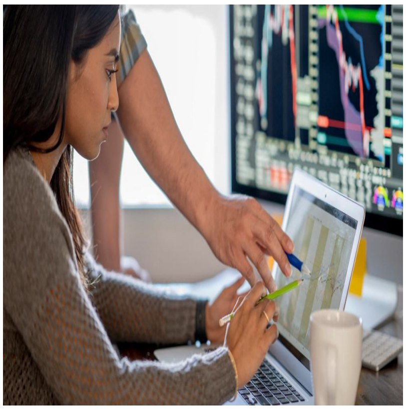

This Is What Warren Buffett Learned From His Worst Deal Ever

Description

Not all your stocks make money. The goal is to balance your portfolio such that gains outweigh losses. For that you have to learn from your mistakes and that of others. Luckily, the information age has many case studies around mistakes and opportunities. One such story is from Buffett's investing diaries.

Warren Buffett's worst deal ever

Warren Buffett admitted that his most expensive mistake was Dexter Shoes. This case study is a combination of three mistakes in his investing life:

- First mistake – He paid for a losing company Dexter Shoes with **Berkshire Hathaway** shares, which were far more valuable. If only he could go back and convert it into an all-cash deal.
- Second mistake – He kept holding onto a company with weak fundamentals. Dexter Shoes was losing to competition from cheaper foreign shoes. A restructuring fix could not solve the problem.
- Third mistake – He didn't exit and minimize his losses when he got the chance. Had he reinvested that money in another company, he would have fetched better returns than on Dexter Shoes.

The Dexter Shoes of today's market

In 2021, many investors bought **Air Canada** (TSX:AC) and **Cineplex** (TSX:CGX) stocks as they were buzzing from the end of pandemic-induced lockdowns. Planes could fly without restrictions, and all movie theatres were open. But these companies have been operating on wafer-thin margins with limited low single-digit revenue growth before the pandemic. Ask yourself, would you have invested in these stocks before the pandemic? If the answer is no, you know what you should sell.

Air Canada has a $6.7 billion market cap on a total debt of $16.6 billion, and Cineplex has a $527 million market cap on a $1.9 billion market cap. Debt outweighs equity by a significant amount.

In January, Cineplex sold its Toronto head office to repay some debt obligations. Air Canada retired

33% of its fleet to reduce its operating cost. Can a restructuring fix the fundamentals? That depends on the demand environment.

Both companies saw revenue return to 70–80% of the pre-pandemic level in the second quarter. But demand stagnation could come when the economy plunges into recession. If these companies go into a prolonged recession, with the kind of leverage they have on their balance sheet, they have a slim chance of surviving. So far, they have the liquidity for slightly above a year.

Applying learnings from Warren Buffet's case study in today's market

My point is, even if the above two companies survive, their stock has limited upside and higher downside. You have already made the first mistake of buying fundamentally weak stocks when you could have bought stocks of companies with strong growth potential.

Learn from Buffett's mistakes and do not hold such stocks. Exit and limit your loss. You can give your money a better chance at growth by reinvesting in better stocks. The bear market has reduced the prices of fundamentally strong stocks. Buying such stocks at a dip can help you recoup AC and Cineplex losses and skew your portfolio towards gains.

Two stocks that can recoup losses

If you purchased Air Canada (~$26) and Cineplex (~$13) in the first half of 2021, you are at a loss of 28% and 35%, respectively. By selling these stocks you can buy **Descartes Systems** (TSX:DSG)(NASDAQ:DSGX) stock at an 18% discount.

Descartes' stock has surged 23% since June 1. If you invested $1,000 in Air Canada stock ($21 price per share), your position was worth $820 on June 1. If you had booked a loss and invested this $820 in Descartes stock, your portfolio would now be valued at $1,008. But if you held AC stock, your $1,000 is now reduced to $721.

Descartes' supply chain solutions help companies comply with changing trade regulations. The growing complexity of trade and logistics help Descartes earn higher revenue per customer. It is a stock to buy on the dip as its products are sticky and have long-term demand, and the company has sustainable profit margins and little leverage.

Descartes stock has surged at a compounded annual growth rate of 20% in five years. It can help you recoup your Air Canada losses in 15 to 18 months and significantly grow your money in five years.

CATEGORY

1. Investing
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2. TSX:AC (Air Canada)
3. TSX:CGX (Cineplex Inc.)
4. TSX:DSG (The Descartes Systems Group Inc)

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