Winning Investing Strategy: Know Yourself. Know Your Stock.

Description

The stock market is one of the greatest inventions of mankind. It allows anyone to make money by buying stocks. Sometimes investors are too focused on the stock price and they forget that there's a business behind each stock, and behind each business there are people running it and keeping it going.

A stock's performance is ultimately directed by the performance of the business behind it. However, not all businesses behave the same way.

Between 1977 and 1990 Peter Lynch was the manager of the Magellan Fund at Fidelity Investments and averaged annual returns of 29.2%.

In his book *One Up On Wall Street*, Lynch categorized stocks into six categories: slow growers, stalwarts, fast growers, cyclicals, turnarounds, and asset plays.

By knowing what kind of stocks you're buying, you can guess the kind of behavior they'll exert and invest according to those behaviors if they suit your investment style. Chances are, you'll buy a mix to create a balanced portfolio of stalwarts, slow growers, and fast growers. Cyclicals, turnarounds, and asset plays can be sprinkled in if desired.

Slow growers

Slow growers are typically large companies. If you think about it, it's much harder for a large company worth $10 billion to grow to $20 billion than it is for a small company worth $1 million to grow to $2 million.

For example, **Fortis Inc.** (TSX:FTS) was a slow grower in the recent past. It only managed to increase dividends at a compound annual growth rate (CAGR) of 3.4% from 2011 to 2014. It was just keeping up with inflation.

However, slow growers can spur growth by investing in projects. Fortis managed to increase dividends at an annualized rate of 17.2% in 2015 thanks to its investments.

Stalwarts

Stalwarts are reliable businesses that grow faster than slow growers but are not the star performers. They grow in the 6-8% range. **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) comes to mind as an example.

You can count on the bank returning profits to shareholders in the form of dividends. Typically, you can rely on it increasing that payout as well. In the past three years, Bank of Nova Scotia increased dividends at an average rate of 7.7%.

Fast growers

Fast growers are companies that are growing 20-25% a year. They are your star performers. You can expect high capital appreciation from these companies. However, if they fail to deliver that 20-25%, you risk multiple contractions, which would make the price go sideways, or worse, fall.

From 2008 to 2014 **Starbucks Corporation** (NASDAQ:SBUX) experienced earnings per share (EPS) that grew at a CAGR of 25%. In the same period, it appreciated 727%!

Cyclicals

Cyclicals experience cycles of expansion and contraction. **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) (and its stock price) does well when the economy does well because more products need to be transported. However, if the economy is not doing so well, the business would grow at a slower pace, or worse, even experience EPS decline.

Turnarounds

Turnarounds are neither slow growers nor cyclicals. They are potential failures. A poorly managed cyclical could be a potential turnaround if it looks like it won’t survive a contraction period. However, if the turnarounds survive they could be lucrative. Consider only putting in, at most, 1% of your portfolio in a potential turnaround, so you won’t be upset if it goes bankrupt.

Asset plays

In my opinion, asset plays are the hardest to find. They’re the companies that have valuable assets that haven’t been realized by the experts and most people.

So, its shares sell super cheap compared to the value of the assets it owns. If you can find these businesses, you should take advantage of them by buying shares before others do. However, you might have to wait awhile for others to realize the value.

In summary

By knowing what kind of stocks you’re buying, you’ll have rational expectations of each stock and can build your portfolio according to your personal investment style.

To figure out your personal investment style, you can buy shares of different stocks to see what suits you.

Just remember that stocks can jump from one category to another. So, you should be prepared to react and manage your portfolio accordingly.

CATEGORY

1. Dividend Stocks
2. Investing
3. Stocks for Beginners

TICKERS GLOBAL

1. NASDAQ:SBUX (Starbucks Corporation)
2. NYSE:BNS (The Bank of Nova Scotia)
3. NYSE:CNI (Canadian National Railway Company)
4. TSX:BNS (Bank Of Nova Scotia)
5. TSX:CNR (Canadian National Railway Company)
6. TSX:FTS (Fortis Inc.)

Category

1. Dividend Stocks
2. Investing
3. Stocks for Beginners

Date
2025/08/23
Date Created
2015/11/25
Author
kayng