ASIA WEALTH VIRTUAL SUMMIT

THE BEST OF VALUE AND GROWTH: MAKE MONEY INVESTING

By Whitney Tilson

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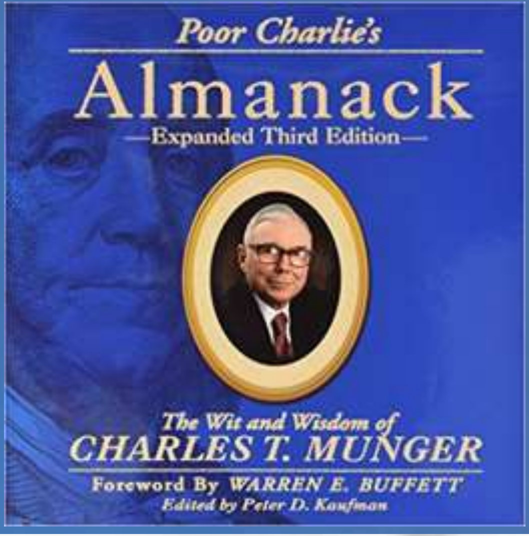
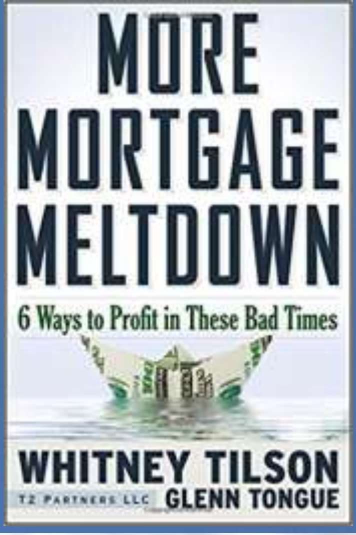
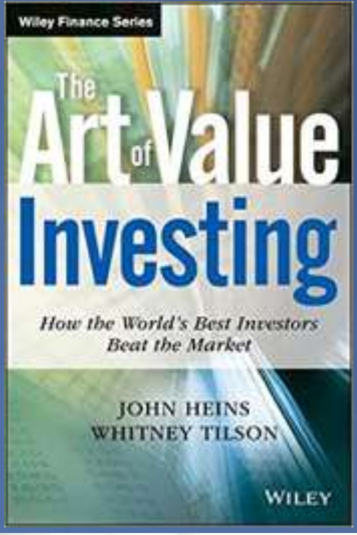
I WAS AN OLD-SCHOOL VALUE INVESTOR

- I pray in the church of Graham, Dodd, Buffett and Munger
- I've been to the last 21 Berkshire Hathaway annual meetings
- I've co-authored three books on value investing:







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I BOUGHT CHEAP STOCKS

- As a value investor, I mostly owned stocks that were trading at low multiples of sales, earnings and/or book value
- In most cases, the stocks were cheap because the companies were performing poorly
- I cared about businesses' quality and future growth prospects, but this was secondary to whether their stocks were cheap

THE FOUR MISTAKES OF VALUE INVESTORS

My focus on cheap stocks led me to frequently make four mistakes that are common among value investors:

1. Investing in low-quality businesses whose stocks were value traps because the businesses' fundamentals continued to decline
2. Failing to buy high-quality businesses whose stocks were fabulous long-term compounders
3. Selling the stocks of great companies way too soon because they'd risen and didn't appear as cheap
4. Failing to understand/appreciate powerful new technologies/trends

HOW A COMPANY PERFORMS OVER TIME IS MORE IMPORTANT THAN CURRENT VALUATION

- I estimate that 75% of what matters in terms of a stock's performance over time is how the company performs vs. only 25% the valuation at the time of purchase
- For my entire career, I had this backwards: I looked among cheap stocks and tried to find good businesses, when I should have looked among good businesses to find reasonably priced stocks

This was a terrible mistake that cost me and my investors dearly!

THE FOUR MISTAKES OF GROWTH INVESTORS

So the message is: "Just buy the stocks of great growth companies irrespective of valuation"? Not so fast…

Growth investors frequently make four mistakes:

1. They overestimate future growth, forgetting the powerful force of reversion to the mean, driven by technology changes, new competitors, size acting as an anchor to growth, etc. Trees don't grow to the sky
2. They pay too high a price for a stock, such that even if the business performs well, the stock doesn't
3. They fall in love with great companies and fail to sell when they should
4. They get sucked into "story stocks"

I'M NOW A MAKE MONEY INVESTOR

- I now combine the best aspects of both value and growth investing to maximize my returns as a make money investor
- I want to teach you how to become one as well

