Inside the Minds of Guru Investors

The secrets of how eight guru investors made a fortune from the stock market.

Stockopedia

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Ben Hobson

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What I learnt from talking to successful investors

As Strategies Editor at the stock market research platform Stockopedia, I'm in a fortunate position. For several years I've had the advantage of spending most of my time reading and writing about what works in the stock market. Most individual investors simply don't have the time to do that.

On my investing journey, I've read a range of academic studies, professional research and investment books. Armed with that insight, it's my job to show individual investors how to turn abstract and unfamiliar ideas into practical, profitable reality. In other words, to build sensible, rules-based investing frameworks that they can live with in good times and bad.

Anyone who has spent time researching the stock market knows that there is a huge amount of information and commentary out there. But for me, the most inspirational sources of knowledge have always been successful investors themselves. There isn't much that compares with the reflections of investors who have fought the market and won.

In seventeen years as a finance journalist I've interviewed hundreds of company owners and managers about what makes a successful business. But to paraphrase Warren Buffett, himself one of the world's most successful investors, great businesses don't always make great investments. For that reason, the suggestions and guidance of successful investors on how to make great investments are incredibly valuable.

In my role, I'm fortunate to be able to access the kinds of guru investors in this book. These interviews have been published as part of the Stockopedia service for our membership. In the case of each investor, they were willing to share their expertise with me, knowing that I would in turn share it with a much, much wider audience.

But this is only the start. More interviews in more countries are on the way. You can keep up to date with those forthcoming interviews by following me here: https://www.stockopedia.com and here: https://twitter.com/BenJamesHobson.

I hope you find the interviews as useful and entertaining as I do.

Ben Hobson
December 2017

Inside the minds of great investors

This book is a guide to how some of the best investors succeed in the stock market, and what you can learn from them.

Over the course of a year I interviewed eight well-known investors who were either trading on their own account or managing large investment funds. Among them was a peer in the House of Lords, an ex-journalist-turned-DIY investing hero, a fund manager who set out to mimic Warren Buffett and made a mint, and a one-time U.S. Investing Champion.

While their styles and strategies vary enormously, what they share in common is that they've all profited handsomely from investing over time. By sharing the highs and lows of their journeys, they offer some fascinating insights for anyone with aspirations of building wealth from the stock market.

One of the overarching themes of this book is how investment strategies based on simple principles are often the most effective. With a sound strategy at hand, it's much easier to maintain the kind of discipline needed to stick with it. That's arguably what really sets the most successful investors apart.

Learning from the best

There are two types of investor in this book; those who manage their own money and those who manage other people's money.

The individual investors include Lord (John) Lee of Trafford, Robbie Burns and Mark Minervini. While they have very different backgrounds, they've all achieved considerable wealth and long-term outperformance. To varying degrees they've also become brands in themselves and attracted a wide following of investors who hold them in high regard.

The professional fund managers include Mark Slater, Gervais Williams, Giles Hargreave, Nick Kirrage and Keith Ashworth-Lord. Again, their strategies, styles and investment philosophies vary widely. But in an industry that is obsessed with performance, they've each built solid and highly respected track records.

What's in this for you?

Behavioural psychologists have found that humans are often ill-suited to investing. Emotional flaws, biases and cognitive errors can hamper the sorts of cold-hearted decisions needed to win in the stock market. Yet just knowing about these pitfalls can put you on the road to overcoming them.

So reading about the experiences, the strategies, the hopes and fears of successful investors is both entertaining and illuminating. All of the investors in this book were humble about their own failures. In fact, their long-term success seemed to liberate them to explain, and often laugh about things that had gone (often badly) wrong. There was a universal acceptance that there was nothing to fear from investments that turn sour - rather it's how one deals with and moves on from a bad situation that is crucial.

These interviews offer a snapshot of how some of the best investors operate. They illustrate how to build and refine an investment strategy and then apply it consistently. And they show how long-term outperformance can be achieved with commitment, humility and good humour.

Strategy screens

At the end of the interviews is a summary of each investor's strategic approach. There's also a web link to a strategy screen on Stockopedia.com that broadly reflects each investor's preferred style. These strategy screens are not endorsed by the investors themselves and are only a guide to each approach. Screening is generally used as a first step to finding companies that meet the basic criteria of an investment style. It's often followed by more extensive research.

Robbie Burns - How to profit like the Naked Trader

Robbie Burns is one of the most popular figures in the UK investment scene. In many ways he's both a finance rebel and investing hero, and to his legion of followers he's best known as the Naked Trader.

The Naked Trader was the title of Burns' 2007 guide to 'how anyone can make money trading shares'. Several updates followed, as well as a new book called *Trade Like a Shark*. Over the years his loyal readers have followed him through booms, crashes, bubbles, successes and failures.

His popularity stems from no-nonsense, down-to-earth prose that literally laughs in the face of complicated investment speak. By keeping things simple, wearing mistakes on his sleeve and encouraging individual investment he's built a successful brand around himself.

In essence, his book is about taking a checklist approach to trading. He suggests looking for profitable, growing companies that aren't debt laden. Dividends are important (mainly to cover trading costs), the shares have to be reasonably priced and they need positive price momentum behind them.

Burns also takes a ruthless view on losing positions, cutting them early, often with a stop loss. It's a strategy that makes a great deal of sense - blending growth, quality, value and momentum - but it needs discipline too.

We discussed all this over lunch at a lively Michelin-starred Italian restaurant on the banks for the Thames, just around the corner from his home in London…

Robbie, I suspect that behind your relaxed persona and easy going attitude is a ruthlessly disciplined investor. Would that be right?

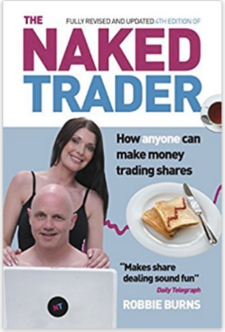
Well, I think I treat the whole thing as a business. If things are getting out of control I just cut them. All my stuff is so simple I think people are quite surprised. They expect charts and lines, but it's nothing like that.

I'm a weird mix. I'm happy-go-lucky in some departments but when it comes to trading, the main thing is that I treat it like a business. To win at trading you've got to be cold, calculating and really hard-hearted. Perhaps you even need to be a bit of a sh** in the trading element of it. Because in the end if you're winning, somebody else is losing unfortunately. But you've done the homework and they haven't, and that's the way of the world. So I think you have to be quite ruthless, and if you're nice you're not going to cut it. In the United States they call it sharks and fishes - the sharks prey off the fishes.

You started trading full time just as the tech bubble was taking off in the late 1990s. What lessons did you learn in those early years?

I learnt a lot between 2000 and 2006, when I wrote the first book. I learnt from mistakes, so every time I made a mistake I asked myself: *"why did I fu** this up and how can I stop it happening again?"* It took four or five years of learning the ropes.

Coffee Republic was my worst mistake. I initially bought it because I liked the coffee. I remember quite clearly buying them at 28p, and then at 22p, more at 13p and then at 8p. But it was one of the best things ever because I remember feeling so happy when I finally cut it at 3p. I felt like I'd been released.



I suppose where I've been lucky is that I've only ever used my ISA allowances and I'm guessing I've put about about £40,000 into spread betting accounts. Even now, £15,000 a year is the only money I add. I try to leave the ISAs to run if I can, I wouldn't imagine taking money out of them for a while. The spread bets are like lucky money, I don't consider that I've got it until I actually bank it.

Your strategy often picks up smaller companies, so with a growing pot of capital I guess you've had to be very conscious of the ability to get in and out of those shares when you're trading sizeable sums?

I think it is harder now for me than it was. I guess if you've got a pot of £100,000 it is quite easy to be nimble and move in and out of stuff. But when you've got more than a million pounds in an ISA - I've got something like 65 positions - that makes things a bit harder.

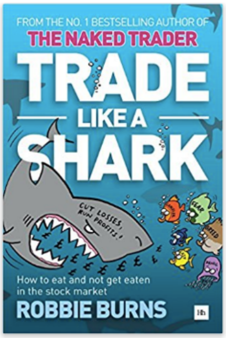
I might have £100,000 of Paysafe and because it's FTSE 250 I won't have any trouble getting in and out of that. But with something like Next Fifteen Communications, I had about £40,000 and it did really well so I cut half of it. With £20,000 it should be quite easy to get out if I need to.

At one of my seminars a guy said that he'd bought £170,000 of Coms, which is a tiny penny share. He'd bought them at 10p, and that was his whole pot. I asked him if he realised that if he tried to sell the whole lot the market makers might only give him 1p for them. People don't realise that the price is there, but only up to a certain amount of money. I know why he did it, he thought Coms would go to 50p and he'd be a millionaire. That was in his mind when he bought them. But at 7p you've lost £35,000. What are you going to do about it? Probably nothing. Then you read the bulletin boards where people are trying to encourage you to keep them or buy more.

Now you're in a terrible place. I said that if I was him I'd be selling as much of them as possible every day until I was down to around £10,000 worth. That's what he should have had in the first place. But I knew that he wouldn't do it and the shares are about 1p now. I think that happens to a lot of people.

There are a lot of psychological forces at work when it comes to buying and selling shares. How have you refined your process to deal with that?

What a lot of people think when they buy a share is that they've got a massive winner at some point. In my book *Trade Like a Shark*, I talk about confirmation bias, which to me is one of the most interesting things in psychology. What I say is that when you approach a share, approach it negatively. What are the bad points? What could go wrong with it and why could it be down 100% in six months? What is the risk involved with the share?



That's where my net debt rule came in - I wouldn't buy anything which had three times debt to profits. There was a share called Aero Inventory that I'd looked at, and it seemed fantastic. The profit was quite nice at about £33 million, but multiply that by three and net debt shouldn't have been more than £100 million, but it was £450 million. I looked like an idiot for six weeks or so because the shares did go up. But they were suspended a few months later and it went bust.

So first you've got to say 'what's the risk?', not 'I'm going to make a million out of this'. The moment you do that you'll be looking for all the reasons that confirm your decision to buy the share.

What else drives the decision for you to buy a share and what's your process for building a position?

I look at my portfolio as a room with a massive door. Any share has to really, really bang on that door to get in. It has really got to have everything going for it.

Before I make the decision to buy, bearing in mind I'm always trying to put myself off, I look at the supply and demand - what's Level 2 looking like? There is no point buying something where there's no demand because it will just carrying on going down. That has saved me numerous times from getting into stinkers. If I see lots of sellers out there I wait. It's quite simple because if you buy it on a strong Level 2, it should then rise. If it doesn't, and it starts to go down, I have what I call my 'get out quick', and I'm just out.

Stop losses for me have changed. A stop loss to me is an emergency exit, way down the line, just in case something terrible happens. But on a new trade I'm much more likely to get out really fast. Then I'm only going to try two more times, a bit lower down. If I've tried three times with a share and it's still not working, I just stop.

On the subject of stop losses, say one of your positions is up 50%. Would you still use a stop loss or is it no longer important?

No, I just top-slice as they go up usually, but I would recommend people to use a trailing stop well away from current price.

So your approach with new positions is to start small and then build up over time?

Exactly. I'll start small with something and as it goes up I get more confident and average up. I would never average down now. Instead of averaging down it's best to just get out. Otherwise, the longer you hold onto it the more you're likely to hold it because you think it's not worth selling. Psychologically it's damaging. This is why airline pilots are such good traders, because they learn confirmation bias as part of their training.

Confirmation bias is a big thing, it's very easy to find other people on the internet that agree with you. This is why bulletin boards are very dangerous. It's what I mean when I say that I treat this like a business. I don’t look at bulletin boards, I look at cold hard figures, I look at what’s going on and I don’t care what anybody else thinks.

There is so much out there that you can look at that can confuse you. I’ve narrowed it down to a very small number of things. If it hasn’t got everything right then I at least keep an eye on what’s going wrong with it. I don’t think there’s anything wrong with taking the odd bit of high risk. Sometimes it pays off but you’ve got to do it to a small degree, and I just assume that I’ll lose the money. I think that probably takes a bit of my gambling instinct out of it, which I think everyone has.

What would be your definition of an ideal investment outcome?

Probably one that keeps going up slowly over time. One with dividends and no big worries and which might eventually get taken over. That was the case with GB Group, which went from 20p to 250p over seven years.

You’re obviously keen on spread betting, but do you think individual traders use it wisely?

I just use spread betting to supplement my ISAs and I don’t use that much leverage. For example, I’ve had a spread bet in Dignity for two years. It costs me 50p every night to keep it open, but that’s fine. After all, death isn’t going to go out of fashion, so who knows it might be open for the next five years. But you can keep longer-term things open in spread betting. It’s a great facility, and of course you can go short, which is great for you to be able to cover yourself.

The problem of course is that it can be addictive, which can lead you to use the leverage and overtrade. You have to use it very carefully. But you can have guaranteed stops, which is fantastic. Let’s say you were shorting something that could be bid for, with spread betting you can know your potential loss for definite. I would only do that where I felt there was just a chance something could be bid for where I was short. Say you were short Wm Morrison but you thought, ‘hang on, what happens if Tesco makes a surprise bid for it?' That's the way I look at it - I'm looking at the risk every time, trying to judge it.

