, value cushion

Nevertheless, we are obviously not saying that all short sellers are always free of misconduct – they are after all human. In "short-and-distort" strategies a share is shorted and then negative rumors about the company are spread to try to push the share price down, where the short seller then covers his position. During the GFC media repeatedly reported that hedge funds colluded to bring shares down. However, the real problem here is the case of market manipulation, not short selling per se.

Short-and-distort

There is even a mirror strategy on the long side called "pump-and-dump" where the culprit buys a share, spreads positive rumors to push the share price up and then sells his position. Unlawful market manipulation should be prosecuted irrespective of which order the offender is doing his buy and sell transactions. Those trading with the manipulator will have made transactions with an incorrect view of the situation. However, over time the share price will normalize to reflect the underlying economics of the business – temporary mispricings will adjust.

Pump-and-dump

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Now, there are some instances when temporary mispricings might not simply adjust. These are situations where the pricing on the secondary market, which is what a stock exchange is, has a direct influence on the economics of the underlying business. In this case the short seller is not only reacting to the reality but also shaping it.

But when influencing the underlying…

One such situation is when a company is doing a (unguaranteed) rights issue at a predetermined issuing price. If potentially colluding short sellers in this situation temporarily manage to push down the share price below the issuing price the company might be unable to raise new equity capital, which might cause the banks to withdraw their loans and the company could potentially falter.

…there is an unfortunate asymmetry

In a bankruptcy the short seller makes 100%. Companies that ought to go bankrupt should be allowed to do so. The risk here is that a potentially economically viable business was forced into liquidation. That cannot be in society's best interest. In our view some sort of restrictions on short selling could be warranted in situations like the above. Why not restrict all selling? The selling long-only investor doesn't profit from the demise of the company in the same way.

The bad reputations of shorting likely comes from the fact that the short seller is profiting on misfortunes, such as declining stock prices and failing companies. It is more socially accepted to profit on success. Still, for example insurance companies also profit from misfortunes – and doctors, or journalists with their articles about the always-immanent or present disaster. Nobody dislikes them and calls them unethical.

The perceived difference is that insurance companies perform a helping service protecting from risk. They bring a positive value. The thing is, we would argue that shorting does the same. Short selling improves the price formation of the equity market by bringing in more perspectives that at times reveals crocked companies and through their trading short sellers improves the liquidity of the equity market.

The last few decades most corporate frauds have been revealed by internal whistle blowers, journalists or by short sellers. Auditors, equity analysts or regulators uncover very few frauds. Different groups have a natural tendency to see what their incentives tell them to see.

The Sherlock Holmes of the equity market? The short sellers certainly like to think so!

Shorting has today become a large part of the day-to-day business of insurance companies, pension funds and other institutional investors as they engage in alpha-beta separation through overlay strategies or adjust the weights of their equity holdings over regions and sectors. Often this is done indirectly through derivatives such as swaps, forwards or futures, meaning an investment bank – for a modest fee - does the actual shorting as their counterparty. But make no mistake, even if it is normal practice today, in the next financial crisis the cries for shorting bans will return again.

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## Selling

New topic…

With this we leave short selling and move on to "long selling". Although the topic of shorting always brings a lot of interest and there is much to learn, most of our customers are after all long-only investors.

…"long-selling"

**Picture 7.18. Two Sides of Asset Management**

*Source: bestsockpickingservices.com*

Structure
- Difficulties
- Remedies
- Hold-or-Sell Strategy

We have structured the section in three parts covering the psychological and institutional difficulties of selling, what can be done to correct these on a more general level and then we finish off with some more practical hands-on advice on how to react to specific situations. Again, as noticed above, the target audience is the fundamental long-term investor – not quants, technical traders etc.

### Why Is It so Hard?

*"Adding to a loser is seen as a 'bad' idea, but so, perversely, is selling a loser."* /Lee Freeman-Shor

Buying fun…

Buying stocks is easy. Anybody can do that. The difficulty lies in selling stocks and it boils down to psychology. Selling is quite simply less fun and less easy than buying. When acquiring a stock the mood is optimistic and the focus is on all the wonderful profits that will be made. While buying is fun and offers opportunities selling is an unsmiling business that still has to be done.

…selling not

Holding a position is clearly stressful. If the share goes down, or nowhere, doubts start to swirl in the back of the mind. If it goes up investors are torn between taking sweet profits but then risk not taking part in a potential further rally. Selling stocks either makes a loss permanent or exposes the seller to the risk of seeing the stock continue to rise in price after it has been sold.