LESSON #1: STOCKS TEND TO FOLLOW EARNINGS

SO FOCUS PRIMARILY ON BUSINESS QUALITY AND GROWTH, BUT BEWARE OF EXTREME VALUATIONS

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HIGH VALUATIONS HAVEN'T MATTERED FOR CERTAIN STOCKS

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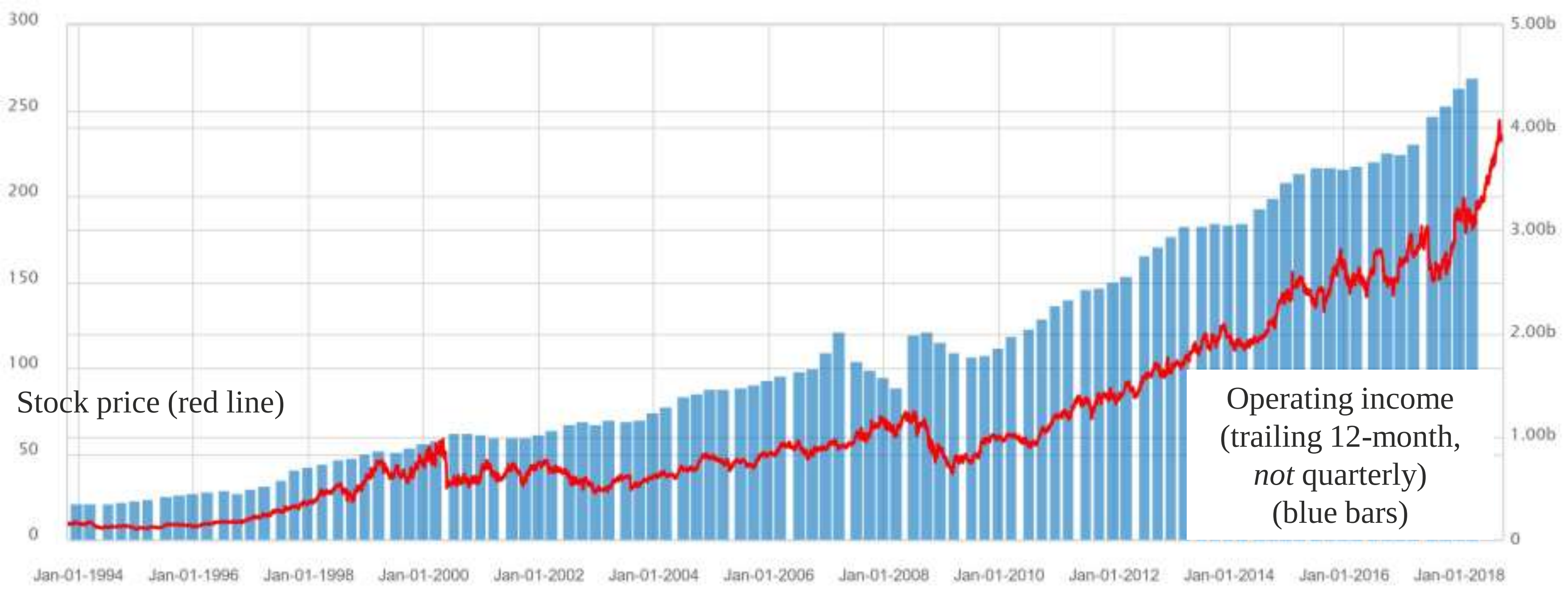
CASE STUDY: COSTCO

A 25-bagger since 1994, driven by extraordinary profit growth



 Source for all charts in this presentation: CapitalIQ

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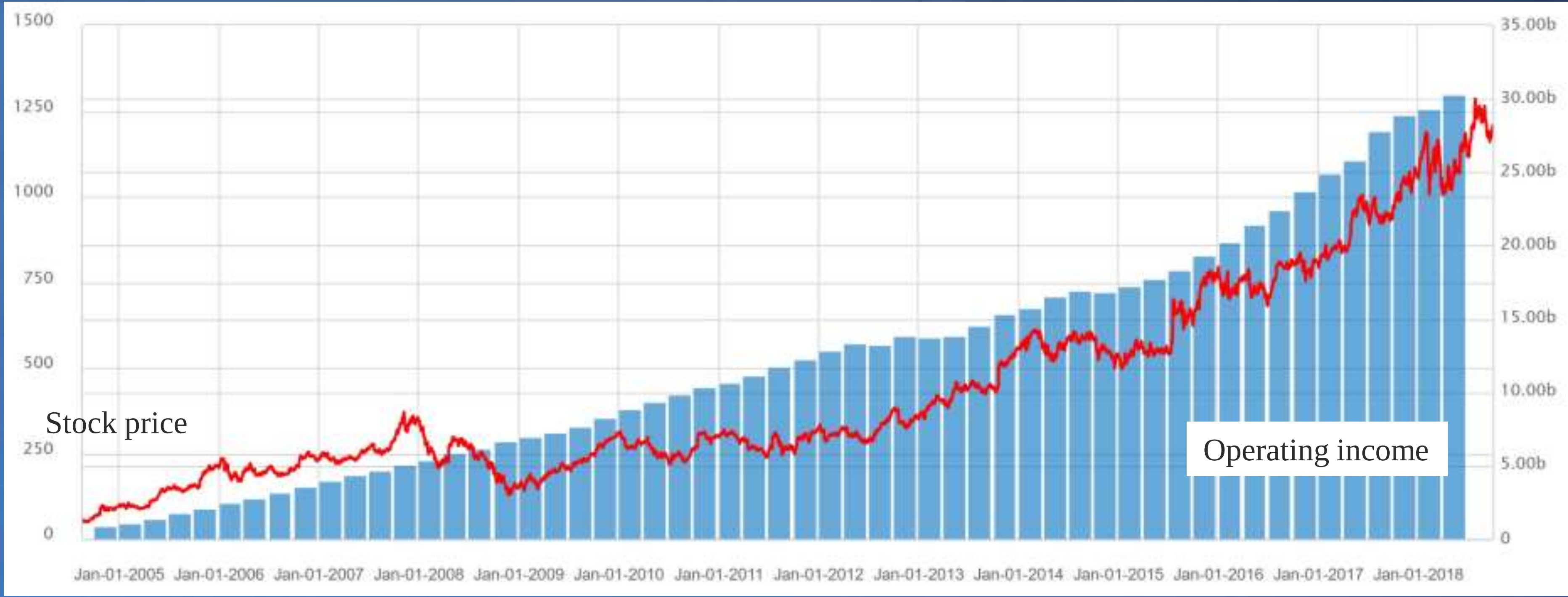
CASE STUDY: NIKE