What do you think is wrong with most of the trading 'advice' that investors are faced with?

Most start talking jargon very quickly and complicate things. The more I did this the more I realised I needed to un-complicate everything. Then I realised you could do that with everything in life. People go to these technical analysis seminars and they just get bulldozed. I say to them, 'do you think your trainer was making any money, really?' I wouldn't dream of doing a seminar unless I could show them what I'd made in my accounts.

People are naturally cynical and I can understand that. I don't look at bulletin boards or Twitter but I'm sure people say 'ah, Robbie Burns makes it up', or 'he said he does this but he doesn't'. I just think, 'if only you could come and see'. But I can understand the cynicism.

One of the final points you make in your book is that it's very easy to over-analyse a share. Do you think there's a risk that you can talk yourself out of investing in anything?

Yes. But the thing is that if you buy it, you can get out if it starts to go down. So I can say to myself, 'well I'm not 100% sure but Level 2 looks strong so I'll give it a try'. If it doesn't work out then I'm out. So although I think that everything has to be in my favour, if I'm not sure about a negative then I will probably give it a go if Level 2 looks good.

But having said that I don't trade very often. If in doubt, do nowt, as they say. If you find yourself over-screening and pushing every button in sight then there is probably something going wrong. You're panicking, you're fearful or you're greedy. You should stop yourself from pressing buttons that much and think before you click.

I think there's also a risk of comfort trading. If you're feeling bored you might trade without really thinking. Right now, when markets are going down there is no real stampede to buy. If you're reasonably covered with a short there isn't much to worry about selling either.

I don't forecast the market, obviously I haven't got the foggiest idea where the market will go. Some people say sell everything while others say it's fine. But generally it's the new trades that you've got to worry about. With a new trade you have to look after it, and if it starts to go down get out of it. But once I'm up by more than 20% I have a look from time to time. I've got many good trades still there from years ago like Avon Rubber and GB Group, which have multi-bagged.

You use short ETFs - including the SUK2 FTSE 100 2x Super Short ETF - to cover positions that you don't want to sell. What are the signs you look for when getting in and out of those positions.

Yes, I have used ETFs to short the market in an ISA. They are great because if the market goes back up you sell and take a small loss. They are a brilliant insurance policy, and incidentally, you can get 3x and 5x short ETFs now.

Where do you think individual investors generally make mistakes?

People want to make money really fast. I think that if you try to chase money it will run away from you. You just need to bring it in slowly. But no-one is interested in that these days because they want to make their money now, and that's why they lose.

Look at the markets. When fear is the utmost emotion, it's a great time to buy. When everyone is feeling miserable, if you look at fundamentals, there are a lot of bargains out there. What's amazing is how everyone is scared and then five minutes later everything is going up again - the market turns in an instant.

Robbie, thank you very much for your time.

Build a strategy like Robbie Burns

Robbie Burns typically looks for good quality, growing companies with shares that have positive momentum but are still attractively valued.

Find out now which shares pass the rules of our Robbie Burns strategy screen: http://stk.pe/nakedtrader

Mark Slater - A masterclass in growth investing

Mark Slater is one of the most successful and widely followed growth fund managers in the UK. Since setting up Slater Investments in 1994, he and his team have delivered an exceptionally strong performance record across their growth and income funds.

A great deal of that success is down to an unshakable focus on buying good quality growth shares at reasonable prices. But for Slater, it's also about understanding the nature and likely longevity of that growth. That means recognising the traits of different growth stocks and dealing with the psychological battles of buying, holding and selling these types of companies.

Back in 1992, Slater worked with his father, the late Jim Slater, on the now legendary investment guide called *The Zulu Principle*. It became, and remains, one of the most influential UK-focused investment books around. The strategy rules in the book have a common sense, yet distinctly buccaneering feel to them. Arguably, that's precisely what's needed in the search for the great growth stocks of tomorrow.

Mark, what's your assessment of how markets, and growth stocks in particular, have performed in recent years?

The period coming out of the crisis has been very, very strong. A lot of companies that we've done well with were really bombed out back in 2008 and 2009. We were starting from a very, very low base so I think from 2009 onwards one would have expected to do pretty well.

Since the crisis our approach has been to assume that life would be tough. Having said that, zero rates have helped and certainly it could have been an awful lot worse. But the key thing is that coming out of the crisis valuations were so low that it didn't surprise me that a lot of companies went up multiples.

As a fund manager focused on growth and value, how do you adapt to different market conditions?

In relation to market action we find that things don't tend to happen in one day, it's a rolling process. You can be waiting and waiting and then all of a sudden a couple of companies you have been very keen to buy over a long period suddenly become attractive.

A good example of that was back in October 2014 when there was an eight percent fall in the market in a short period. In the space of two or three weeks some companies fell 20-30 percent and in one or two cases they fell by that much in a day. Within a couple of days of each other, we bought a holding in Liontrust Asset Management, which is a very well run business, very cheaply. We also bought a big holding in dotDigital. That was a company we'd always found just a little bit too expensive. They'd already drifted a bit and then fell 20-25 percent in a day and we were able to buy a good slug of shares, four or five percent of the company, in a day - bang! We'd been looking at it for 18 months before that but it had always been out of reach.

Do you think it's possible to time the market when it comes to making investment decisions?

We don't look to invest according to a market view, that's just too difficult. The number of people who are good at getting markets right you can count on the fingers of one hand. And I am not sure they are consistently good. The vast majority of people try to time the market even though they probably know they are not very good at it. They still try and do it even though it doesn't make any sense.

Do market conditions ever lead you into compromising on value and paying a bit more for quality?

I think in general your entry price is an important determinant of the investment outcome. But in the case of equities, and particularly in the case of quality, growing businesses, I think quality is more important than price. There are two reasons for that. The main reason is that a quality business can compound your money over a long period of time. Whereas a low quality business simply can't do that. The second thing is that your risk is actually lower in many ways with quality businesses.

I think as a generality it makes sense to pay up for quality. The hard thing of course is determining what is quality and what isn't - that is the hard bit. It's not a formulaic thing, I don't think one can say: 'okay, I'll pay a PEG of 1.5 rather than 1 or I'll pay multiples of 25 rather than 20 going forward'. It doesn't work that way because you can end up paying 25 times for rubbish and then you have a problem. There is something comforting about owning really good quality businesses because when they report, you are not worried about them. You know the results are going to be good, they are doing their thing, the management are good and they focus on the right things. The problem is they are rare and they are quite difficult to identify.

Has that process of finding growth stocks got easier over time, or harder?

Certainly, it's difficult to invest in growth businesses in an environment where growth is more rare than it used to be. The ability to grow reasonably consistently with some sort of track record is harder to find now than it was in the late 1990s.

Our universe was probably two-and-a-half times bigger in the late 1990s than it is now, which is quite a big change. In the late '90s it was an extremely benign environment where even pretty mediocre businesses were able to grow quite quickly. Whereas now, we very much take the view that life is tough for the average business, and as a result you don't really want to be in the average business.

It's pretty hard to find companies that can grow reliably where you can ask the sort of Warren Buffett question: 'is this business going to be significantly bigger in three years time, five years time or 10 years time?' For anyone who is interested in growth, that's the question you are asking. You are not going to ask whether it is going to grow 10 percent this year and 15 percent next year, you don't know because it's not that precise. It's much more about whether it's going to grow at a decent rate year after year after year with the occasional exception.

Growth can have a habit of accelerating and slowing down, so how do you approach what, as you say, is a hard thing to define?

What we tend to find is that we have a number of companies which are those really high quality ones where you are very, very comfortable. You really feel they are just going to do their thing for a very long time and they can compound your money many, many times. They are wonderful but they are very rare.

We are often debating one or two that we don't own and it's a question of how high you are going to reach in terms of price. Ideally in a portfolio you would just have that kind of company. In practice they are quite rare and there is a limit to how much you are going to pay and sometimes they get very overpriced.

At the other extreme you might have companies that are growing very rapidly but may not be able to sustain that rate of growth indefinitely. They can sustain it for a reasonable period after which it will fade, but it's not going to fall off a cliff. I think that kind of company is much more common. They are not easy to find but they are more common than the wonderful compounders. With these companies you are looking to capture the period of rapid growth, the period of re-rating and then probably move on within a few years. Occasionally they will surprise on the upside and they will continue to do better than you expected. They may gradually get to be long term compounders but the majority don't, they will just do their thing for a period and you come to a point where you have to move on.

Then I think you have a group of companies in the middle which are not growing at stellar rates. They are growing steadily at high single figure or low double figure percentage rates, which in today's world is very good. You wouldn't call them super dynamic, they are just steady, and although the growth rate is more modest, the price is more modest too. Often they'll be on the same PEG (price-earnings to growth ratio) as some of the more dynamic companies. You can argue that in risk terms they may be better in some cases because you're paying much less so there is less downside if things go wrong.

So you can end up with three quite different types of animal in the same portfolio. There are times when you think: 'I am definitely paying up for growth to buy this company'. There are times when you are thinking: 'this company is not going to grow forever but I am going to make quite a lot of money over the next three or four years'. Then there are times when you think: 'this company is growing nicely, and while it's not going to shoot the lights out it's much better than cash'. They are all perfectly valid and they are all under the same umbrella.

One of the issues of targeting growth is that you're often dealing with smaller companies and potentially less experienced management teams. How do you manage that?

When we buy into a growth business we want to buy into a company that we think is working now. We are not interested if management say that trading is terrible at the moment but will be better in six months. In that case we would rather come back in six months. We want everything to be working well today, and that includes having a management team that we believe are able to run the business properly. Obviously the ideal scenario is that the management team have a big shareholding, they aren't excessively greedy with salary and options and have incentive schemes that are aligned properly.

We want all that in there but the most important thing to us is the business. I really do believe the Warren Buffett line that if you have a business with a reputation for terrible fundamental economics and a management team with a reputation for brilliance, it's the business's reputation that wins out. There is only so much management can do but having said that, really bad management can mess up a good business.

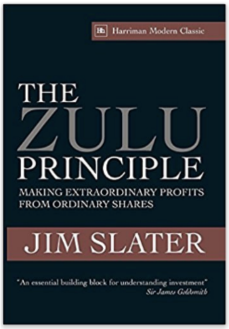
When there are problems you either sell or you have to do more. When we engage with management it's typically because there is a problem. It could be a simple thing like they have suggested a new incentive scheme that we think is crazy, in which case we will say so. We have a reasonable track record of engaging with them and winning.

If the problem is more fundamental than that, and things really go wrong - such as a massive profit warning - then we are normally minded to get out. Sometimes you don't want to get out because the price is too low and sometimes you think it can be fixed. Those are the situations where you then engage and become potentially much more active.

Your father wrote *The Zulu Principle* in 1992. When you reflect now on the strategy that he set out in the book, do you still agree with it?

Things change a bit around the edges but I think the fundamental principles haven't changed at all. It is a very sensible idea as an investment strategy to seek out companies that have a reasonable record of earnings growth, that are forecast to grow well in the future, that generate lots of cash, and where you can buy the growth at a sensible price.

Like any measure, the PEG is imperfect and it doesn't work when it's applied to the wrong thing. But when it's applied to the right thing and you combine cash flow and check the trading and that the most recent Chairman's statement is positive, those sorts of things are extremely sensible. Like anything I think the main skill is in the interpretation of those principles and applying it. It's not easy to do that.



Following *The Zulu Principle*, my father developed REFS and that involved a lot of back testing. Again it was interesting that in the back testing, just very basic measures like the PEG and cash flow combined, historically worked really well. You obviously got some rubbish in there too, that's the nature of data, but it actually worked surprisingly well. I have been surprised over the years how the systematic approach is occasionally better than anything else you might be able to do.

In other words, a systematic approach can guide you into areas that you'd otherwise think twice about?

I have a respect for the pure data. Obviously one has to interpret it and look at businesses carefully, but *The Zulu Principle* has stood the test of time very well.

There has been a lot of research since showing that when you combine growth and value filters you get that combination which is what *The Zulu Principle* is really about. It's not growth at any price; it's growth at a reasonable price with additional protective filters. When you combine those things it is one of the most powerful investment strategies in most of the academic works that I have seen.

There is a guy called Richard Tortoriello who wrote a book called *Quantitative Strategies for Achieving Alpha.* He looked at 1,500 different combinations of statistical criteria to see how they performed over a long period. Growth with value and cash flow filters is one of the top two. It doesn't surprise me, it makes perfect sense.

Obviously you have great discipline and control but are you conscious of some of the psychological biases that can sometimes hinder an investment decision?

Yes it happens all the time! Take anchoring on price. One can get obsessed on price, you can look at a company, decide you are going to buy it, you have done all the work and the price moves very slightly against you and goes up a bit. You had it in mind to buy at a certain price and it's a very human thing to get stuck on the price and of course it's very stupid. If it's a brilliant business, a few percent on the price doesn't really matter.

I don't want to give money away but at the same time, if you have done all the work and it's a great opportunity over the next few years and you are going to make 50 or 100 percent over 3-5 years, it's very silly not just to get on and buy it. So I am very conscious of that.