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Pain avoidance

Investors, being human, are largely ruled by emotions and a falling stock price risk freezing them into inactivity. The emotional experience of a loss is about two times stronger than that of making a profit so it is littler wonder we try to avoid the pain of realizing a paper loss. Holding on to the position at least gives a theoretical chance of a turnaround. Selling comes with a finality that is hard to come to terms with.

Consistency seeking

Our mind also strives after consistency. Selling is hard as it means a total reversal of our earlier positive opinion that we have invested effort and prestige into. Denial and holding on is much more psychologically comfortable than selling and admitting that we were wrong about the stock and as such perhaps we are not the great investor we thought we were.

Poor and stupid

The immediate result of selling at a loss is making us poorer and feeling stupid – no wonder we dread it. As a result the investor might very well unconsciously screen away new information that is unfavorable for the investment case of the stock even if it really should have affected the investors view of the case. The real defeat for our irrational selves is when investors freeze in the initial part of a downturn and then panic later on and sell at the bottom.

Enjoying the view?

**Picture 7.19. Less Fun on the Way Down**

*Source: idanny.wordpress.com*

No help

A second issue with selling apart from the psychological difficulties is that it is a solitary activity. There simply isn't much help from anyone else when it comes to selling. As Count Galeazzo Ciano expressed it "Victory has a hundred fathers and defeat is an orphan." Few investment books cover selling (or position sizing for that matter) with anything more than a few paragraphs. It's all about how to find stocks to buy.

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7% even though most underperform

Sell-side research reports don't offer much support either. In the 1990's less than 2% of US broker research recommended selling stocks. After criticism post the TMT-crash the number rose to about 7% in the next decade. In fact, since the recommendation scale of investment banks is so skewed a hold recommendation should probably be considered as a plea to sell a stock.

There are reasons

There are very clear business reasons for the lack of sell recommendations. The problem for the analyst in recommending selling a stock is that he can never be quite sure if he is right. With very even odds it might not be worth rubbing corporate executives the wrong way and by this risk jeopardizing the access to primary deals and other business for his employer and to preferential treatment in access to information from the company for himself.

Also, there is an asymmetry in numbers that explains the few negative recommendations. A buy recommendation has a wide audience for the equity sales force as almost all investors can buy a stock or buy more of it. A sell recommendation is really just actionable for those asset managers who already own a stock – in comparison a much smaller target group. In an industry that lives of the fees from trading a less actionable recommendation isn't exactly the stuff that builds a career.

No career builder

Further, the equity sales force might also be reluctant to bring forward a sell recommendation to the few clients that own the share since having bought the stock the client obviously likes it and if the recommendation turns out to be wrong and the share keeps moving up after the asset manager sells his position, this can be a thorn in the side for a long time. The customer will have lost money that he previously had locked in because of the recommendation. Better not to be the bearer of evil tidings.

**Ways to Handle the Difficulty**

*"[Investing], in part, is like a poker game, wherein you have to learn to quit sometimes when holding a much-loved hand - you must learn to handle mistakes and new facts that change the odds."* / Charlie Munger

Having a plan…

Winning in financial markets depends a lot on staying levelheaded and rational when everybody else is panicking. The problem is that when we are under stress the quality of our decisions deteriorates. Winners use self-imposed thought processes to stay rational. To be able to do this there has to be pre-determined plans for which actions that should be taken depending on various developments. Thus, success in investing is very much down to execution of a good process and investors therefore must develop a sell-or-hold strategy.

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Writing down a plan on paper reduces stress and since we take our best decisions when we are relaxed over time it should improve profitability. A written plan reduces tension by separating the tasks of analyzing and trading. The investor needs the peace and quiet to think things through in a calm state of mind and then benefits from clear instructions in the heat of the battle.

…helps tough decisions

To outperform other competing investors and by this the market, an investor cannot do the same things as everybody else. The advice to not follow the crowd goes for selling as well as for buying. One key to success is to do what isn't easy. It is easy and cozy to join the herd. Remember that the market isn't there to give you comfort. A well-defined sell-or-hold strategy will help taking tough decisions.

General framework

In our view all this means that an investor should both develop a general framework for his sell-or-hold strategy covering a number of potential developments and that there should also be an individual documentation for each position penciled down before the investment is even executed.

Stock specific documentation

This individual documentation should outline the reasons for buying (i.e. the investment case) and the plan for selling including trigger points for how to handle losses, a profit target (in absolute monetary terms or in absolute or relative valuation multiples) and the planned timeline for the investment case plus a course of action if things don't materialize as expected. The position and the investment case are monitored and the documentation is potentially added to as things change.