A 57-bagger since 1994

CASE STUDY: GOOGLE (ALPHABET)

A 25-bagger since its IPO 14 years ago



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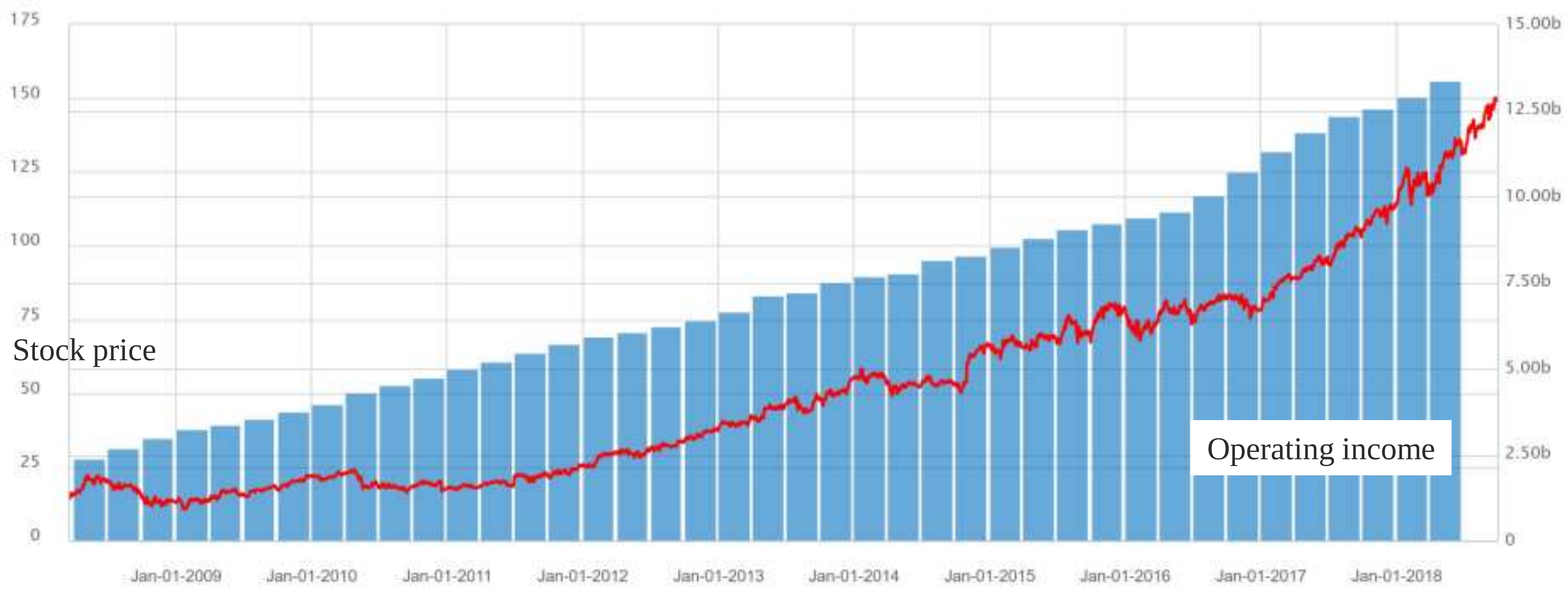
CASE STUDY: VISA

A 10-bagger since its IPO 12 years ago



HOWEVER, EXTREME VALUATIONS CAN OFFSET EVEN ROBUST GROWTH

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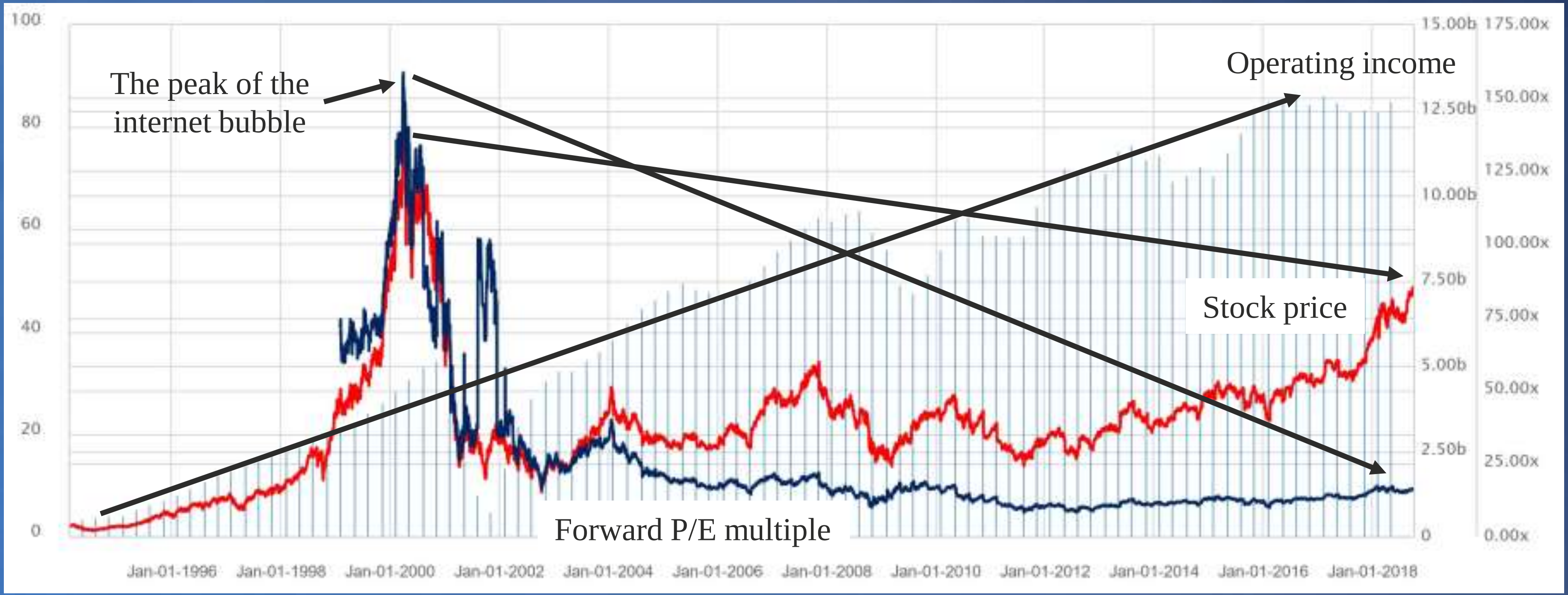
CASE STUDY: CISCO