I am also particularly conscious of when things go wrong. It's very easy to hope rather than just move on. In our experience probably eight times out of 10 it pays to cut, almost irrespective of the price. But there are times when it doesn't pay, and that is probably the hardest decision in investment - when should you cut and when should you not cut.

There is an interesting book called *The Art of Execution* that looks at the characteristics of good fund managers, and the key point is that when things go wrong you should do something. Either you should buy or you should sell but what you should not do is nothing. We normally sell if we can at a reasonable price, and normally you can at some point if you really want to. Very occasionally, in very illiquid situations, you can't get out and then you've got to try and make it better and you have to get involved and try and move it on.

Occasionally we decide we are going to keep a holding but we are not going to buy more of it quite yet, but we will buy more at some point. We have one or two like that. It is very important not to be a rabbit in the headlights, you have got to do something. I think the worst investments are the ones where they just drift down and down and you do nothing. That is the thing people find psychologically very challenging.

I actually find cutting a loss extremely cathartic because you end it and you can put the money into something you like. It's a double whammy, not only are you getting out of something you don't like, you can put it into something that is better. A lot of that is about psychology. For most investors the battle to a large extent is with themselves, it's managing their own psychology just as much as researching investments.

A lot of quite good investment decisions might not look right for a period, for whatever reason they don't immediately work out. One has to have the courage of one's convictions but not be pig headed about it and be open to the possibility that one might be wrong. You have to have a mixture of conviction and humility, which is very difficult.

How can clients of yours can know that you've not just been lucky over the years, and that your outperformance can continue over the long term?

Our numbers have been very strong since we started and I am confident that's because we are doing something sensible. I think for anyone assessing a fund manager or a fund, the key is to look at what they actually do, how they make their money and whether they are doing it consistently - and we are. We are looking for a certain type of company and we are pretty good at finding them. We are pretty good at running our profits when we should be and we are not bad at cutting our losses when we ought to.

In investing you need a methodology, if you haven't got one I think it is punting really. We definitely have a methodology and we stick to it. It's about getting good at it and not veering off in different directions when it doesn't work quite as well - and there will be times when it won't work quite as well.

I am always conscious of the fact that if markets are drifting, it doesn't take very long for islands of extreme value to appear, and then it's very exciting. Markets are just averages so you get interesting things happening all the time.

I would also say that people who are not good at market timing - i.e. everybody - shouldn't worry too much about market timing! If they find a good investment, they should buy it - there are very few people who make a lot of money being negative all the time.

Mark, thank you very much for your time.

Lord Lee - How he made millions from British small-caps

When it comes to investing successfully in UK smaller companies, Lord Lee of Trafford needs little introduction. Famous for being one of Britain's first ISA millionaires, he invested around £150,000 in tax-free wrappers over the course of 17 years after personal equity plans were first introduced in 1987. His investments took him past the million pound mark in 2003 and his portfolio is now worth considerably more.

Lord Lee credits his success to a patient, common sense approach to investing in smaller companies. He takes positions in attractively valued, good quality, high yielding shares. Many of them he buys and holds for many years, often with no intention of selling.

He's an evangelist for individual investing and played a role in opening up the predominantly small-cap Alternative Investment Market to ISA investors in 2013. He is also a strong believer that investors should take every opportunity to get face to face with company executives. In 2014, he wrote about his investing successes (and failures) in a book called *How to Make a Million - Slowly.*

Lord Lee, what do you think it takes to be successful in the stock market?

I believe that the stock market is much more simple than people imagine, and I encourage people to back their own judgement rather than go into funds. There are only two things you need for successful investment, and that's patience and common sense. Patience I think is number one and it's something most people don't have. They see a profit and they want to take it. In a way, modern technology actually encourages more of that short term trading activity. Days before we had instant prices and instant coverage people would invest in a share and almost forget about it for years. Now you can press a button and the prices instantly come up. If you have got patience and common sense and are prepared to put some time to it, you should be able to do reasonably well.

In all my articles I have always tried to simplify the stock market for people. In some ways I suppose the one thing I regret in life is that I never started a fund that people could invest in. But because I focus very much on the small-cap sector I think I have brought to the attention of a lot of private investors companies that they had never heard of before. I have always been very honest in terms of saying when I got things wrong, as well as what was successful.

It sounds like you're fond not just of investing but of the mechanics of how businesses work, particularly British manufacturing and engineering firms. Would you agree?

Yes, I'm very proud and believe that we have far more good businesses in this country than people imagine. People say we have no manufacturing, and of course we have lost some big sectors, but there are still some excellent businesses in this country.

Is it a source of frustration that these generally aren't the sorts of companies that you see floating on the stock market these days?

The days of old, when established companies were coming to the market in a traditional form, have almost gone. Now the companies that are coming to the stock market are either near start-ups or in many cases have been in private equity hands. In other words, businesses that have been built up and have a profit record and come to the market with an offer for sale to the general public are very rare these days.

Which means that investors are being presented with heavily indebted companies in frothy priced IPOs?

Exactly, and that's why I rarely find any of the IPOs attractive. Obviously the private equity people are trying to get the last buck and sadly a lot of these companies are overloaded with debt, which I don't like anyway, from any point of view. It puts these companies under great pressure, and I don't like that either.

I like companies that operate conservatively, that are stewarded and have cash or low borrowings rather than being geared up to the hilt. So it's very much a conservative style of investment and one that is designed to minimise the losses. That is the key - not chasing the profits but minimising the losses. Everyone will have some successes but the key is to avoid the failures.

The parallel I draw in various articles is with golf. Things might be going quite well and, bang, you hit a shot into the river or a shot into the woods and it ruins the round. With a portfolio the key is to avoid those losses and that's what I think I've succeeded in doing with a very conservative approach to investing.

Do you think your passion for investing has made it easier for you to deal with emotional strains and periods of underperformance?

Yes I think so. There is obviously massive human content and input in a business. It is the people who are taking the decisions and running it. So to me it is all about understanding the motivation of those people and assessing them. That's why I like going out to visit companies and talking to chairmen and chief executives. Not in terms of finding out any inside information, which is obviously illegal anyway, because I'm not worried about the short term, or what the results are going to be in three months time or similar. What I'm interested in, taking very much a long term view, is what the overall strategy is and whether the person stewarding the business is taking a long term view.

It's very much a personal assessment and I've rarely been let down by individuals. The only problem of course is that by developing those relationships, which I've done over the years, if there is ever an occasion where you decide to sell those shares, you feel a bit of a heel cutting down the relationship.

Did your career in business and politics equip you well for spotting a suspect company boss?

Yes, I suppose that's right but I also tend to be a little bit trusting and therefore I find that when I have been talking I usually come away more enthusiastic about the company. I ask myself: 'are you being a little bit naive or are you having the wool pulled over your eyes?' But I suspect the answer, generally speaking, is no. That's because the process of selecting that particular company has eliminated a lot of the more risky companies and a lot of the more dodgy characters.

So I'm looking for 'long fuse' companies where I invest on a modest rating where there is a reasonable dividend yield and a modest P/E ratio. I'm hoping, I'm expecting, that over 'x' number of years there will be profits growth and hopefully a re-rating. So you get that double whammy that brings quadruple appreciation.

In addition, in the sectors that I fish in there is a tradition over the years of smaller companies being taken over by larger companies. I have been on the receiving end of about 50 takeovers over the years. I'll really only invest in a company where the people running it have got good stakes in the business. Where they are professional managers or people starting the business, at some stage they normally want to capitalise on their life's work. Of course their shares can be placed by a broker with institutions. But a placing would probably only be at the market price or at a slight discount. Whereas a takeover would generally produce a premium over the prevailing price. So those individuals are looking for an exit by way of a takeover. That's why we get more takeovers, that's the logic of it.

There has been a re-rating in the share prices of many smaller companies in recent years. Has that led you to rethink your approach of buying shares on single figure multiples and exceptional yields?

That's quite true. The days have gone when good, small regional PLCs on single figure P/E ratios and yields of 6.5 - 7 percent could be found relatively easily. Also, the days when the stock market really fell in the 2008 period, when yields were up on really good companies to 9 or 10 percent, have also gone. That was a great buying opportunity.

This is where some sense of history comes into it. I remember back in the 1970s when I was running what was then termed a secondary banking operation, the stock market fell. This was when some builders and property firms went down and there were rumours about NatWest. No-one would buy any shares at all in the early 1970s. Top quality blue chips were yielding about 20% but no-one would buy. Soon afterwards the market turned around and the recovery was pretty dramatic.

So apart from those exceptional periods when there were very high yields, and I bought things like Clarkson on a 9-10 percent yield, and Fenner on a good yield as well, you're right, there has been an overall upward movement in the market. Therefore, now I have to be content with a 3.5-4 percent dividend yield and a P/E of 10 or 11 rather than a yield of 6.5-7 percent and P/E of 6, 7, 8.

So one has to live with that. But even so, the key is getting in at the right price because value always comes through in the end. If you're investing nearer the ground, it's safer obviously if things go slightly wrong. I don't like what I term, 'investing on the high wire', where you're buying at P/Es of 20-plus as it were. Because if things go wrong, it can come down very, very sharply and you can lose a lot of money.

On the subject of market crashes, your portfolio took a serious knock in 2008. How did you manage your emotions at that time?

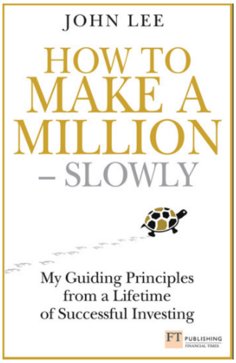
I don't spend a lot of time worrying about the macro side of life because you can always talk your way out of investing at any particular time. You could say, 'well heavens, who would invest now - there are problems with ISIL, China is on the decline, interest rates are about to rise'. You can talk yourself out of investing at any time. What I would say is that broadly, the world will generally become wealthier, the population will expand, people will want a greater quality of life, and the long term trends are encouraging. That's subject of course to a major armageddon type situation. But if you think that's coming along, what do you do anyway? Do you hide under the bed with a crate of whisky and a couple of bars of gold?!

So you have to work on the basis that we will get through these difficulties and there will be growth. But I'd preface that by saying that because of what I saw in the 1970s when the market really crashed and no-one was buying, I know that it can happen. I don't know what will trigger it, but it can happen. Therefore, you don't want to be caught in a borrowed money situation, and I've never borrowed. All I am interested in during the short term is the flow of dividends - and the capital value will hopefully take care of itself over a long period.

I'm very focused on companies paying dividends and what you can interpret from the announcement of a dividend. The main thing I'm interested in when a company has just reported is what it has done with the dividend. The decision on the dividend tells you three things. Firstly, it's a reflection of the actual results themselves, the year that is being reported on. Secondly, it tells you what is anticipated for the next year - because only a stupid board would lift its dividend if it can't at least maintain it next year. And thirdly, it tells you what the cash position of the business is, because they have to be in the position to actually pay the dividend.

In addition, when a company pays a dividend it gives a certain prop to a share price, as well. I don't want to invest in a company where there is no dividend and it's all hope and prayer stuff. And of course within an ISA, the reinvestment of the dividend for compounding has a massive impact over a period.

You've done very well from long-term buy-and-hold positions. It it the classic case that 20 percent of the holdings made 80 percent of the gains, or is it more evenly distributed?



I think it's rather more evenly spread than that. I have had some spectacular successes but when I look at the portfolio now - both my ISA and non-ISA portfolio where I have not sold because it would trigger capital gains tax - there are a lot of holdings that are showing five, six, seven, eight, nine times appreciation. There are no real loss makers now, although there have been loss-makers in the past, don't get me wrong.

What I've learnt is to apply a 20 percent stop loss. If you have got it wrong, take it on the chin and get out as quickly as possible. Not only is your loss likely to get worse, but it knocks your confidence. Every time you look in the portfolio, you see that share there showing a 40-50 percent loss and it pricks you and draws blood. So get rid of it.

Stop losses divide opinion among many investors. You discuss the merits of a 20 percent stop loss, but is that a fixed instruction to sell or just personal discipline?

Historically I have never used stop losses and I now realise that had I done so I would have done rather better. Fortunately there have not been too many losses in recent years, so I have come to stop losses relatively recently. But the answer is that I don't instruct a broker. I would judge each case on its merits, there may be exceptional factors. There may be a general crash in the market, for example, and I wouldn't want everything to be disposed of. Having incurred costs building up the portfolio, I wouldn't want that. I think a 10 percent stop loss, which many people have, is too limited. So 20 percent is more realistic, but with discretion.

You have written that on occasion you've held on to positions for too long before selling. Have you changed your approach to the way you deal with losing positions?

Yes, at the end of the day no-one is perfect and it's not a science. Events that one can't foresee will all of a sudden come along. Who would have thought that the price of oil would have slumped to the level it has done? All logic would have said that the world is growing, industrial demand is increasing, the population is increasing and therefore the price of oil should, over the long term, tend to rise. There isn't a living economist who forecast that it would slump to anything like this level. So that's why I operate below the macro and focus on the particular company.

You have also mentioned in the past the frustrations of selling stocks like Clarkson and James Cropper too soon. Do the missed opportunities still sting?