Tracking the fundamental investment story is made much easier if specific milestones for sales, margins, capital efficiency, market shares etc. at specific times in the future are specified at the time of the purchase of the stock. Further, simply by focusing on trigger points for how to handle losses the investor gets a more balanced picture of the position.

Cleaning the slate

Clearly, an investment case can change over time and this is often a warning sign, but there could be reasons to keep a position that hasn't developed as expected. What is important but mentally tough is to constantly try to reassess all investments, in or out of the portfolio, as if you are looking for them at the first time.

Doing so hinders the investor from lazily assuming that his original assumptions are still valid. The most central question that should guide the sell-or-hold dilemma is "If we didn't own it, would we be buying it today?" If not, it should probably be sold, but it (and the method of selling) depends on what type of company/stock we are discussing.

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**Picture 7.20. A Key Tool**

If there is one take away

**§ 1. "If we didn't own it, would we be buying it today?"**

*Source: The author*

The question helps us to break free from the psychological biases that come with holding a position. It helps viewing buying and selling as two fully separate decisions with an unconnected process for the sell-or-hold decision. It is hard to sell darling ideas where we have invested time and ego and very easy to hang on to them despite that they have passed their due date. If investment decisions are taken in a group of for example three persons, demand unanimity to purchase a stock but only a majority to sell.

Avoid anchoring

A good sale is one where the price shows an unfavorable development after the disposal and the initial purchase price has nothing to do with this. Knowing what the entry price was risks creating a mental trap called anchoring, an unwarranted focus on an unrelated number. "The share doesn't know you own it." Getting even is not relevant and being tempted to take home profits too early can be deadly for returns. Therefore we would think twice about including the entry price in the individual documentation about a position.

A separate process from buying

**Picture 7.21. The Sell-or-Hold Strategy**

*Source: nashvillebeaconpropertysolutions.com*

Framework

1. When profit
2. When loss
3. Other

The general framework for a sell-or-hold strategy should at least cover three types of selling situations a) selling with a profit at a profit target, b) selling with a loss and c) selling for other reasons such as that the conditions have changed the investment case, growing doubts with regards to whether the initial analysis was correct or that there are other uses of the funds that are expected to be more profitable.

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We start with the losers

Since the sell-or-hold decision is the most painful when it comes to losing positions, let's start with this miserable situation. When a stock is significantly down the investor must accept that he was wrong, either with regards to the case or in the timing. When you are wrong you have to adapt, you have to act.

Drawdowns kill compounding

The thing with losses is that they become disproportionally harder to come back from the larger they get. If a stock goes down 25% it has to go up 33% to get even. If it goes down 50% it has to go up 100% and if it goes down 75% it has to go up 300%. Nothing of this is impossible but the deeper underwater a position gets the less probable is it to get back to scratch in near time. Research shows that out of stocks that go down as little as 20%, only 1/3 make up for it over the next year.

Never do nothing!

Due to asymmetry described above the one thing you cannot do when experiencing losses over a certain magnitude is nothing. Two things work – either you sell or you buy. Never do nothing.

Either you sell…

The first strategy uses stop-losses that give investors a fair number of small losses but never the big ones that are impossible to turn around to profits. To quote George Soros "It's not whether you are right or wrong that's important, but how much you make when you're right and how much you lose when you're wrong." The advantage of a mechanical stop-loss that you decide on in advance is that it forces action at a time when a person otherwise might be psychologically unable to handle the situation rationally.

The configuration of the stop-loss to get out of a position before it gets too large is less important than the consistency of its use. It could be a rule to sell when the stock price is 20% or 30% below the entry price. It could be a trailing stop-loss to sell 25% below the highest price during the holding period.

…using a stop-loss

The one important thing is that the stops aren't set too tight or else the volatility in the share price will whipsaw the investor and more or less all positions will end with a small loss. What we in this case as long-term investors want to avoid is digging such a deep hole that we cannot get out of it and then for example a 25% loss is manageable. The really advanced shaping of stop-losses differentiates between the volatility of various stocks. The greater the noise level, the wider the stop.

Or you buy…

The other way to avoid the hole too deep to escape, is to double down on the position. In this case we wait a little longer than in the first strategy and then we double down by adding to the position in a series of smaller purchases. This process can be initiated at for example 25% or 35% thresholds. By doing this the average purchase price of the position is lowered to something that is possible to make a profit from when the stock turns up again.

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…but with discretion

This second strategy cannot be perused as mechanically as the first and to work the reinvestment has to be in well-chosen stocks. Just because something is cheap doesn't mean it will be a good investment. If the stock has declined for a good reason it should be sold. One potential issue with this strategy is that it depends on either having money at the sidelines in cash to reinvest or you have to sell some of your other positions. It is also very difficult to execute during periods when the portfolio is seeing redemptions and money to reinvest is hard to get by.