After briefly becoming the most valuable company on the planet, the stock is still down nearly two decades later



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BEWARE OF VALUE TRAPS

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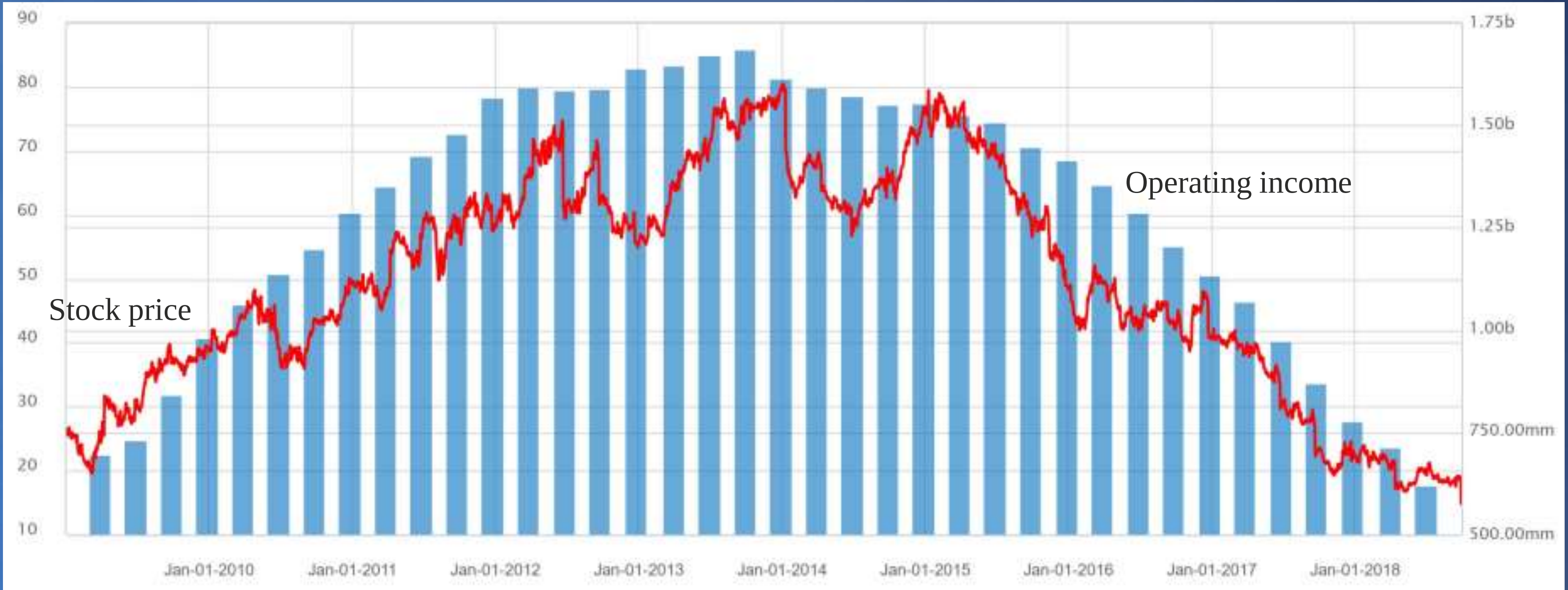
BE ESPECIALLY CAREFUL OF VALUE TRAPS:

COMPANIES WHOSE EARNINGS DECLINE AND DECLINE

- These value traps suck in value investors because they appear cheap all the way down
- Is it extremely difficult to make money on a stock, no matter how cheap it is, if the businesses’ fundamentals steadily decline

CASE STUDY: BED BATH & BEYOND

A round trip of both earnings and the stock over the past decade



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LESSON #2:
TRY TO IDENTIFY INFLECTION POINTS