Selling too soon is my biggest mistake. But on the other hand, the monies I got from selling those shares I invested in other things that have done reasonably well. I have never worked it out from a mathematical point of view, but as a generalisation I have sold good stock too soon. So I say to people that if you are into something that is good, stay with it unless that which you are going into is demonstrably better. Value will always come through in the end; it could take years but it will come through.

If you were starting out today, would you change anything in your approach to investing?

If I were to make 10 new investments now, I'd be very disappointed and very angry with myself if more than one was a total failure. I would expect two or three to do exceptionally well, two or three to do reasonably well and two or three to break even and maybe one to be disaster - and even then I'd be angry with myself. That's after 50 years of endeavouring to hone one's technique and improve.

The principles of business remain the same. Companies should be cash rich or low on debt, the management should have a big stake in the business, there aren't frequent board changes, you can understand the business and it has some sort of profits record. But it's one type of investing. There are obviously people who specialise in investing in the biotech sector or the exploration sector. They can do enormously well if things go right but they accept that a number of their investment will go the other way. But I'm fishing in a different sort of river.

On the current climate for investing, where are you on an optimism scale of 1 - 10?

Generally speaking I suppose I am 5 or 6, I'm fairly cautious at the moment. I tend not to get too obsessed with the overall levels of the market, what I'm more focused on are particular companies. But there aren't many that are outstanding buys at the moment. Most prices are reasonably full. That's not to say there isn't more growth to come, but they've certainly had a good run in the recent past.

Lord Lee, thank you very much for your time.

Build a strategy like Lord Lee

Lord Lee typically looks for companies that are growing at a reasonable pace, paying dividends and have shares that are attractively valued.

Find out now which shares pass the rules of our Lord Lee strategy screen: http://stk.pe/lordlee

Gervais Williams - Big ambitions for smaller companies

During his 30 year career in the City, Gervais Williams has been a huge advocate for investing in one of the London Stock Exchange's most exciting and occasionally controversial offshoots - the Alternative Investment Market.

Williams has utter conviction in the value of investing in smaller companies. They've been a regular source of outperformance for him: first during a long spell at Gartmore and latterly as Managing Director of Miton Group plc. But more than that, in the aftermath of a protracted credit bubble, he predicts a resurgence for small-caps. He also believes that fund managers could and should be allocating more capital to the very best home-grown firms, not just for clients but for the sake of everyone.

Gervais, you literally wrote the book - *The Future is Small* - on why smaller companies hold such strong investment appeal. Can you tell me why you think that is?

As we all know, the long-term purpose of investing is to allocate our collective savings to the best and most productive companies. One of the problems is that when you're making a lot of money for your clients, as many people have since 2008, that doesn't necessarily mean that the money is getting down to the best companies. People have made money in indices, in various types of options and sophisticated structured products. I think I'm more cautious about the future and I think we'll have to get better at allocating and better at improving productivity and better at explaining what we're doing in terms of being socially useful. This is a factor that I think is going to become much more politically mainstream.

Take index funds, which are very popular at the moment. They're low cost, which is brilliant, I love low cost. But if it's just allocating to the biggest companies, which aren't all that UK orientated in the first place, then effectively we're putting our savings overseas. Now there are good reasons for diversifying overseas but the truth is that we should be investing more at home. It's good for job creation and domestic growth and takes advantage of the ability of some of these smaller companies to grow even when the world's not growing.

For some years I've been talking about the credit boom coming to an end in 2008, and how we've had a mini-credit boom since in China. What's happened is that credit boom trends have been with us for so long, that there's nearly an entire generation in the City that think that credit boom trends are normal. My view is that they're not normal, that abnormal is coming to an end and we're getting back to normal.

It's no secret that you're a big supporter of the Alternative Investment Market and the companies quoted on it. Where do you see the main attraction?

I think we're very lucky to have the AIM market. If you look around the world, the leading micro-cap market used to be Nasdaq up until the mid-1980s, but smallness has fallen down the agenda. There is no Neuer Markt or Nouveau Marche, they've all closed down. With AIM, we have on our doorstep possibly the leading micro-cap market in the world. There are lots of companies in there, some have done well and some haven't, some are in fashion and some are out of fashion.

The wonderful thing is that it's such a wide investment universe. The point is that there are loads of pebbles on the beach. I can pick up a pebble and I just don't know if they're telling the truth or not and I don't know if their proposition is going to work or not. But there are 1,600 other ones, so I can put it down.

But if you're a big-cap fund manager looking at Shell or BP and you put it down, the oil price may half or it may double, and your clients will ask you why you have missed out on a big rise. You have to be very sure footed when you're dealing with many of the largest companies because if you miss certain companies' outperformance that can spoil things even if you are doing everything else right.

There have been calls for AIM to introduce more regulation and change certain rules. Do you think that the rules need tightening?

I would be careful to not get too regulated. It's easy to keep shutting doors after horses have bolted and then you gradually get a longer and longer rulebook. So I think we have to be cautious about adding more layers of rules, although sometimes things have to be changed. We have to be focused that we don't inadvertently make it more difficult for liquidity.

It's easy to say sometimes that short sellers or market makers are wicked people. Some of those that came out with bear raids on stocks aren't motivated by being helpful, they're there to put one side of the story and move the share price for a profit, which is abusing the system.

Generally, I think we should find ways of having investors who invest on a day trading basis along with investors who invest on a three years basis, along with people who are buying on financials and those that might have a short position. All of that means you've got different investors buying for different reasons and selling for different reasons. That gives you a vibrant market with liquidity and prices that are continuously being set at the appropriate level. That's largely what we have. I'm sure we can improve on AIM but I do think that it's a winning formula already.

Low liquidity on AIM is a key issue for some stocks, which must

mean that you face challenges when it comes to dealing in size?

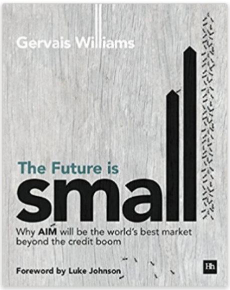
It's a percentage game I suppose. Sometimes we want to buy what might be a fantastic stock and we can't get any shares. We've done all the work, it ticks every box in the book and it's all looking great but we miss out. But more often than not I would say, just drip, drip, drip, we'll buy little bits now and maybe later and build up a holding gradually. It takes a long time. I was recently looking at one of the largest holdings in the Miton UK MicroCap Trust, James Cropper. The fund has only been in existence for a year and we got lucky with a line of stock soon after we set it up. But off and on we have been buying that company for pretty much four years. It didn't matter that we didn't get a lot to start with.

Now it can be the same on the way out. The company has done well, or may not have done well, and we need to reduce. Again, it maybe drip, drip, drip to get the money out, and it does take time. But we've got a really long list of holdings - the Miton UK Multi Cap Income fund has around 150 holdings. We might get lucky selling some and not so lucky selling others. Usually if companies are successful they are quite easy to sell. If they are unsuccessful or their share prices have gone down, so they are a smaller part of our portfolio anyway, the liquidation doesn't have the same impact on the portfolio. The combination of both those factors means that actually the liquidity issue, in our view, is probably slightly overstated as a worry.

That hasn't stopped a general trend for small-cap managers to gravitate towards mid-caps, though. I guess you think it's likely that trend will reverse?

Certainly over the past 25 years the industry has had redemptions at the smaller end. Most small-cap funds have got smaller and most small-cap fund managers have moved into mid-caps. Pretty much for 25 years of my 30 years career we've had a period where it's like lobster pots - you can get in but you can't get out, and that's something I had to get used to.

But that was then, and my view going forward is that the lobster pots will turn around and you'll be able to get out any time you like. We haven't got there yet but that's where we're going and that's why I think the future is small. It will be very exciting because illiquidity can suddenly mean a whole lot of different things.



There have been some high profile company disasters on AIM. Is this just a natural hazard when it comes to navigating the market?

Let's put this in context, you can lose money in fully listed companies as well as AIM companies. For all the negatives like Quindell, which did go up like a rocket, and it came down like a rocket, but certainly when it was well known you could buy or sell a million pounds worth of stock every day. You might not have liked the price, but the market was open.

Generally, the AIM market isn't perfect and it has lots of negatives about it, but it's better than almost anything else out there at the moment. If we're lucky enough to continue to get the vibrancy of smallness and capital allocations to smallness it could become a dominant market in the world. It's not just about UK quoted companies, we're seeing US companies listing on AIM, European stocks and there are a number of Israeli stocks of course. So it's gradually becoming a more international market. That is good because we've got some fantastic tiny ones under the bonnet but we also have some international companies where valuations are wonderful. That means we can diversify and participate in their success as well.

What are the key features of your investing process - what are you looking for in a company?

The best part of the process is meeting companies and making decisions. We can use sophisticated models and pick up new trends coming through, but there is nothing better than talking to the companies themselves. I probably see more companies than anyone else, in between reviewing portfolios, meeting clients and looking at new challenges that are coming up.

As a fund manager, you can't always rely on share prices moving your way, so you have got to find a way of delivering an attractive return for your clients. If the world isn't going to help you much, you have to find companies that can help themselves, so it's about fundamentals. It's not just about those that are generating cash now or paying dividends now, but certainly over a three or five year period we've got to find companies which are going to be in a strong position to generate cash and pay dividends. Some companies are doing that straight away. But we are also investing in companies where it's a bit uncertain for sure when they're going to do it.

A lot can happen in three years so you can't really look that far ahead. But if you can invest in companies that have a good chance of being in a very cash generative position with productivity improvements coming through, which then drive up cash generation in the business, then that is really what we're about.

A lot of those are companies that are out of fashion, too small or they've upset people in the past by making a mistaken acquisition. But they are also companies which are ambitious or moving into new areas or doubling their sales force or bringing in a new product.

There are some companies which just go up vertically and people get awfully excited about them. But there are a lot more companies that go up a lot more steadily, where the chances of losing your shirt are pretty light and the upside can be very substantial.

Can you give me an example of a stock where that investing approach has worked well for you?

There have been plenty of them. The truth is that often they go up, the valuation moves up and we take some profits, and they carry on going up for much longer than we think. Some that I've made good money on, others have made good money on them too, because they've bought them from me.

There have been companies like Finsbury Food, which we were buying at 23p-25p. It had upset people in the past by becoming too geared and because of the debt its service levels came off a bit. They were having to run the business for cash rather than customers. Plus, cakes and things sounds like a bit of a dull sector. When we first got involved the debt was coming down but most particularly, they could make productivity improvements with a cash payback of between nine and 18 months. But they were constrained on making those capital investments because of the balance sheet, so we suggested that they do a Rights Issue. The share price was on the floor and the valuation was low in absolute terms. But the point was that they could put the cash in for productivity improvements that on average had an 18 month cash payback. So you put in £5-10 million and within a year and a half you have £5-10 million on the balance sheet. Now that is seriously good.

It's a terrific company, the top line is growing nicely, they are still getting cash paybacks and they're still investing hard. They've started paying dividends and the share price has moved on, but it's still cheap. The underlying growth rate isn't that high but the risk/reward ratio for shareholders is beautiful. Those are the really successful ones.

Presumably there have been a few disappointments, too?

Well, I've lost my money 100% in certain places - not many times, but a few times. I suppose the biggest one in recent years was Independent Insurance. To be fair it was a complex balance sheet and we didn't anticipate all the risks correctly so we lost money on that. More recently there was Silverdell, and we lost money on that too. It happens occasionally and there's always a story.

Where do you think individual investors get things wrong, and are you wary of falling into similar traps?

I think we all love stories and sometimes it's such a good story that people get a bit over-anchored to it and they lose sight of the valuation. I think that happens quite a bit. There is a lot of fuss about Quindell or whatever, and it's all very exciting and the more the share price goes up the more you think it must be right. But it may be that the risks are going up without the fundamentals. So you have got to separate the share price from the underlying fundamentals.

We've got such a broad spread of portfolios and the opportunity set is so wide that if a share price rises strongly we don't need to stay for the finishing post. We can take our profits and allocate elsewhere. So it's not that we're cleverer than anyone else it's just that we've got a wider number of new ideas coming through all the time - so we can rotate our capital around a bit.

During your time at Miton you've established a stable of funds and trusts. What has been your approach to doing that?

What we've done at Miton is put together strategies which aren't just better than the competition but to position the portfolios so they are very differentiated. It's not there to outperform the competition just a little bit, although we love to do that. More particularly we will zig and zag at different times.

We've set up single strategy funds over the last five years which are very different. Take the Miton UK Multi Cap Income fund, which was the first fund out there which said that you can get income from large-caps, you can get it from mid-caps, you can actually get it from small-caps and even AIM stocks. Around 35% of the fund is invested in AIM stocks. People don't think of AIM as an income area but there are some decent income stocks there. They're not being well covered and the shares are often not quite so accurately priced so there's a bit more added value from stock selection. That's been so exciting for us.

Finally, you're one of the best informed investors in smaller UK-quoted companies. Are you still confident that the future for these firms, and those that invest in them, is very exciting?

