

# When To Sell Webinar

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## When to Sell

### The Emotional Problem

*The field of behavioral finance has demonstrated that the pain we derive from market losses impacts us twice as much as the pleasure we feel from market gains.*

Deciding when to sell I find to be the hardest thing to do as an investor. Why?

It is a much more emotional decision. You have already made the decision to commit to this stock and have formed some sort of bond with the stock. So selling it is a bit like departing with a loyal (or perhaps disloyal) friend.

### Your Stock is Making Money

If it has treated you well, you feel disloyal. And you feel if it has done well in the past, why can't it continue to do well in the future? After all it has momentum on its side, which is Newton's first law of motion and a well know and real effect in financial markets.

Also you will faces two other issues:

- 1) Generating a guaranteed tax bill
- 2) Finding a better replacement (which means work on your part)

### Your Stock is Losing Money

If your stock has treated you poorly, you may secretly feel that it is only a question of time before the market recognizes its virtues and you should wait it out.

If on the other hand, things have really changed for the worse and you clearly see that or if you missed a key fact in your investment analysis that matters (like maybe the company carries too much debt and we are heading for rising rates), you know in your heart it is time to go. But you feel loss. However selling will be the acknowledgement of a big mistake, and is also the abandonment of hope. It makes you feel stupid. Or why didn't I just set fire to my money? And hope beats stupidity on the emotional scale.

And, of course there is the other big fear. After suffering with the stock for what seems ages, you finally sell and then stock rallies right after. There is no worse feeling in investing. You are left behind while everyone else has a good time and feel even stupider. I have been there, it doesn't feel great.

So the emotional component of ownership makes selling a much tougher decision than buying. A side example, is when people sell their houses, they invariably think their house is worth considerably more than the realtors, who try to talk the client down to a realistic selling price. People tend to overestimate the market value of their home. Unfortunately the same holds true for stock ownership.

## The Practical Solution

The best place to start is to ask yourself the following question and answer it honestly;

### **If I didn't own the stock, would I buy it today at this price?**

If the answer is no, you should probably sell. There are exceptions to this. For example, if you have a huge gain that will generate a big tax bill, and stock is not great in your estimation, but is "Okay", you may want to hang on.

Note if you are really unsure as to the answer to this question, you can always sell just part your position to hedge your own judgement a bit.

## Deciding Whether To Sell – Factors to Consider

- Business Fundamentals
- Valuation
- Health of the Market
- Price Performance
- Technicals
- Management Issues
- Stock in Play with Hedge Funds

## Business Fundamentals

- Is there a change in business outlook for the worse?
  - Declining sales – IBM and Qualcomm
  - Key product pricing/competitive pressure Gilead (GILD)
    - Via Merck (MRK) and the Massachusetts Attorney General
  - Disappointing outlook relative to expectations - Alliance Data (ADS)
- Is there a drumbeat of negative headline news that underlies real fears?
  - Apple iPhone sales
  - China growth and the effect on commodity stocks
  - Oversupply of energy and plummeting energy prices
- Are analyst estimates decreasing?
  - Polaris (PII)
- Wrong business set up for future business environment?
  - A company with a lot of debt in a rising interest environment (URI, R)
  - A company that sells capital equipment where capital expenditures are drying up due to slowing growth (CAT)
- Markets that are thought to be at a cyclical peak and therefore peak earnings
  - Autos - the market is pricing the expectation of plummeting sales
- Key competitor(s) are getting stronger
  - Twitter – Facebook and Google are tough and getting tougher competitors for advertising dollars
- Industry concerns
  - Hilary Clinton and Biotech
- Major lawsuit
  - Trinity Industries sued by the Federal Government and the State of Virginia

## Valuation

- Extended P/E
- Declining E

## Health of the Market

- Bad Market
- Bad Sector
- Bad Industry
- Sector industry rotation – area is getting more “out of favor” – negative momentum

## Price Performance

- Chronic Underperformance

## Technicals

- Extended price
- Moving Average crossovers
- Downtrend
- Double top
- Lower highs and lower lows

## Management Issues

- High turnover of top executives (Yahoo)
- Abrupt changes (Twitter)
- Changing auditors
- Greedy management (too many options) and then selling lots and lots of stock (Sketchers)

## Stock in Play with Hedge Funds

- Herbalife (HLF) and Valeant Pharmaceuticals (VRX)
- Unless you know something very few people know – get out/avoid

## Summary

Examine all the selling factors listed before, **honestly and with an open mind**. Then after looking at all this stuff. Ask yourself the critical question:

***If I didn't own the stock, would I buy it at this price today?***

If the answer is anything but yes, then it is time to start re-thinking your ownership position.