If you are to keep the loser then you buy more

**Picture 7.22. Selling Decision for Winners**

*Source: uscommercedaily.com*

We turn to winners

In a winning position an investor buys a stock for a price that is less than he thinks the stock is worth and then he sells it when it reaches the pre-determined price target. With a predetermined price target the risk of an unhelpful pro-cyclical enthusiasm for a position becomes lower. It also helps the investor to hold on to a position and not get spooked to sell by smaller setbacks.

Enough is enough

Ideally the stock is of course sold above the estimated value but it is important to have a sense of what is "enough" - overextending a position risks bringing larger losses. Still, winning positions often come with stocks that have a strong current momentum and long-term investors have a tendency to both buy too early and sell too early.

Rising E or PE?

To avoid the latter the investor who uses absolute target prices for when to sell can benefit from distinguishing between situations when the rise in the share price is mostly a matter of rising fundamentals or of rising valuation multiples. When the cause is better business momentum it might be well worth doing a new valuation estimate and potentially jack-up the target price. Even if a pre-determined valuation multiple level is set as the exit trigger a strong business momentum can motivate some sort of structured process to delay the sale to be able to ride the stock further.

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Some investors use a moving stop, also called a trailing stop, once prices approach their price target but they still want to stay in a stock with strong upwards momentum. Here the long-term investor is borrowing a medium-term investor's tool for exiting. It is vitally important to consider this as an investment decision of its own with a separate set of risks and rewards. At the same time as there is a chance of an extra gain there is a risk of giving back the profits already made.

Trailing stop-loss…

To mitigate the latter risk in this investment decision a trailing stop-loss should only be initiated when a stock reaches its target and have a certain level of strength in its momentum. If there are bearish signs when the target is met a trailing stop should never be used. Further, the level of a moving stop is never to be moved down.

…if strong momentum

The trading literature is littered with suggestions on how to apply trailing stop-loss levels. One method is to use a very short moving average and use this average as the trailing stop. Another is to set a distance y% from every new market top (although much narrower than the 25% discussed above). Further, it is possible to complement rules like this with a time stop to get the investor out of the now overvalued stock if it doesn't move sufficiently within a certain amount of time.

**Picture 7.23. Pre-determined Rules Help Stressed Minds**

Yes, there are a lot of pictures on selling around

*Source: googlepictures.com*

And then there are the other stocks

Investor's selling isn't confined to selling clearly winning or losing positions. Selling for other reasons can be that the conditions have changed and by this the investment case, that doubts are growing with regards to business fortunes the correctness of the initial analysis or even that there are other uses of the funds that are expected to be more profitable.

It is important not to abandon positions too casually since transaction costs eat portfolio returns but there is still no obligation to keep a stock until it reaches its price target. Changes in the corporate environment of sufficient importance should trigger new research and a new independent investment decision.

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Expect trouble?

If you start to expect future trouble it is better to get out. If for example the investment thesis is showing signs of not developing as expected it might be a reasonable first step to take partial profits. The gut feeling is often right: "When in doubt, get out". Also, for stocks that show no signs of going anywhere it is possible to use time stops that force the investor to sell after a pre-determined time period.

Monitor investment case changes

To be able to sell either because the investment thesis was wrong or because changing fundamentals made it incorrect, it is a good practice to prepare a regular exception report that flags issues that indicate changes to the investment thesis. If the fundamentals that caused an investor to own a stock change and the investment case gets weaker it is important to recognize this early to be able to move on before everybody else does the same.

All positions in a portfolio must naturally as much as is practical be viewed in relation to all other potential investments available. This means that stocks now and then could be forced out of a portfolio to make way for another position that is deemed superior.

Better alternatives

Still, selling one stock to raise funds for a new purchase of another stock could be a bad practice. The reason is that the sale isn't entirely due to the merits of the disposed of stock itself but to other considerations. A solution could be to hold a certain amount of an intermediate asset like cash for an absolute return investor or an index future for a relative return investor. With this "money parking tool" at hand the two decisions can be separated.

**Picture 7.24. With All Reasons To Sell, Will There Be Stocks Left?**

*Source: googlepictures.com*

Bad reasons

Bad reasons to sell positions are frustration or boredom, alternatively stress due to market noise and financial media chatter. When analyzing news stories, imagine yourself situated 5 years into the future and ask yourself if this piece of news is something that will be remembered at that time.