It's going to happen, which is why I wrote *The Future is Small.* It's partly to help people to start looking ahead and preparing themselves. It's to help clients like wealth managers, IFAs and pension schemes get conviction about what's going on. This absolutely helps us and the companies themselves. It reduces the cost of capital for them because the valuations go up, which means they can issue fewer shares for the same acquisition. The cost of investing goes down and the productivity improvements are better still as a result of that. Net, net, net it's a virtuous spiral.

As a sector, the more small companies outperform, the more people will come in, and the more people will want to come in, the more illiquidity will drive outperformance. My view is that it all got a bit too skewed to globalisation and bigness, and the pendulum is now swinging back to the middle. It's nothing like convention, but the trend is beginning to go our way. It will be transformational for growth and share prices and productivity, and that's going to be great news for all of us.

Gervais, thank you very much for your time.

Build a strategy like Gervais Williams

Gervais Williams typically looks for small companies with reasonable valuations that have the potential to grow fast. He focuses on the ability of firms to increase cash generation and pay dividends.

Find out now which shares pass the rules of our Gervais Williams strategy screen: http://stk.pe/gervaiswilliams

Giles Hargreave - Lessons from a top small-cap fund manager

There aren't many people who know more about successfully investing in small companies than Giles Hargreave. Along with Eustace Santa Barbara, the co-manager of his flagship Marlborough Special Situations fund, we met to talk about strategy, management and the intricacies of running a £1bn+ fund.

At 68, Hargreave has stepped down from the day-to-day running of his investment management firm, Hargreave Hale. He continues as chairman and is hands-on in running £1.7bn across three of the seven Marlborough funds the firm handles. At any time he can tell you the precise details of any of his portfolio holdings, aided by a folded spreadsheet that he carries everywhere: *"Wherever I go, even at a cocktail party, you'll find it tucked into my pocket."*

The joint venture with Marlborough - where Hargreave Hale manages the funds and Marlborough does everything else - works well. So well, in fact, that since the Special Situations fund started in 1998, Giles has earned a reputation as one of the top performing smaller company fund managers in the UK.

What comes across more than anything is that Hargreave and Santa Barbara have a determination for getting under the skin of the companies they invest in. In an area of the market that's notoriously under-researched, they've created an edge by relentlessly meeting and re-meeting management teams and having a keen eye for detail. As for their strategy, they're looking for fast growth and quality management in businesses that are simple to understand.

With a universe of 2,000 stocks, the £1.049bn Special Situations fund has an eye-catchingly diversified 204 companies in it. But for anyone concerned about issues of liquidity and capacity, the answer is simple. They believe the fund actually has the potential to double in size without compromising the strategy or making any major alterations to the stocks it holds…

Giles, it looks like you're enjoying the freedom of focusing on managing these funds, is that right?

Giles: Absolutely, the funds is what I do! Over time the funds have got quite a lot bigger and they required more personnel and more managing, so there are now 15 in the fund management team. That means that I can spend my whole time looking at companies, meeting companies and managing the funds.

When you started Hargreave Hale did you ever expect things to turn out quite as successfully as they have, and why do you think that is?

Giles: No, not at all. We have been very fortunate in the quality of the people we've employed - the fund managers, the administrators, compliance and finance. We've managed to employ good people and keep them, and that's the reason for the success of the business.

Plus we did what everybody ought to do which is to put our clients first and our commissions second. We've built a pretty substantial private client base now and fortunately the performance has been good. The only real way you're going to build a business like that is through personal recommendation. The Special Situations fund started at 56p in 1998 and today it's just short of 1200p. When people open their portfolio and they see that, they tend to tell their friends.

You're obviously passionate about fund management, but is

there anything about it that drives you crazy?

Giles: When I make mistakes and get things wrong - that's the most annoying thing. Obviously, if the funds do well and the clients do well then the firm will do well. If I'm going to be chairman of the company then it's my responsibility to make sure we do as well as we possibly can. If I'm running a fund, especially the flagship Special Situations fund, it has got to do well. Your reputation is only as good as what you do tomorrow - you have got to keep the performance up.

There have been a number of IPOs in your space recently, so how actively involved have you been in them - and what challenges do they pose?

Giles: We did the IPO of Hotel Chocolat, and that has done well so far. Then there was Fever-Tree, which has been a terrific share since the IPO.

Eustace: They do pose problems. In part there is limited history so you have no track record of management saying one thing and delivering on it. You don't really know what happened behind the scenes or what their internal targets were.

The second thing is that when we meet some of our many holdings, and we do run very diversified portfolios, we're going on past meetings with the management with individuals that might have met them 10 times before. So we have a bank of knowledge. With an IPO it's entirely new and there is a lot of information to absorb quickly.

One of the real advantages we have is an extensive team which allows us to maintain the existing positions, but also to explore new ideas and see new IPOs. We run £1bn in AIM of a £60bn market cap, so we're one of the largest institutional investors in AIM. We are on the map for brokers and they may well bring us in at a pre-IPO stage, which is very helpful.

A big part of our process is meeting management and a big part of our confidence in the equity stories that we meet is re-meeting them and constantly re-testing the investment cases to the point of paranoia. It's about asking whether we're right and understanding what the management says is what they actually do. If they say they want to be growing revenues at 'X'percent and they're delivering on that, that's what we like to see.

Giles: To my mind, IPOs are an obvious place to look for investment. Effectively, you wake up in the morning and assume that all the stocks in the market are correctly priced (of course they're not, but assume they are). Something else comes along so why would you buy it any more than you'd buy anything else that's on the market already? The only reason you'd do it is because they're cheaper. So by definition, IPOs have to be relatively cheap.

We get more right than wrong and when they do go wrong we tend to get rid of them. In our game you've got to cut your losers and run your winners and maximise your good ones. I would guess that most professional fund managers do that. But of course sometimes that's wrong and sometimes you make a fool of yourself.

When it comes to investments that have gone wrong, do you tend to engage with the management of just sell out?

Giles: I try not to. I would much rather spend time looking at something else - you can get your money back on something else quite quickly. You shouldn't spend too much time trying to salvage a lost cause. Normally it's a question of whether or not you're going to put more money up, and on the whole I try not too.

But in a way, the best result could be to sell on a profit warning and wait for the price to fall again after another two or three profit warnings and then buy back in at a more enticing price. You have got to be flexible and I don't believe in having rigid rules. The answer is that generally we will sell but now and again we might not.

Eustace: With profit warnings, it's not normally guaranteed that you're going to sell but actually these things do often come in threes. When there's a problem it's usually 12 months before anything happens. So unless it's a very obvious blip, which is unusual, you've got to lower the position. That comes with experience and humility to say the facts have changed.

I certainly know of some fund managers who have such a high opinion of their thinking that they will add to a stock when they're 10 percent, 20 percent or 30 percent down. That might well work but there are scenarios where you can get blinkered and caught out.

Presumably the wide diversification in the Special Situations fund means that you don't have to worry too much about individual disappointments?

Giles: I think so. We have got 200 stocks in the Special Situations fund and we're often criticised for doing that. But think about it like this… there are 2,000 stocks in our universe, so we own 10 percent of them. When we've selected our stocks, we've obviously gone for the best quality. We tend not to have very large holdings to begin with but we expand them as we get to know each company.

Two hundred stocks is very likely to contain one or two really hot stocks, you're unlikely to miss them. In that case you average up and if you follow that principle, you should do okay. The chap who has 20 stocks and five percent in each is either going to do spectacularly well or spectacularly badly. We're not trying to do that, we're trying to have relatively low volatility and relatively good performance. Conviction is a very dangerous word, I'm not keen on conviction. Falling in love with shares is a terrible mistake.

There is a great deal of research that shows that smaller companies tend to outperform over the long term. When in your career did you focus your attention on small-caps?

Giles: From when I very first started dealing in the stock market. It's just so obvious that with a small company you can make money a lot faster in percentage terms than with a big company - you've got a real chance. You can buy stocks that go up three or four times quite quickly, but you're unlikely to do it with larger FTSE stocks.

The second thing is that you're not going to have an edge with a FTSE stock. Everybody is going to know as much about it as you do, and probably a lot more. But you can make your edge with a small company - just look at Jim Slater's Zulu Principle.

I was going to ask about your biggest influences - I take it Jim was one of them?

Giles: Jim was a great friend of mine, he and I belonged to the same Bridge club. Fortunately for me I learned Bridge at the age of seven, and he learned Bridge at the age of 47, so it was always going to be more difficult for him - he was never going to be as good as me! He showed me that if there was something you wanted to learn about in life - just like the Zulus - then very quickly you can become one of the world's leading experts. It's the same with shares. The great thing about Jim is that his methods are very simple, he certainly taught me a lot.

You're looking for companies with a combination of the best quality and growth, but where does valuation fit into your thinking?

Eustace: There is no rule for finding the best small-caps. You get some very fast growing, great quality businesses that at any given time might trade above the P/E that you anticipate. Where we have potentially very high growth companies in terms of earnings, and we believe that they can continue to grow over medium term, we are willing to pay a higher P/E. So we would look at PEGs more than other people.

When you've got EPS growth of 30-40 percent, which is attractive but not unheard of, what do you pay? Do you pay a P/E of 40, is it a PEG of 1 or over 1, or is it a PEG of 2 - is it 80x P/E? That's where we have to try and establish whether a £30 million company today can be multiples of that because of what we see the management being able to do.

Giles: The worst thing you can do in investment management is to sell a good stock and snatch a profit. Every time I do it - which I like to think only happens once every several blue moons - it make me feel so sick. I remember when we sold Dignity - I get so cross! I never bought them back again and I've been cursing about it ever since.

Are there any other stocks that you you particularly like at the moment?

Eustace: Ah, I've got a nice one, it's called On the Beach. It was a Numis IPO in 2015 and it's an online travel agent specialising in beach package holidays. Unlike Thomas Cook and Tui Travel, where you have to take a package holiday leaving Saturday and coming back Saturday, you can fly on any day at any time. What that means is that if you fly on a Tuesday with easyJet, it'll probably be cheaper. So On the Beach is an aggregator of those sorts of propositions. Last year they did about 1m package holidays. Thomson and Tui do about 4m each and Dart Group's Jet2 Holidays do about 1m.

What we really like about On the Beach is that've spent a lot of time and money on the personalisation of the product. When you walk into a Thompson or Tui Travel, you might say, I want to be 50 metres from the beach, I want 4 star, I want a pool for the children and I need daycare for the toddler. With On the Beach, once you've logged in, it will know that those were my criteria for the last holiday that I booked. It will know what I selected and that I also looked at Portugal, Spain, 100 metres from the beach, etc - it will know all these things that I was thinking about.

So I think the proposition is compelling and that the incumbents, Tui Travel and Thomas Cook, are offering an inferior service at a higher price. I like the ease and functionality of the website and I think the earning growth potential should be well over 20 percent and perhaps nearer 30 percent over the next three years. It's on a valuation of 18x earnings dropping to 14x. Why is it valued as such?

I don't think terrorist atrocities have helped. On top of that, it's a recent IPO and people want to see that they can deliver on what they say.

In addition, Simon Cooper who started On the Beach, had an original business that he ran for 10 years called On the Piste, which was the same thing except for ski holidays. He sold that to Thomson, so he's got form. He's typical of something we like in the small-cap space, and that's repeat winners. Simon Cooper is one, and someone like Vin Murria would be another.

How can you tell when a management team is telling you the truth?

Eustace: It's because we have so many meetings. Given that exposure, you'd have to be pretty slow not to gradually develop a sense of what you're being told. A simple, credible strategy well executed - that's what's going around my head over and over again. I like to ask management teams in a couple of minutes to remind us of the investment thesis. If they can't answer that two minute question well, then how are they ever going to convince someone they meet for the first time to buy shares? Ultimately that's what is going to drive the share price higher, so you want to make sure that the management do what they say.

What are your reflections on the performance of the Special Situations fund, and does its success actually create challenges in terms of liquidity and the potential to outperform in the future?

Eustace: There are 48 funds in the IA UK Smaller Companies index, and to qualify for that you need 80% of the assets in the bottom decile of the market. So with £1bn under management we have drifted up slightly in terms of the FTSE 250, but when you compare where we are in terms of market cap to where the other funds are, we're still slightly below the average.

Liquidity we don't see as an issue, and capacity we don't see as an issue either. There is a case to be made that the Special Situations Fund could double in size without compromising the strategy or indeed altering any positions except the top five names held by the Marlborough funds collectively, which are Cenkos, Parity, Tricorn, Fairpoint and Acal.

Giles: Since we started the Special Situations fund we've had some very good years. The only bad year was 2008, although we did better than the market. Generally all the way through we have been as good or better, which is what we're trying to do, and we've ended up with 19 percent compound annual growth. Even if you deduct the first three years when it was very small, you still get a good number.

There are a variety of skills among our fund managers. If I go and ask one of the guys what he thinks about a stock, he tells me what he thinks and not what he thinks I'd like to hear. Or if I tell them that I really like a particular stock, I have to tell them why. I can't get away with it just because it's me!

When I retire - if I do retire - I will start running my own money, at which time I'll probably end up with positions that are far too big and not listening to any of my own maxims!

Giles and Eustace, thank you very much for your time.

Build a strategy like Giles Hargreave

Giles Hargreave typically looks for good quality small companies with the potential to grow quickly.