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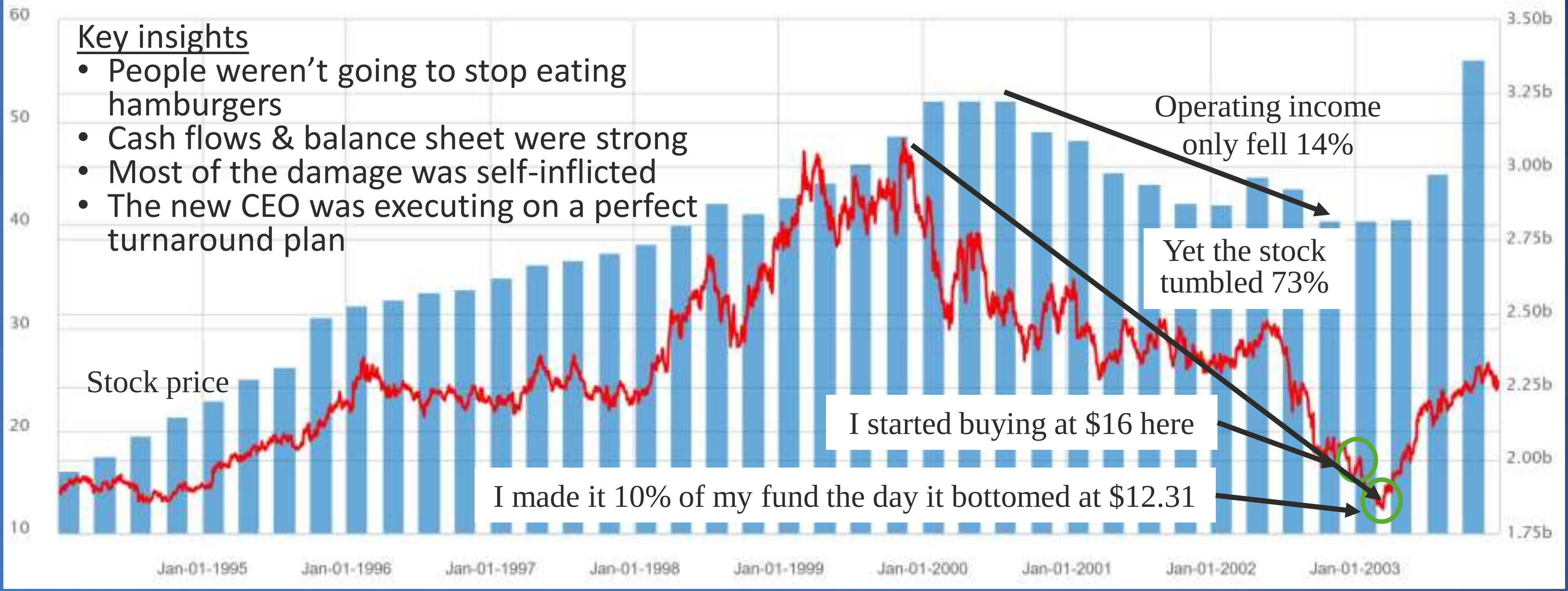
THE BEST OF BOTH WORLDS: COMBINE VALUE AND GROWTH APPROACHES

- If you correctly identify great companies that grow strongly and buy their stocks at anything but the most extreme valuation, you'll do well
- But if you *really* want to make a lot of money, buy the stocks of such companies when they're out of favor and the valuations are reasonable (if not downright cheap)
- If you catch an inflection point, there's a double tailwind for the stock: earnings grow and the multiple on those earnings expands as well
- <u>I am not talking about waiting for a market correction</u> – 90+% of the time, you should ignore the market
- I'm talking about *individual stock* corrections, which are typically driven by changes in sentiment toward the company or sector, or the company experiencing a short-term hiccup

CASE STUDY: MCDONALD'S

It's been a great growth stock in the past 25 years, up 8x

THERE WAS A GREAT BUYING OPPORTUNITY WHEN IT FELL 73% FROM 2000-2003



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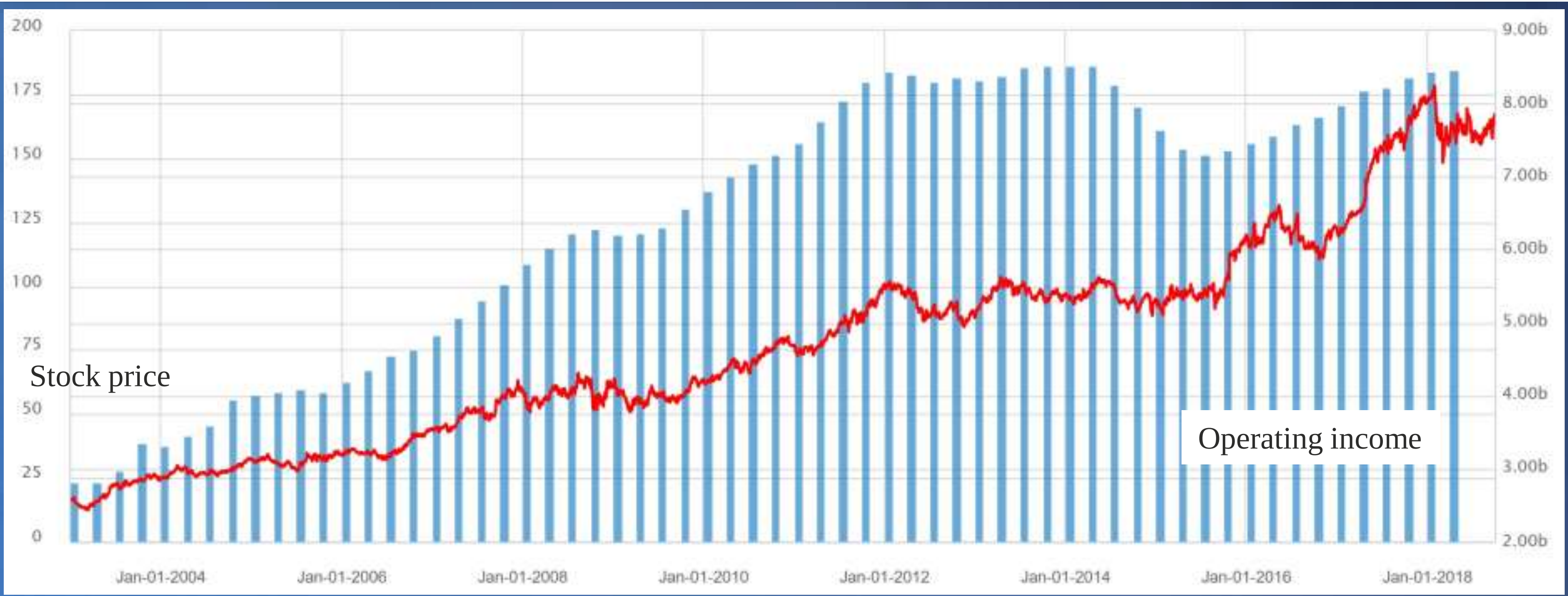
MCDONALD'S STOCK IS UP 13x SINCE 2003