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It is important to realize that in markets all investors make mistakes and they have to learn to live with this. How costly the mistakes become depends on the actions taken – try to be right large and wrong small. After positions have been closed they – and especially the losing ones - should be analyzed and turned to a learning experience. To be able to do this the investor needs to set up the initial type of documentation on each position that we discussed above.

Learning from mistakes

Before we move on to our suggestion for the practical implementation of a sell-or-hold plan we shortly want to discuss the use of analytical stop-losses and their formation. An analytical stop-loss is when a price decline of a predetermined size instead of triggering a sale of the share, triggers a new mandatory review of the investment case.

Analytical stop-loss

A review in relation to an analytical stop-loss should try to clean the slate and look at the situation objectively as a new case, carefully considering all new and old information and redoing the relevant documentation to reach a new separate purchase decision. Simply put, if the story changes and this still warrants a portfolio position this should be recognized as a new investment decision with new documentation.

A brand new case…

However, cleaning the slate entirely is psychologically very tough. The risk is that the investor rationalizes, trying to come up with excuses to avoid having to take the pain of selling and just keep the position. The danger is then that the review process simply gives the illusion of control rather than actual control.

To mitigate this risk it might be beneficial if the person responsible for the new research is changed from the person who recommended the stock in the first place. We realize that this practice requires resources from the asset manager and cannot be implanted by all, but is probably the psychologically right thing to do and if the practice is known up front it doesn't have to be seen as a defeat for the first person researching the share. Facts change and this should change opinions.

…by a new person

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**A Sell-Or-Hold Strategy**

Fundamental long-term investors

To set the stage, with reference to the Rubik's cube shown above, we will in this section only focus on the long-term fundamental investor. From the above illustration this only leaves the three scenarios of selling winners, selling positions that are treading water and selling losers.

Franchise stocks and deep value stocks

We now add the complicating aspect that the character of stocks differs and they then probably shouldn't be treated in the same way. Different investment cases bring different sorts of stocks into the portfolio. The two types of investment cases – and by this types of stocks – we intend to include are a) the high quality, compounding, franchise stock with strong barriers-to-entry and b) the beaten down, deep value, recovery case where the prospects (or assets) of the company are better and more valuable than the stock market is pricing in.

First forever, second as short as possible

It is in our view important to distinguish between franchise stocks and deep value stocks. While the first is meant to be kept forever if nothing goes wrong, the other is bought for 50 cents on a dollar and is meant to be sold as soon as it returns to 100 cents on a dollar – the sooner the better. Once a deep value stock comes back up, it is highly probable to back down again so it is vital to exit promptly. With regards to a franchise stock it is more a judgment call at which point the valuation is simply too high compared to other equivalent stocks.

Decision trees

To bring clarity and overview to situations with many scenarios it is often useful to construct so-called decision trees. This helps a person decide what to do in any given situation. These trees can understandably be structured in different ways but we have chosen to make one tree for the franchise stock and one for the deep value stock.

Assumptions

In discussing the scenarios we are going to make some huge assumptions that might not apply to all investors. We assume that they for each position has specified what they think the bear case value of the stock is and similarly the base case value and the bull case value – i.e. three different absolute valuation estimates. Further, we assume that the price target is set in accordance to the base case value. In our view explicit bull and bear cases based on scenarios for the key factors affecting the company's value is superior to simply setting a price target and then using a +/- range of a certain percent around this.

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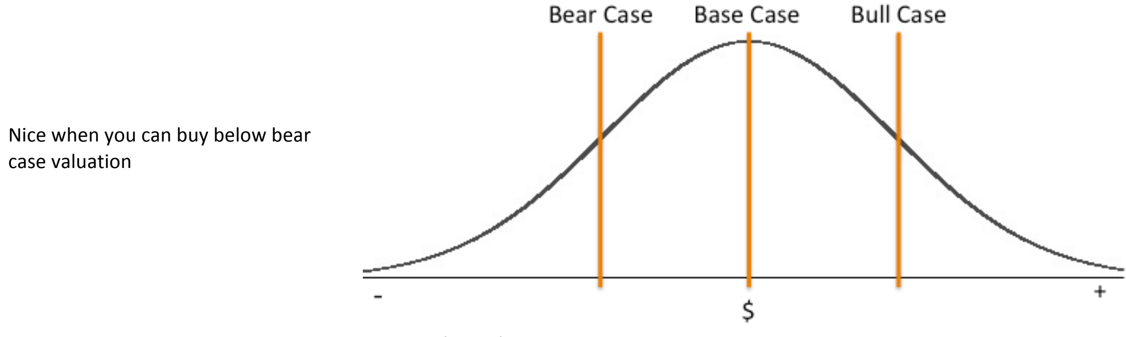
Picture 7.25. But The Distribution Is Rarely This Orderly