Find out now which shares pass the rules of our Giles Hargreave strategy screen: http://stk.pe/gileshargreave

Nick Kirrage - Inside the mind of a deep value fund manager

Buying bargain basement stocks that nobody else wants is a strategy that's forged the reputations of some of the world's greatest investors. But while value investing has a rich heritage, it comes with drawbacks. Performance can be volatile and deep value stocks can be unpredictable. Ultimately, it's an approach that suffers periods of underperformance.

With this in mind, it's hardly surprising that disciplined, long-term value investing isn't exactly prevalent in professional fund management. In an industry notorious for short-term performance targets, value-focused fund managers arguably suffer from career risk more than most.

But one exception is the Value Investment Team at the asset management giant, Schroders. Headed by Nick Kirrage and Kevin Murphy, the team manages around $18 billion across a suite of value funds. They include the Schroder Income fund and the £750 million Schroder Recovery fund. After taking over the Recovery fund in 2006, the team took it to a 127.1 percent return over the next ten years, against a sector average of 72.5 percent.

I met with Nick Kirrage to find out what it really takes to beat the market in stocks that nobody else will touch.

Nick, you've been running the Schroder Recovery fund for a

decade. What are your reflections on what you've achieved and how it has performed?

Kevin and I have been investing for over 15 years, and 10 of those have been spent running the Recovery fund. When we took it on there was quite a lot of responsibility, even though very few in the UK market knew about it. It was an unconstrained fund that was benchmark-unaware and half the book was institutional and internal money. We were invited to showcase what we could do, as long as it was in a value style. Of course, the first thing we did was underperform for two years!

But that's the nature of the market. Value outperforms over time, and when it doesn't I think a lot of the skill in the job is psychological. It's about learning not to drive yourself crazy or fall apart on bad performance. Over time you have a strategy that outperforms, but you also know that you'll struggle with it.

So it was a huge source of celebration after 10 years because we'd set ourselves the target of being in the top decile over that time period, and we were. The fund's performance is around 18th out of 320 at the start of that period. But the job is only half done. We always said we'd like a 20 or 25 year track record. If we could repeat the fund's performance from the first 10 years it probably starts to put us in a group of names that everyone knows. It's not really about running a lot more money, it's about doing something that, statistically, would have proven that it's not complete luck. We'll have done something rigorous, repeatable and valuable for clients.

At what point in your career did you develop this strong value-focused philosophy?

I didn't do economics at university, I did aeronautical engineering because I like things you can prove and build. The numbers say the plane will fly if the lift is more than the weight and the drag. I'm inherently drawn to an approach where you can look back over 100 years and say 'this will work'.

The question as to why it will work is really important. The reason why value works is that everything changes in investment except one thing - humans. We're the bit that's constant. Our behaviour, our emotion and our psychology is the only thing that doesn't change. So being able to say that this works because humans are pretty predictable on average over a long time period is a very reassuring thing for me.

Presumably you need that reassurance given that value investing is well known to have periods when it doesn't work?

While it's reassuring, someone can take you to one side and say the bad news is that if you invest in a classic low-P/E value strategy you've got a 70 percent chance of underperforming for three years in a row over 25 year investment career. Doesn't everyone get sacked if they underperform for three years in a row? Yes, probably. So the first thing you sign up to as a value investor is that you hope those three years aren't the first three. You can't pull out of the strategy when you're two years in and starting to get nervous.

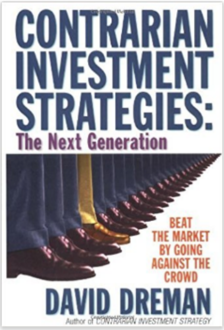
Psychologically you've got a set of criteria and you have got to fully sign up and embrace it. I love the fact that I've got an approach that means I just need to be mentally tough. We do a great deal of statistical and company analysis and I spent a lot of time learning about balance sheets and accounting. But while that's important, in the end our big advantage is being able to do what other investors don't, won't or can't for reasons that are either real or imaginary.

How do you balance the inevitable periods of underperformance with working in an industry that is so competitive and judged on recent performance?

I can't escape the numbers that value may underperform. Every value investor in the world is crossing their fingers that we're not going back to the late 1990s, when there was five years of aggressive value underperformance. People like Neil Woodford did a great job holding the line for many of those undervalued investments. But the truth is that for every guy that survived and and went on to become a guru, there were 10 guys that got sacked three months ahead of time.

There is a luck element but you can help yourself by doing a number of things. The most important thing is to be honest with your clients. The volatility of an approach like Recovery is quite significant, and even though it is low turnover it has got very high benchmark volatility because it is so different to the benchmark. When we're 50 percent ahead of the benchmark, as we were in 2012/13, we don't go to clients and say now is the time to invest. But when we're 15 percent behind the benchmark, as we were in 2015, we do approach them with the tough sell that now would be a good time to give us more money. After 10 years they can see there's quite a good track record of us bouncing back. Even though those periods of underperformance are brutal as an investor and difficult for clients, you give yourself the full three years to come good.

There are a lot of well known names in value investing, but are there any that have been a particular inspiration to you?



David Dreman's *Contrarian Investment Strategies: The Next Generation* was the first value book I read and I was blown away by it. He's one of the elder statesmen of value investing and he's still getting sacked from places he goes to! After that there was The Intelligent Investor and Security Analysis and then Joel Greenblatt and James Montier and all the behavioural finance stuff by people like Daniel Kahneman and Michael Mauboussin.

There's another guy called Richard Oldfield, who's a value investor in the UK, and he wrote a book called *Simple But Not Easy*, and I think that totally encompasses value investing. When people talk about it, you think that everyone can do go off and do it. And in many ways everyone can do it, but it is not easy.

When it comes to your investment process, where do you start?

My job is to identify risk and reward, balance the two and work out where the risk is mispriced. We believe that reward is identified as some function of normalised profits and a normalised multiple. You work out what you want to pay for it, which is typically somewhere between eight and 12 times earnings - bearing in mind we're pretty stingy people. Then you'll work out a target price, which will give you an upside or a downside. There are a lot of factors that go into that, like looking back at the accounting and watching for red flags.

On the other side you have risk, which is a more intangible thing. Everybody wants to turn risk into a number, and typically that will be volatility. But I believe that permanent risk of capital is associated with indebtedness, although there maybe business factors that are genuine structural risks that you have to take into account.

Leverage tends to be the way that you permanently lose money because businesses get squeezed to death. It's not always balance sheet leverage, it could be working capital adjustments, factor financing, pensions, lease adjustments or cash trapped overseas.

Once you've done all of that, you have work out how to compare these two things - where is my target price and where is my risk/reward?

How do you deal with the fact that you might miss something or that some of these companies just will not recover?

We are continuously trying to evolve how we think as a team and asking how we can get better. It's a strange industry because if I buy a stock that goes to zero a year later, did I do the right thing or the wrong thing?

Typically, the answer of course is that I did the wrong thing. But I don't believe that because I live in a world of probabilities. What I want to know is if I make that call 100 times over my investment career, will I be right with 70 of them? That's an incredibly powerful thing to do. With a portfolio of 50 stocks, if 28 are great ideas and

22 are disastrous ideas and I repeat that percentage every year for 30 years, I'm in the best 5 percent of fund managers who ever lived on the planet.

That's hundreds of mistakes, so I need to have high conviction but also humility and understanding of my ability to forecast the future and the probabilities of the world. So we do have a checklist in terms of how we think about things like the balance sheet, the profit and loss and businesses generally. But it's not completely formulaic and we're open to evolving it.

Investment is the classic 'Dave Brailsford cycling team' world of marginal gains. Tiny differences compound up to massive improvements. And of course tiny mistakes compound into massive impacts on you returns over time.

As a contrarian, you know that there is a long list of behavioural traps that can force investors into making bad decisions. Are you conscious of those risks?

Just knowing about behavioural finance doesn't absolve you from making those mistakes. In our team we often talk about process over outcome. Outcomes will come if processes are good. So do we have a process that allows us to avoid these kinds of biases? There is a trust element to how Kevin and I work in terms of sharing ideas. But are we too cosy and perhaps a bit afraid to say 'I don't like your idea'? How do you keep that tension to avoid confirmation bias? You have to try and avoid that representativeness heuristic. Having said that, we've all got natural biases and we're only human.

Coming back to the David Brailsford example, you don't have to undo your entire human nature. You have to understand yourself and understand and stick with the style and then mentally suffer. When it's underperforming you don't have a lot of happy people in the team. Mentally, we need to understand ourselves and understand what it is that we do well - but there will always be errors.

What have you learned from the big successes and disappoint-

ments in the Recovery fund over the past 10 years?

I think the failures are more instructive, but we have had some wonderful successes with things that have made us multiples of our invested money. Take housebuilders like Taylor Wimpey. Back in 2009 you couldn't force people into them because the house price fear was real. Housebuilders back then were a great example of people being worried about the economy and house prices did fall in real terms by 15 percent, but Taylor Wimpey went up 400 percent. You don't know it will happen that way but as part of a diversified portfolio, that's why you buy it at that point.

With loss aversion of course, the winners don't stick in your mind like the losses. So you remember the ones that went to zero, the ones where you got wiped out or the horrible capitulations where you were forced to sell in the rescue rights issue at a low level. They're the Wagon Automotives, the Luminars and the Blacks Leisures of this world.

How do those individual disasters affect you?

As a fund manager, high conviction borders on egomania and overconfidence. As a result, the idea that you'd open yourself - Schroders - to being the biggest shareholder in Blacks Leisure when it goes bust, leaves you thinking 'I don't want to be in the papers for that!'

But that is the reason it's attractive. When you get to those levels of distress, the valuation is so extreme because there isn't a fund manager in the world that wants to touch it. With the Recovery fund, that's why we never say never. When you're dealing with that perception of distress you can make extreme amounts of money. Sometimes it's not a sensible bet to take because the risk/reward isn't in your favour, but often they can be very interesting ideas.

Special situations can occur anywhere in the market, but are there places that you won't go with the Recovery fund?

We need a very good reason to go below a £50 million market cap, although if something is very distressed we might look at it. My experience is that below that level there often isn't enough upside to offset things like single-person founder risk, liquidity issues, narrowness of the business and single product companies.

With very small companies you have to be very careful because the risk increases very substantially. People obsess with 'small' because then it can go up a long way. But British American Tobacco was a £5bn company in 2003 before it went up 1,000 percent - a ten bagger. Kevin likes to use the phrase 'deep value hiding in plain sight'.

Having said that, we do believe in the tail and we do believe that we're looking at businesses that are falling very sharply and getting smaller, so we're going to cap the size of the UK Recovery fund at £1 billion - it's around £750m today. The incentive to keep funds open when money is coming in is very high and psychologically you feel like a hero after many years of toil. But taking the decision ahead of time to limit the fund will allow us to continue to access the small-cap end of the market that we think is important.

Finally, when you look at the market today, do you feel optimistic about the value opportunities that you are seeing?

This is not a vintage period for value investors because it's such a narrow market. I look at it like this: what is the average valuation of the things you pick from and then what is value versus growth within that? It's not a great time for average valuations because the US is going through the roof. The UK doesn't look very cheap to us because the averages are being skewed by some big, cheap stocks and some that are very expensive.

Having said that, the stuff that is cheap is despised and is value. When you look at banks, commodity stocks and food and drug retailers, there is no fund manager that wants to touch them. The disparity between what is cheap value and the rest of the market is increasing, so that's a great time for value investors because nobody wants to do it. If you look at the half trillion of unit trusts in the UK invested in equities, less than 9 percent have more than 50 percent in value stocks.

I feel that in this environment that if you can hold the line, the rewards to doing that are increasing. You have to understand that when the market is really on sale again, like in 2009, go big. Be picky, but buy and don't drag your feet too much. Today we're in a different environment where it's not psychologically hard to buy stocks, but it is psychologically hard to buy value stocks. Over the longer term, more difficult choices tend to lead to higher rewards. That bodes well for our deeply out of favour investment style.

Nick, thank you very much for your time.

Build a strategy like Nick Kirrage

Nick Kirrage typically looks for companies that are out of favour and have very low valuations. He prioritises low debt and positive profitability in companies with the potential to recover.

Find out now which shares pass the rules of our Nick Kirrage strategy screen: http://stk.pe/nickkirrage

Keith Ashworth-Lord - How to invest like Warren Buffett

The great US investor Warren Buffett once remarked: *"The highest rates of return I've ever achieved were in the 1950s. I killed the Dow. You ought to see the numbers. But I was investing peanuts then. It's a huge structural advantage not to have a lot of money."*

What Buffett meant was that the more money you have to invest (in his case tens of billions of dollars), the harder it is to make outsized returns. So what would happen if you took the essence of Buffett's strategy and used it on a smaller scale in the UK? Fund manager Keith Ashworth-Lord is finding out.

Ashworth-Lord set up the Sanford DeLand UK Buffettology Fund in 2010. It's a concentrated fund with a strict methodology that's approaching £200 million under management and growing fast. In 2015, it made an impressive 27 percent return in a falling market, propelling it to the top of the IA All Companies sector.