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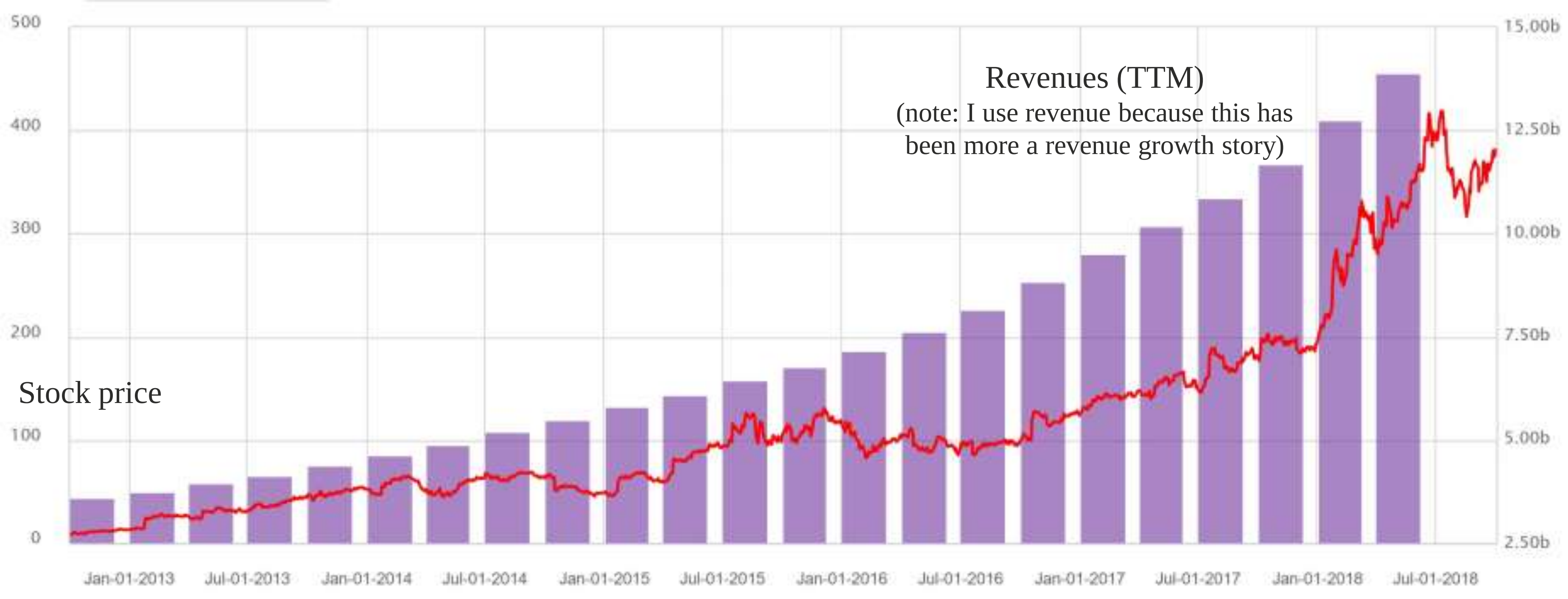
CASE STUDY: NETFLIX