Nice when you can buy below bear case valuation




*Source: The author*

Remember the transaction costs

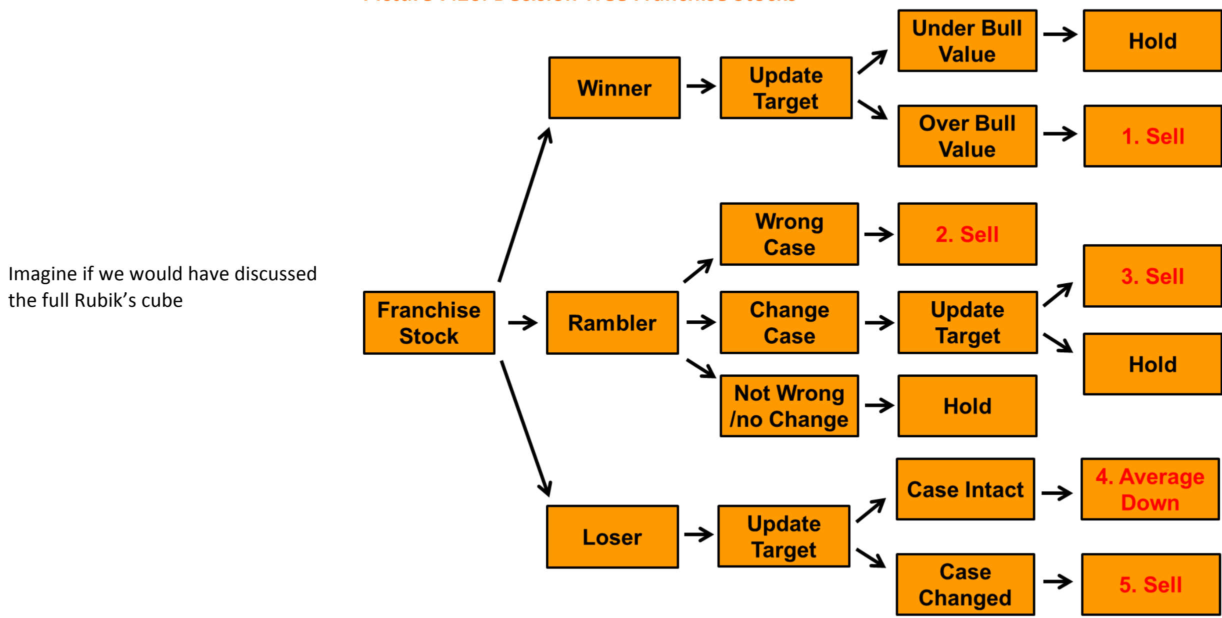
Also, we assume that there are sufficient personnel resources so that several persons can analyze the same case. Finally, in the discussion below we will not factor in the relative attractiveness of stocks outside the portfolio when thinking of the handling of the current positions. We implicitly assume that the investor can have sufficient money in cash or index futures to be able to handle each stock as an individual decision. Even so, remember transaction costs and throw some friction into the trading in and out of the portfolio.

Start with franchise stocks

We start with the high quality franchise stock. The reason we ideally want to keep them for as long as possible is their compounding ability. With an ability to continuously reinvest retained earnings at a high return on investment comes an exponentially growing compound interest that over time can take the value of the stock to drizzling heights – think Berkshire Hathaway. Hence, they are valuable to hang on to – if nothing goes wrong with their future compounding capacity or they get way too overpriced and by this introduce a price risk to the portfolio.

Imagine if we would have discussed the full Rubik's cube

Picture 7.26. Decision Tree Franchise Stocks




*Source: The author*

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From the top

We work our way from the left to the right and start with winning stocks that are approaching their price target. Our handling of winning franchise stocks tries to balance the fact that while we don't want to trigger disposals of shares we fundamentally like (especially in the latter part of a stock market cycle when they often all are priced close to their fair value) with the equally important fact that we don't want to introduce too much price risk in the portfolio. A very expensive franchise company can become quite vulnerable to even minor deteriorations to their quality.

Revisit research

The first action would be that when a stock only has 5% upside to its price target the research should be updated. Perhaps the stock isn't really close to its price target; maybe it is the three valuations, and by this the price target, that should be moved up? However, don't move the valuations up just because you want to keep the stock – there has to be fundamental reasons.

Over/under bull value?