As the fund name suggests, Ashworth-Lord has adopted some of Buffett's best known investing traits. He takes a quality & value approach, looking for 'moat-like' characteristics right across the market-cap range. When he likes what he sees - and he can buy it cheap - he takes high conviction positions and holds them long-term.

Ashworth-Lord runs the fund from his home turf in Manchester, where he's been a fixture in the city's investment community for 35 years. But he's just as well known among US 'Buffettologists', and close friends with the likes of David Clark and Mary Buffett (from whom the eye-catching 'Buffettology' branding is licensed).

He's also written his own book - *Invest in the Best* - where he explores what he calls Business Perspective Investing and the financial clues to finding great quality companies on attractive valuations.

Keith, early on in *Invest in the Best*, you mention that you wrote much of the book on the lanai of your Florida home. That's a pretty big hint that you've found an investing methodology that works very well for you!

Ha! Well I wasn't saying it to show off. The point I was making is that had I not been successful with my investments I'd never have had the wherewithal to buy that house. Lesson number one about investing is that it's nothing more than deferred consumption. You're laying out cash today to get a whole lot more back in the future. With everything I've learnt, it was a very easy book to write. Some people said to me that I was giving away secrets, but my experience in life is that the best place to hide something is in a shop window.

That echoes a lot of what Warren Buffett was saying in his article on the Superinvestors of Graham-and-Doddsville. He was pointing out that investors generally ignore 'value' despite the fact it's been such a successful strategy for so long.

Exactly. People find value investing boring. But you can spare me the excitement because it works. It's interesting that you mention the Superinvestors of Graham-and-Doddsville, because that article was what turned me on to what I'm doing now. It was the mid-1990s and I'd been in this business for 15 years. I'd been head of research at Henry Cooke, head of research at Daiwa in London and worked in various corporate finance roles. But it occurred to me after all those years that I'd really learned very little.

I had no anchor-line to my own investments at all and I realised I needed a more robust investment methodology. In all the reading I was doing, the two books that really caught my eye were *The Intelligent Investor* by Benjamin Graham and *Common Stocks and Uncommon Profits* by Philip Fisher.

The Superinvestors of Graham-and-Doddsville is Appendix 1 of *The Intelligent Investor*. In there, Buffett mentions these guys who had been students of Graham who were battering the S&P year-in year-out. Yet when you looked that their portfolios they contained very different companies. What they had in common was Ben Graham, who was the true north on their investment compass.

So I started to look closer at why they had been such successful investors and gradually I focused on Buffett. He'd been the most successful of all of them. In the mid-1990s, myself and a colleague called Jeremy Utton, who had started a publication called *Analyst*, began going to the Berkshire Hathaway AGMs in Omaha. The first time we went we were fortunate to be mistaken for journalists and managed to get a private meeting with Warren and Charlie Munger, which was great because not many people manage that.

We also got to know all these Buffettologists, people like Roger Lowenstein, Andy Kilpatrick, Larry Cunningham, Janet Lowe, David Clark and Mary Buffett. On Boxing Day 2009, David Clark called me and explained that he and Mary would like to see a fund launched in Europe using the Buffettology methodology, and they wanted me to run it. The call couldn't have been more timely because I'd been running my own money for 10 years using those same principles and it was doing very well. So we cut the deal, launched the fund and away we went.

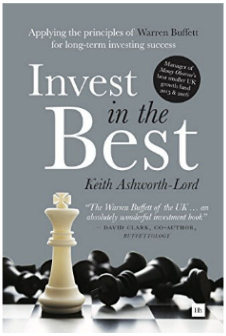
As a value investor, I'm guessing that you see market volatility as an opportunity more than a threat. Is that right?

Absolutely, I was doing cartwheels on the 24th June 2016 - the EU referendum - partly because I think we can do very well outside the EU. Two weeks before the referendum there had been a clutch of polls that Leave would win and the market had dipped as a result. At that stage I topped up some of the bigger stuff in the fund, like Diageo and GlaxoSmithKline.

After the vote I waited to see where the market would settle, and within a few days it looked like we'd seen the worst. By that time the larger companies had shot up but others that I really liked had fallen. Even Domino's Pizza got hammered.

I tend to be a manager who runs with quite a bit of cash so I do like it when markets collapse. Several times with this fund we've seen 10 percent corrections in the market that have come back very quickly, and I took advantage each time. When I sense that I can buy things five percent or 10 percent cheaper than I could yesterday, that to me is what investing is about.

Can you tell me about your investing strategy and how you analyse companies?



There are two sides of my character that make me the investor that I am. The first is discipline and having what I think is a robust methodology and sticking to it religiously. People sometimes say that value investing is out of fashion, but it has never been out of fashion. The second thing is to have patience. That means when you have found something that you really like but you can't buy it at a price that makes sense - there's not enough margin of safety - you need the patience to say 'hold off and wait'.

We put one new business in the portfolio in 2016 and that was Restaurant Group. It had been on the watchlist since day one. Previously it had a fantastic reputation and had done well for many years but it was always selling on a P/E of between 20x and 25x. There was nothing there that suggested value to me but it was always on the watchlist.

We know that Frankie & Benny's is a tired offering and it needs attending to, and that represents more than half the business. So we had the first profit warning in November 2015, and then again in January and April 2016. Broker earning forecasts had been cut by a third by the time of the third profit warning and the de-rating had taken it down to a 10x multiple. That's when I get interested. I didn't rate the management particularly highly but I felt that if they didn't get it right then someone would get it right for them.

I revisited all my forecasts and all my spreadsheets, taking into consideration no growth or perhaps low growth and what private equity might be prepared to pay for it. I was coming up with fair value of between £4-5 per share. The shares had come down from over 700p to 280p, and I felt that was all the margin of safety that I needed. It wasn't going to go bust and that's just the sort of value investment proposition I like.

As Buffett says, wonderful opportunities arise when unusual circumstances surround good businesses. That's how I saw this. I'm not saying it's going to be easy to sort out, but a good manager should be able to sort it out.

The whole idea of using Business Perspective Investing is that you use the methodology to find the company. Only then do you go on to valuation and ask whether you can buy it at a price that makes sense. To me, it's two completely different mental processes - identifying and then buying.

You're an advocate of the Graham and Dodd principle of having a margin of safety. Are there companies out there that you've never actually been able to buy because of that?

As it stands, it's really an all cap portfolio at the moment but I have found that valuation anomalies are easier to find at the smaller and poorly-researched end of the market.

The smaller companies that I've liked I've been able to buy much easier at a price that made sense. A lot of the better researched companies have had to go on a watchlist, because they are all fully priced or worse. Take Unilever and Reckitt Benckiser - I would like to own those businesses but I'm not paying anything like the current prices for them. In my judgement they are overvalued.

You talk about having a circle of competence that's a foot wide and a mile deep. For that reason you run quite a concentrated portfolio. What are your views on the need for diversification and the risks of too much correlation?

I have always said that I would never take this portfolio to more than 35 companies because after that it becomes a zoo. The key thing is that I want to feel that I know as much, or more, about the companies I own as anyone else does. For that reason, I'm never going to have a massive portfolio of holdings.

I think 30 companies in a portfolio is more than adequate diversification. Obviously you then get questions about correlation. But look at my financial companies - how are Hargreaves Lansdown, which is business-to-consumer, and Mattioli Woods, which is business-to-business, correlated? They are totally different businesses.

The same goes for Restaurant Group and Domino's Pizza. Are they correlated? No, they're uncorrelated. In times when eating out is off the menu, ordering from Domino's is on the menu, and vice versa.

My support services groups have got nothing in common with each other, either. You've got RWS, which does patent translation, Lavendon, which does plant hire, and Driver Group, which does consultancy. They are completely different businesses with completely different dynamics and revenue models.

You have a very strong focus on good quality, strong cash flows and sustainable growth, whether it's in a mega-cap or a micro-cap. They range from the likes of AB Dynamics and Bioventix

to Diageo. What do you see in those smaller companies?

I met the team at AB Dynamics 14 months before I invested in it. I'd done a lot of work on it in the intervening period and really kicked the tyres. Right from the off it reminded me of a company from the past called First Technology. Often I'll see things that remind me of something else, which is what happens when you've been around donkey's years!

First Technology made crash-test-dummies and it was doing wonderfully well before it bought another company that eventually dragged the whole thing down. Before that, the core business had the same strong relationship with automotive manufacturers that AB Dynamics has. When I first bought into it, AB Dynamics was sub-£50m, and it's gone on to be a wonderful kicker for our performance.

But in the case of Bioventix, I'd never even heard of it because it had come to AIM from ISDX. I met them at an investor conference and it sounded a lot like Abcam in the early days, which is a fantastic business.

I did the financials and was coming away with a return on equity of 46 percent, the entirety of profits converting to free cash and absolutely no need for capital at all. So it was a 90 percent gross margin business and revenues nailed on for the next five years and cash on its balance sheet. I couldn't believe it, so within the space of six weeks of knowing they existed, I'd invested in it.

So there are businesses out there with barriers, or moats. There are around 3,000 companies listed across the FTSE and AIM and I see most of them as uninvestable. At any one time, there might only be 50 or 60 that I think are worth investing in. It's just a case of drilling down and finding things. And it does mean doing a lot of work that never sees the light of day.

I've never regretted doing the work on a company and then turning the page on it. But there have been moments when I've regretted not having the time to follow up a suggestion that has turned out right.

You're looking for instances of mispricing in the market, but everyone makes mistakes. How do you deal with the disappointments?

I don't have regrets because if you get something wrong you have to try and learn from it. There are two sorts of things that go wrong. The first is that the story changes - something happens to the management or the industry or some sort of disruptive technology comes along. Suddenly, it's not what you thought it was and it's time to say goodbye. I've seen instances where the story has changed, and it has happened with companies like Homeserve, and a small company of consultants called Sweett Group.

Then there have been episodes that were all my fault. The first was Tesco, which I invested in the summer of 2013. Three months later, the very first trading statement said they were going to reinvest extra returns back into margins. In other words they were having to cut their prices to compete with Aldi and Lidl. The whole investment thesis was blown to smithereens, so that had to go.

What I learnt from that was to never try and anticipate a turnaround, always wait for it to start. The key in circumstances where you've got it wrong is to admit it, rectify it and then try and learn from it.

Clearly, you very much take a buy-and-hold approach with your fund. But under what conditions do you consider selling positions?

Of the first 20 businesses that we put into the portfolio, 16 are still in there. We've never made a sale from the fund on valuation grounds because I prefer to stick with things. There are so few great companies that when I've got one I prefer to stay with it.

Apart from when the story changes, the other time where we've chosen to sell was a switch situation. I'm very wary of switch situations because if you've owned a company for a long time you almost get a sixth sense about it. The risk is that you end up selling old gold for gilded plastic.

Right from the start of the fund I wanted to own Dechra Pharmaceuticals because I've known that business since the turn of the millennium. Bear in mind that animal pharma is nothing like R&D, it's more like 'D' because it's often taking drugs that are already proven in humans. So it's not blue-sky.

The first opportunity I got was in the middle of 2012 but the fund was fully invested, so I took the decision to sell AstraZeneca. The fact that they were both pharma companies was just happenstance. I took the decision because we'd had some great performance out of AstraZeneca but I felt its pipeline was a bit weak. So I sold one to buy the other, and it has turned out to be a good decision.

The worst possible reason to sell a position is to crystallise a profit. By all means sell it if you got it wrong or something has changed. But if something is winning for you, stick with it. My experience has always been that the winners produce the nice surprises and carry on winning. But with losers you seldom gain back what you lost.

Keith, thank you very much for your time.

Build a strategy like Keith Ashworth-Lord

Keith Ashworth-Lord typically looks for high quality companies with a track record of strong profitability. They should have high growth potential but the shares must be reasonably priced.

Find out now which shares pass the rules of our Keith Ashworth-Lord strategy screen: http://stk.pe/keithashworthlord

Mark Minervini - Achieve superperformance like a stock market wizard

When you're trying to interview a man with a deadline to write a book, finding a convenient time isn't easy. When that man is Mark Minervini, whose hectic days were split between trading and finishing his hotly-awaited new investing guide – *Think and Trade Like a Champion* – the pressure's even worse. When I finally managed to catch him - after the market close in New York - he was generous with both his time and his views.

For more than three decades, books have played an important part in cementing Minervini's reputation as one of America's most closely-watched traders. 2017 saw the follow up to his popular guide, *Trade Like a Stock Market Wizard: How to Achieve Super Performance in Stocks in Any Market.* That was written 10 years after he was profiled in Jack Schwager's hugely popular *Stock Market Wizards.*

So what's his appeal? Minervini started trading with very little capital in the early 1980s. After several years of losses, he took his strategy back to basics and got scientific with what was working, and what wasn't. It was a turning point that transformed his results.

In 1997 he was named U.S. Investing Champion after smashing the contest with a gain of 155 percent. It served to prove the effectiveness of his strategy even under the most competitive conditions. Since then, he's won a huge following and built an education business on the back of it.

In essence, Minervini is a growth investor. He made his name shooting for big gains in fast moving stocks with a strategy that blends fundamentals, technicals and strict risk management. The process is carefully laid out in his first book, with a particular focus on getting the timing of trades absolutely right.