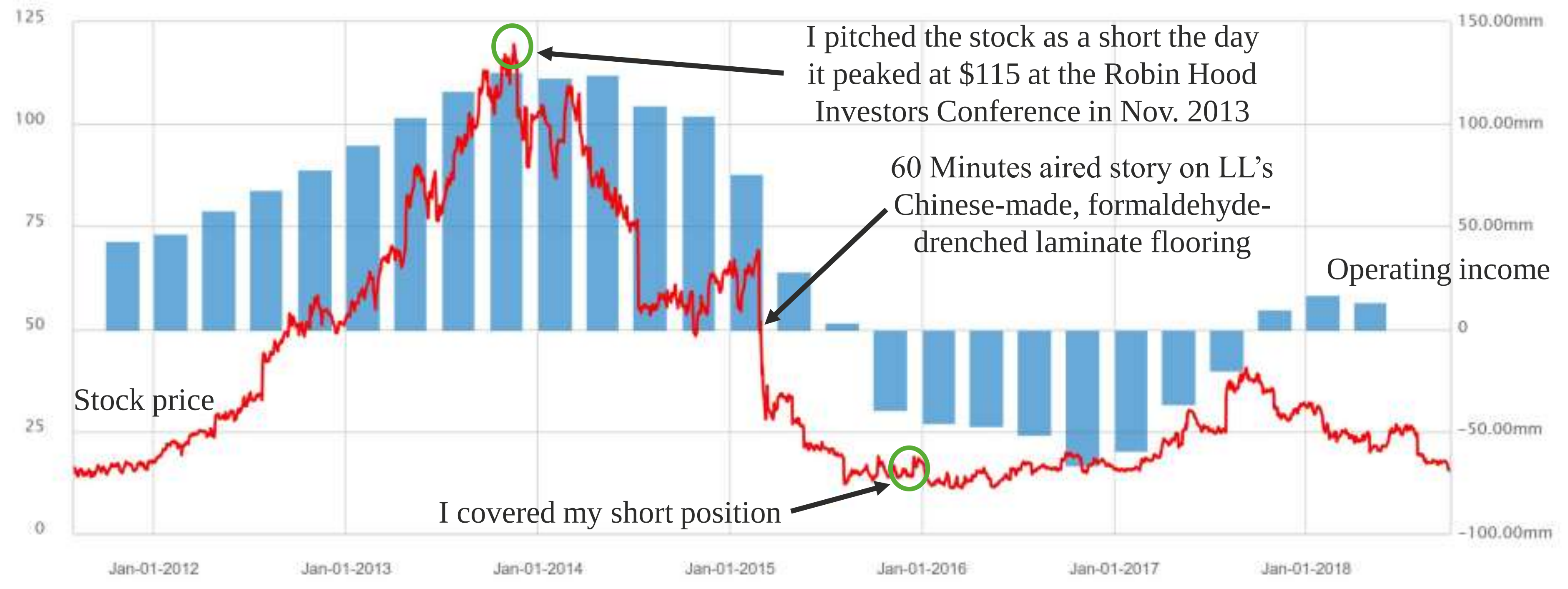
This was the situation when I pitched it in October 2012

NETFLIX IS UP *50x* IN THE PAST SIX YEARS

Driven by revenues up nearly 4x and P/S multiple up from 0.8x to 12.2x



CASE STUDY (SHORT): LUMBER LIQUIDATORS



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HOW TO IDENTIFY INFLECTION POINTS

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INFLECTION POINT = VARIANT PERCEPTION

- An inflection point in a stock occurs when the consensus view is that the company will continue to stagnate/decline, but instead it grows
- They are very difficult to identify – but you don't have to be exactly right
  - "It's better to be roughly right than precisely wrong"
- If you believe a company/stock is at an inflection point, then you have a variant perception – a belief that a company will perform much better (or worse, if you're shorting) than most investors expect
- But having a variant perception is easy – you must also **be right**!

HOW TO HAVE A CORRECT VARIANT PERCEPTION

- To have a correct variant perception, you must have a unique piece of data, insight or analysis
- This is much more likely to happen if you're in your sweet spot – a country, market or industry in which you have deep knowledge, experience and relationships
- This typically requires a lot of hard, focused work, often over years, even decades
- It's very easy to be the sucker at the poker table – avoid this at all costs!

LESSON #3: LET YOUR WINNERS RUN

ONCE YOU BUY A GREAT STOCK, HOLD ON

AS LONG AS THE STORY REMAINS INTACT

(IT'S OK TO TRIM TO MANAGE RISK/POSITION SIZE)

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CASE STUDY: BERKSHIRE HATHAWAY

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CASE STUDY: BROWN-FORMAN

Maker of Jack Daniels and other spirits

I SOLD FOUR OF THE GREATEST GROWTH STOCKS OF ALL TIME

- I not only owned but publicly pitched four of the greatest growth stocks of all time – Apple, Ross Stores, Home Depot and Netflix – and then sold them *far* too early

THE THREE MOST DANGEROUS WORDS IN INVESTING

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THE THREE MOST DANGEROUS WORDS IN INVESTING: I MISSED IT

- The four most dangerous words in investing are: “This time is different”
- The three most dangerous words are: “I missed it”
- The many case studies in this presentation highlight a critically important point: just because a stock has moved up – even doubled or more – doesn’t mean it’s expensive and shouldn’t be bought
- Value investors like to buy stocks trading at or near 52-week (if not multi-year) lows – it makes us feel like we’re getting a bargain
- I’ve lost count of how many times I’ve looked at the stock of a great company and failed to buy it because it’s moved higher and I said to yourself, “I missed it. Maybe I’ll buy it if it pulls back” – but it rarely does
- Lesson: ignore where a stock has been and focus exclusively on where it’s likely to go