Now, say that the stock has moved up to its renewed price target. The next action would be to keep it as long as the share price is below its bull value. It is a stock we ideally want to keep over the long term, our estimate of the base case value can never be fully correct but the intrinsic value of a stock is more of a range and the stock obviously has a good momentum. Potentially the size of the position could be scaled back at this point to take home some profits. Being slightly expensive it might not give the same potential returns going forward if the stock has to tread sideways to grow into its valuation multiples.

Sell when too expensive

If instead the stock has moved up to the bull case value then we initiate sell procedure number 1. If the stock momentum the last period, measured by the slope of the 22 days' moving average of the share price, has been strong enough we decide on a trailing stop that gets us out of the share when it breaks below the 22 days' moving average, if that point isn't below the bull case value. If the momentum isn't sufficiently strong the stock is simply sold.

Ramblers

We now come to the handling of the franchise ramblers. They can be of many different sorts and they often don't have to be handled as promptly as a winner or loser. Every position however has to be monitored and the view on the investment case periodically refreshed.

No moat = ruin

If the conclusion of such a renewed view is that the initial investment case was wrong and that the competitive advantage of the company or the barriers-to-entry for the competition to the firm isn't as durable as originally thought, then we initiate sell process number 2 (a faulty initial conclusion almost never results in a positive change), and since it's a rambler the momentum isn't great so we just sell the stock outright.

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If events post the purchase results in changes to the investment case the cause of action will differ if the current potential still is attractive or if it's not attractive enough to warrant a position in the portfolio. If the latter is the case the sell procedure number 3 is in force and with ramblers we sell straight away. If the changed investment case is strong enough or if the initial case wasn't wrong or hasn't changed the share is kept.

"When the facts change, I change my mind. What do you do, sir?" / John Maynard Keynes

In real life things aren't as binary as we describe them here (a case is wrong or not wrong etc.). The bias for franchise stocks are towards keeping them so small negative changes to investment cases should probably be given some leeway. It's a judgment call case by case.

So how should we handle the fact that the ramblers don't move much and tie up capital to little gain? We don't want to use time-based stops since it is very hard to know when the market will start to price in the fundamentals of a stock and thanks to their compounding franchise stocks grow more valuable over time. Instead we propose the use of covered calls to earn money while waiting.

Covered calls

A covered call is when the owner of a stock issues call options on that share and by this earns an option premium. If the strike price of the written option is equal to or above the target price of the investor and the option gets exercised then he is in effect selling the share at a price point where he could have considered parting from it anyway.

Profiting while waiting

It isn't always possible to issue call options at the prices requested and running a structured covered call operations doesn't come without some labor attached. Hence, the asset management operations must be of sufficient size for this advice to be effective. Still, for someone that knows what his absolute price targets are, covered calls is a great way to get paid to wait until the stock price reaches its estimated value.

We turn to the losers

In handling the losers among franchise stocks, we have chosen not to use actual stop-losses, but to instead use analytical stop-losses to force a sell-or-average down decision. Since the research takes time to perform we activate the analytical stop-loss when the stock is down 20% from its 52 week high and it has underperformed the equity market by 15% since that high point.

Revisit research

A separate analyst or investment manager from the one that performed the original analysis researches the investment case again and sets new bull, base and bear values and a new target price. If the case despite the downturn is deemed intact the buying process number 4 is initiated. The position is increased to a size that reflects its current risk/reward compared to the other stocks in the portfolio. If the case is not intact but the downturn has been justified, the stock is promptly sold in selling process number 5.

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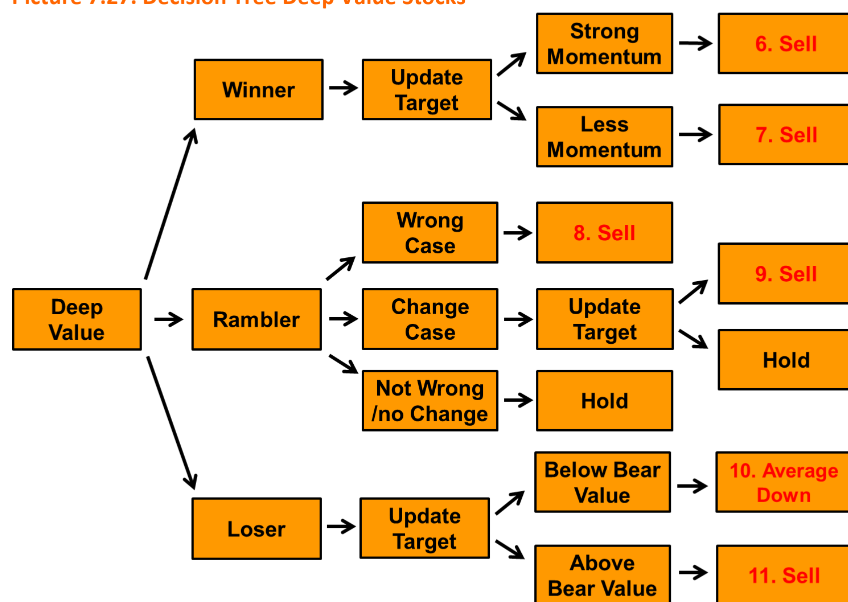
A profit warning or a poor quarterly report could very well have caused the loser's share price decline. With regards to these events we haven't forgotten the cockroach theory - if you've seen one there are probably more around. Still, as a long-term investor in these high quality companies and as long as the troubles are deemed temporary and don't affect the intrinsic value too much, we should be able to withstand a few bad quarters.

