# ART OF SELLING

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In a thriving bull market, our spotlights shine the brightest to scout the next big idea which can create fortunes. However, fortunes are created not only by buying the right stocks but are more driven by how much you ride the stocks when you are right and how soon you get out when you are wrong.

Take Stanley Druckenmiller, for instance, an investor I deeply admire. Over his remarkable three-decade tenure at Duquesne Capital Management, he achieved an astounding 30% annual return rate without ever experiencing a down year. His quote encapsulates the essence of successful investing:

***"It's not whether you're right or wrong that's important, but how much money you make when you're right and how much you lose when you're wrong."***

Re-emphasising, the same point made by Legendary Investor Peter Lynch:

**"Selling your winners and holding your losers is like cutting the flowers and watering the weeds"**

In my investing journey, I've realised that too much emphasis is on buying but too little is on riding the winners or selling the losers. This is a very costly oversight. Either we sell too early, leaving much of the profits on the table or it is too late where our profits may run into losses.

- **Let your winners run**

  In a bull market, we often feel tempted to sell off our winning stocks early. This is largely on impulse; we worry they're expensive or have risen too fast. But bull markets can surprise us by going even higher than we expect. Suzlon from being a CDR case post covid is up 10x in less than 15 months. RVNL, again a 10x, went from trading at PE 7x in 2021 is now trading at PE 32x FY24. Many investors bought PE 7x, but how many could hold it?

  So, if a stock is doing well and your thesis is intact, it's usually best to hang on to it. This is easier said than done but this is how fortunes are created. Bull markets climb a wall of worry and especially if a sector is in fancy, valuations tend to get overstretched. I am not suggesting to wait for the exact top for the perfect exit, but at the same time idea should be to ride major parts of the up-move.

  If you're concerned about valuations getting too high, you can use a trailing stop-loss based on recent highs, i.e. sell at 20% / 30% from recent highs. Range can be subjective, but having pre-determined level helps you lock in profits while still staying in the game and riding the up-move.

  Now that we have discussed how to ride you winners, its equally important to have a strategy to cut losses while they are still small.

- **Have a stop loss, even as investors**

  I've observed retail investors cling to stocks despite significant draw downs. There is a fear of booking initial loses which ends up becoming larger losses. Hope becomes an investment strategy for investors to recover their capital.

  There is ignorance that steep drawdowns require substantial recoveries just to break even. For instance, a 50% correction necessitates a 100% gain to return to the initial investment price, while an 80% drawdown demands a fivefold increase. This rarely happens, even if it does it comes at the cost of massive opportunity cost.

  In my approach to investing, I prioritize risk-reward dynamics. If I anticipate a 100% return on a stock, I'm willing to accept a 25% risk exposure, i.e.; a 4:1 risk-reward ratio. While individual risk tolerances may vary, having a pain threshold is very important.

  **Small loss is the best loss**, when a position hits the pain threshold i.e. stop loss, act swiftly, cut losses short, and protect your capital.

- **Track Fundamental Changes**

  It is extremely important to track and monitor fundamental changes in the companies or sectors where you've put your money. Investing requires dedicated attention and focus. There's a saying: ***"Investing can never be a hobby because if you treat it like one, it'll pay like one – and hobbies only cost money."***

  To start with, if there is a material change in fundamental thesis itself, position should be squared, no questions asked. Waiting for a better price when the thesis has changed is nothing but gambling. E.g: Apparent corporate governance issue, event led significant earnings headwinds, regulatory changes, technology obsolesc etc.

  Beyond these material changes, here are some subtle fundamental triggers which can act as an early warning signal before both price and fundamentals actually deteriorates.

**Peak Margin + Peak Valuation Multiples**
e.g: CDMO pack in Q4FY21/Q1FY22. Most down 30-50% of ATH.

**Industry wide overcapacity**
e.g: Paint Industry, Asian Paints gave 0 returns over last 2.5 years.

**Insider Selling**
e.g: HIL Ltd saw directors selling at INR 6400, CMP INR2850.

**Regulatory Changes**
e.g: Delta Corp & GST notification. PayTM & RBI

**Global Headwinds**
e.g: China & Chemicals. USFDA & Generics.

**One-Offs vs Sustainable Business**
e.g Vaccine contracts in CDMOs. US Generic shortages.

**Promoter Pledge**
e.g Zee, Indiabulls Group, Yes Bank etc

Can use these triggers as re-thinking points to assess the implications on the broader thesis and don't recommend selling right away.

- **Have a pulse of consensus sentiments**

Consensus especially on social media act as fantastic contra indicators. Think back to the abundance of memes circulating about Zomato and ITC on platforms like Twitter. Despite the scepticism, both stocks turned out to be top performers. On the flip side, recall the Twitter frenzy surrounding CDMO stocks post covid. Many of these stocks plummeted by 50-60% from their highs. Warren Buffet has it right again when he says **"be fearful when others are greedy and to be greedy only when others are fearful"**. Some of the sentiment indicators are as follows:

**Discussions / Analysis across social media**

**Sell Side Consensus build-up**

**Over-ownership across retail and Institutions**

**Frequent Media/Investor interactions by Management**

**QIPs/PE Exits/Fund Raise**

**Stock Splits/Bonus**

Again, these are broader indicators and don't recommend selling right away. Use these as re-thinking points.

- **Be Dispassionate while dealing in stocks**

Stocks have to be bought and sold dispassionately, investors do it on the basis of fundamentals and chartist do it on technical. Retail Investors tend to get too attached to their stocks which can seriously cloud their judgments. Some of the behavioural biases are as follows:

**Loss aversion**: There is somehow a belief that loss is not real unless it is booked. Hence Investors hold on to loss making position in the hope to recover capital.

**Anchoring**: Buy price at times is a strong anchor to decision making vs changed fundamentals or changed market condition.

**Herd Effect**: This is common across Investing WhatsApp groups where buying happens in tandem without much analysis.

**Recency Bias**: More weight is given to recent announcements while ignoring the history and long term fundamentals. Clearly apparent from retail participation in penny stocks.

Of all the above mentioned rules/triggers, behavioural biases are the most difficult to manage. Easier said than done, but we can always try!

These are few principles that have worked well for me, but each investor's situation is unique. Hence would recommend that these principles be used in conjunction to the fundamental / technical analysis tools, individual risk appetite and in alignment to the prevailing market conditions.

Disclaimer: Please note that stocks discussed above is purely for educational purpose.