YOU MUST SELL IF THE GROWTH STORY FALLS APART

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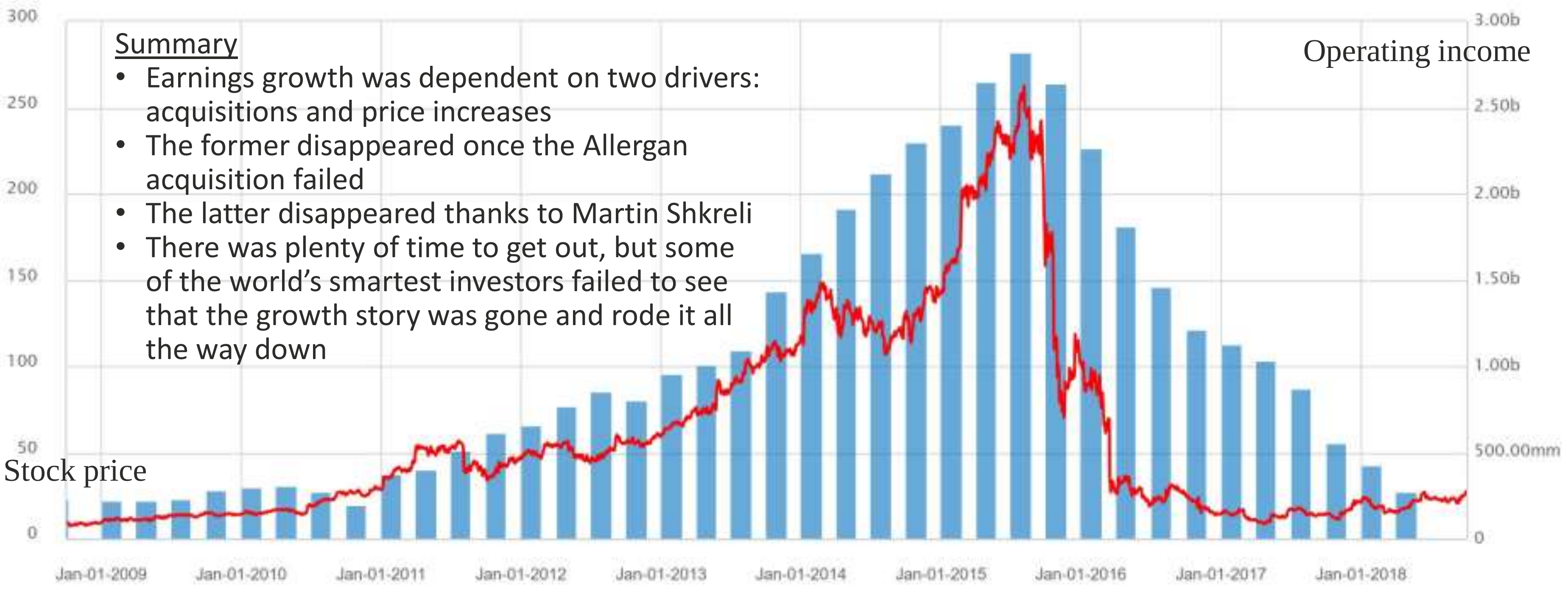
CASE STUDY: VALEANT

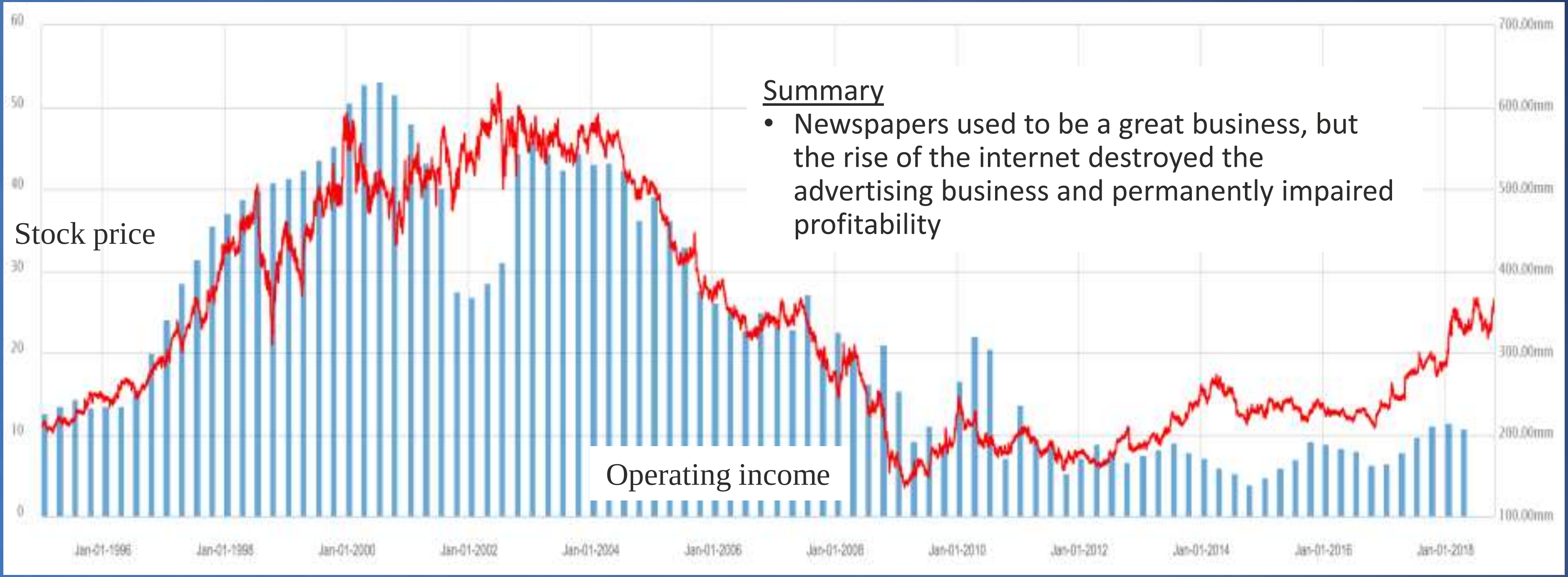
Earnings rose 11x, driving the stock up 20x – before it fell by 97%



 (Valeant has been renamed Bausch Health Companies – BHC)

CASE STUDY: NEW YORK TIMES

The stock is half its peak reached nearly two decades ago



<u>Summary</u>

- Newspapers used to be a great business, but the rise of the internet destroyed the advertising business and permanently impaired profitability

Q&A

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