Take the long view

We now turn the page and take on the sell-or-hold strategy of the deep value stocks deemed too cheap. This isn't stocks in companies with a quality that obviously makes us want to hold on to them forever so we are more trigger happy in the selling.

Next up deep value

**Picture 7.27. Decision Tree Deep Value Stocks**




No, it's not the same picture

*Source: The authors*

Just like previously with franchise stocks we work our way from the left to right and we start with the winners. The first trigger is when a stock only has 5% upside to its price target. Here the research and the price target are updated. If the price reaches the renewed target price then the investor should take stock of the strength of the current momentum.

Start from the top with…

If both the share price momentum, again measured by the slope of the 22 days' moving average of the share price, and the business momentum, either measured by the strength of analysts' consensus earnings revisions or simply sales and earnings year-over-year growth, is above set thresholds then we initiate the sell strategy number 6 using a trailing stop-loss.

…the winners

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Selling faster

This is the same method as the trailing stop-loss strategy in process number 1 for franchise stocks but we now initiate it in relation to the target price instead of in relation to the bull value. If the momentum isn't strong enough we quickly sell the stock in process number 7. We bought the stock low and we sold it high so we are happy.

Different ways to be wrong

The handling of rambling deep value stocks is totally parallel with that of the franchise stocks treading water, covered calls and all. The reason the investment case might be wrong (because of bad initial research of change of events) is now however not that a company of high quality potentially is deteriorating, but that a company of less quality no longer is deemed to be significantly improving (or its financial situation, and by this its saying power, is worsening).

Richard Perry of Perry Capital has expressed it as "Value is buying a dollar for 50 cents and having a business plan that turns that 50 cents back into a dollar. Value traps are buying a dollar for 50 cents and a business plan that makes that dollar worth dramatically less than 50 cents."

Avoid value traps

We want to avoid value traps so the bias for deep value stocks is not equally lenient as for franchise stocks. Small negative changes to investment cases could probably still be tolerated but not as easily. It's a judgment call case by case.

Deep value losers

We now come to the bad lot of deep value losers. When the stock is down 20% from its 52 week high and it has underperformed the equity market by 15% since that high point a separate analyst or investment manager from the one that performed the original analysis researches the investment case again and sets new bull, base and bear values and a new target price.

Harsh standards

If the current share price is below the bear value by at least 10% the position is increased to a size that reflects its current risk/reward compared to the other stocks in the portfolio in the buying process number 10. The reason for the relatively harshly set limit is that this case has shifted from an offensive one to a defensive and this should often be avoided. If the price is above that mentioned limit the stock is promptly sold in selling process number 11.

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You have almost reached the end of the text

Time-based alternative

Potentially we could also choose to add on yet another process to the losers and ramblers within the deep value stocks. We didn't want to use a time-based stop loss for franchise stocks since they are compounders that build their intrinsic value over time. This isn't obviously the case with deep value stocks. Time isn't their friend in the same way.

No trigger

The tool we would implement would be to trigger an analytical stop loss two years after the purchase of the position if the stock hasn't moved up by a certain amount. The review would focus on the investment case overall but mostly on triggers for the revaluation and if the new research cannot point to a clear trigger within the next year the share could be sold. This is outside the decisions tree above.

Follow but break

The power of a predetermined framework is that it aids rational action in times when stress otherwise would have made rationality tough to muster. Still we must to the above decision trees add the subordinated clause: "if nothing else makes more sense." Rules should always be followed but you must know when to break them…

Develop your own method

This ends the text on selling. Was the sell-or-hold strategy too complex? Didn't it fit your asset management model? If you have disagreements, opinions or suggestions for improvements give us a shout. We hope the text at least has given you the inspiration to develop your own framework.

Happy investing.

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