But what comes across when speaking to him is that the precise strategy is very much a personal decision. What's more important is the belief and mindset to stick with it, and an unswerving discipline to avoid big losses.

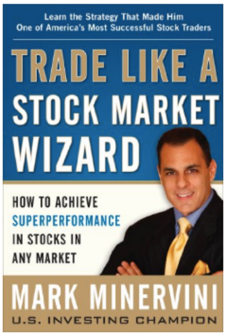
Mark, tell me about how you've evolved and developed your strategy over time?

My strategy developed very simply because I had a small amount of money and I wanted to turn it into a large amount of money. So I had to find a way to trade the markets and be able to very rapidly compound my capital.

In the beginning I couldn't do short-term trading or swing trading like you can nowadays. Back then, commissions were more than $175 per trade. With a small account back in the early 1980s, with a few thousand dollars, I couldn't pay that much commission trading in and out. You had to pick up the phone and call your broker, and he called someone that called someone else on the floor, and it was a much lengthier process to make a trade.

Back then we would look for big moves in stocks. But now you can trade for pennies and have instant liquidity so there is a lot more in-and-out trading, swing trading and day trading. Over the years I've refined it more and more to the point where I've got down to pretty much a science. It's still an art, but the science takes out as much guesswork as possible.

Your strategy is very much focused on growth companies. In terms of fundamentals, what sort of profile are you looking for in a stock?



My books spell everything out much better than I can explain in a brief interview, but from the fundamentals side, if you're investing in growth companies you're obviously looking for signs of growth. It doesn't necessarily mean that just because a company is showing decent earnings, say earnings are up 30 percent over the past few quarters, it's attractive. It's really a matter of asking whether it's doing better than it was previously.

For instance, if you have a company that's growing at 30 percent annually, but prior to that it was growing at 80 percent or 90 percent, that's not very good because the growth has slowed. That's what you saw at Dell Computer in the 1990s. Dell was growing at a rapid rate but it decelerated towards the end of the decade and the stock topped.

But if you take a stock that was previously losing money but is now growing at 10 percent or 15 percent, that's a big improvement from where it was. That could actually do better than a stock with a higher growth rate that's actually slowing down.

Sometimes that confuses people, but it's really the change in growth rate that you're looking for. Wall Street likes it when things are going better than expected, and when a company suddenly shows that its growth is accelerating faster than anticipated.

So I'm looking for big quarterly earnings growth. But sometimes you'll get big fundamental changes that aren't apparent in the earnings. Maybe you'll have a company that has got approval for a new drug and you might not see it in the earnings. So it depends on the situation and the category a company falls in to.

I treat various industries and different types of companies differently. That's why I break it down into four or five basic categories. You have Market Leaders, Top Competitors, Institutional Favorites and Turnaround situations. Those are the four that I usually concentrate mostly on. Then you have Cyclical stocks, which I tend to avoid, and anything involving mergers I tend to avoid most of the time as well.

What advice do you have for investors when it comes to honing a strategy and developing a trading style?

One of the problems for the average investor, particularly for those that are new to trading, is that there is so much information out there; information overload is common. There is more than one way to skin a cat, and my way isn't the only way. It just happens to be the way that I know really well, and I've focused on for so many years that I'm good at it.

You can have a value player buying stocks that I wouldn't touch, and they do very well. Whereas I'm buying growth stocks with P/E ratios that are higher than a value investor would ever think of buying, but we can both do well. The key is to really know your strategy.

But you have to narrow it down and come up with something that makes sense to you and then commit to it. You're not going to be good at a lot of different strategies. You have to make a commitment to one area and spend time learning it so you become really good at it, rather than just dabbling with different styles. You want to be a specialist, not a jack-of-all-trades.

If you're going to day trade, that's a lot different from being a long-term investor. There are going to be different rules to follow - but it's important to have a set of rules and a process.

It took me a lot of years of course, being successful didn't happen overnight. I didn't do very well for almost six years but over time it started to click for me. Nowadays you have access to information that can help shorten the learning curve. When I first started trading, I had to go to the library. I was reading books that were old and outdated, and it wasn't as easy to get access to good information like it is today.

The investment environment has changed a lot since you started trading. Do you still believe that individual investors have an edge despite new developments like algorithm-driven, high-speed trading?

Absolutely! If you'd asked the average investor in 1930 if it was too complicated and whether the big, rich investors and institutions had the edge, they'd have said yes. If you'd asked them in 1950, 1980, 1990 it would always be the case. It's always the case that people feel it's a rigged game and that the big guys have the edge. Actually, it's quite the opposite; the big guys don't have the edge. They have a handicap because they have to move big amounts of money and their process is very slow and lethargic.

The individual investor can move very quickly and has a huge advantage. The smaller you are and the smaller your portfolio, the bigger advantage you have. Nowadays, you also have the exact same tools as almost any professional. You have access to the same information, and laws have been changed to level the playing field as far as the information flow. All your tools, your quotes, your execution are as good as anybody else's. So it's a great time to be a stock trader and it's going to just get better and better.

Your approach has some of the hallmarks of other trading legends like Jesse Livermore and Stan Weinstein. Who have been the big inspirations in your trading, and what have you learned from them?

I met Stan Weinstein back in 1990 at a big investment event in New York City. He was a very colorful, fun guy and he really impressed me with his passion for the market. That's when I began to fold-in the trend work. It really got crystallized for me after I met Stan.

One of my biggest influences early on was Richard Love. He wrote a book called *Superperformance Stocks*. Richard Love and William Jiler are the two who really are the backbone of the fundamentals side and the technicals side. Jesse Livermore would also be one of my big influences. I would say that I am a modern version of those four traders and I've combined and refined the best of each.

Paul Tudor Jones is also someone who I modelled a lot of my trading after, particularly on the risk management side. As commissions came down and I was able to trade quicker and cheaper, I started applying the types of rules that futures traders were using. That meant being much more aggressive with trading stocks, and taking a more mathematical approach and mitigating the risk quickly like if I were a highly-leveraged futures speculator.

Risk management is clearly a major part of your strategy, and particularly cutting losses early. Where do most traders go wrong with this, and why?

Most traders go wrong because they usually don't have a good strategy to begin with. For most, their egos are more important than making money, and they don't figure out how to differentiate the two. When a stock goes down, they don't want to be wrong so they wait until it comes back. The loss gets worse and before you know it, a big chunk of your capital is gone. They hit what we call the 'uncle point' where your arm is twisted so far that you can't take the pain any more. Do that enough times and you start thinking about throwing in the towel; and when your confidence is damaged, then you're doomed.

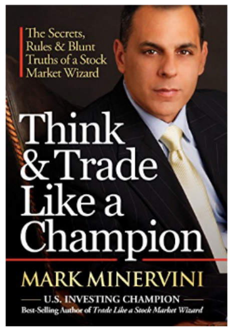
Maybe then they'll read a book like mine and decide that cutting losses sounds like a good idea. They try it, the stock goes down and they sell it and then it turns around and goes back up and takes off and they think: "my god, I'll never do that again, that was stupid".

So you have to realise that you're not going to be right all the time, in fact you'll likely be correct only about 50 percent of the time. You have to manage the risk, that's the most important thing. There is a lot of risk in trading stocks. All stocks are risky and that has to be managed. The goal of stock trading is to make more money on your winners than you lose on your losers - it's not to be right all the time.

For some, it takes a while to shift their thinking, but you have to focus on avoiding big losses by embracing smaller losses.

Selling at a small loss is one challenge, but knowing when to sell for a profit is another difficult subject. What's your advice on how to run winners and how and when to exit a successful trade?

In my new book what I've done is to try and cover all the things I didn't cover in the first book because I ran out of room! It covers all my rules and the types of things that you should look for when it comes to deciding whether you should hold the stock longer for a larger move. But also when you should reduce or sell the stock even before it hits your stop loss. There's a whole chapter on selling and a chapter on what I call "violations".



The main thing is that you have to have rules. Without them you're just going to be operating from your emotions, your hunches and the seat of your pants. It's never going to turn out good when you do it that way. So those rules should be based on a sound philosophy, which means sacrificing. Let's say you are going to be a swing trader for instance, and you buy a stock at 20 and it goes to 30 and you sell it. If the stock takes off and triples you can't be upset that you weren't in it because you already accomplished your goal.

Take day trading as another example. A day trader goes flat to cash every night and is out of the market. They'll go in there and scalp the stock for sometimes a few pennies, or a nickel or a dime or half a dollar. They're not getting upset when they sell the stock and take 50 cents profit on it if the next day it gaps up 5 points. It's not part of their business plan.

It's the same thing if you're a long-term investor and you buy a stock at 20 and it goes up to 25. You're trying to play it for a much bigger move and it comes back down and stops you out at 18 or 19 dollars. Now you're a Monday morning quarterback and thinking you should have sold it at 25. Again, if you're playing for a larger move, you're going to have to sacrifice the shorter move. If you're going to play for the shorter move, you're going to sacrifice the larger move.

You must define your trading. You have to learn to sacrifice and focus on a particular style, which is all based on having a framework that you operate in. The whole idea of this scientific approach is to remove as much of the emotion and as much of the luck factor.

There are still going to be intuitive decisions to be made: What to buy? When to buy? How much to buy? When to sell? There are always decisions to be made and you're never going to be truly scientific, it's still going to be an art. But that's the beauty of it. If it was purely scientific then you'd be able to put it into an Excel spreadsheet or computer program and let it run, and humans wouldn't be needed and the edge would be gone. But that's the beauty about trading, there's an art to it. That's the challenging part but it's also what makes it so rewarding.

What was your best trading year, and what was your performance?

One standout year was 1995, when I was up 412 percent, the 1990s were good, of course. I was out in 2000 and came back in 2004 and had some big triple digit years. Since then I've done very well and been very consistent. I haven't had any down years in perhaps 20 years. Early on, I had a lot of volatile periods when I'd do well and then blow myself up in a few months of bad trading. These days I trade more conservatively and without my whole net worth on the line as I did in my initial years when I was trying to build my capital.

When you look back, is there anything the stands out as being

a key moment in your trading?

As far as any one trade, not really, because I've traded hundreds and hundreds of thousands of stocks and it's not like I had one big winner that accounted for my success. My returns have really been produced through consistency and a lot of trading year after year.

When I look back in time, back in the 1980s and early 1990s I was more of an investor holding for larger moves out of pure necessity. As a result, I got some really big movers. The names that I was buying back then, if you look at them today you'd say "oh, of course" - Amgen, Dell Computer, Microsoft, Costco, Home Depot, Gap Stores, etc. But at the time few investors had even heard of those companies, they were all small-cap, underfollowed names. After that, it became sort of a blur because it was a lot of trading and the stocks just became symbols that I was trading on a daily or weekly basis.

Over time, how have your ambitions and the focus in your life changed?

I've come to realize that my calling hasn't just been trading but it is also helping others. My editor told me I was a natural born teacher. I didn't realize it was something I was good at and it wasn't really something I planned on doing.

Back in the late 1990s I got in the public eye after winning the U.S. Investing Championship and I was on TV a lot. As a result, I was offered a lot of money by publishers to write a book, but I didn't because I didn't want to give away the "secret". I was advising some very big institutions and I never saw myself dealing with individual investors or having a retail product or doing seminars. To me, I was a just a trader and I wanted to avoid all that. The reasons why I started trading in the first place was that I could be in a room by myself and be responsible for my own success.

But that all changed as I started thinking about passing the torch. When I wrote my first book I was not sure if anyone would even like it. Then I did a seminar and that turned into a big success and I've been doing it ever since. So it feels like my ultimate calling is to be an educator; it feels really good when people tell me that I've helped them improve their lives.

One of the things that I always tell stock traders is that while you can read about the mechanics behind the big returns from superstars, it's probably not going to get you the same sort of success unless you feel that you can do it and it's possible and you believe in your own abilities.

A big part of me writing a book and doing workshops is to empower people to help them understand that not only can they do what I have done, but with the benefit of my knowledge, they can do even bigger and better than what I've done. Ultimately, a belief in your own abilities is more important than the strategy.

Mark, thank you very much for your time.

Build a strategy like Mark Minervini

Mark Minervini is focused on fast growing companies. Before looking at technical analysis, he screens the market for companies with recent earnings accelerations and that are beating expectations.

Find out now which shares pass the rules of our Mark Minervini strategy screen: http://stk.pe/markminervini

Seven rules for successful investing

One of the striking themes that emerged from talking to the investors in this book was how each of them had made a success of very different investment styles and strategies. But while they each of them had absolute conviction in the strength of their own approaches, they also accepted that different strategies suit different investors - and they can all work well.

Each of the eight investors has a set of rules that guides them towards stocks with the particular investment profiles they are interested in. They each use specific entry and exit rules that they've honed over time. Some invest solely in large-caps, while others swear by the growth potential of small-caps. Some prefer concentrated, high conviction portfolios, while others spread the risk of loss by holding many positions. But while their approaches all differ, they also share some common views...

1. Individual investors have an advantage

Unsurprisingly, the individual investors in the series felt strongly that private traders have an edge over the managers of large funds. Mark Minervini insisted that individuals investors have a huge advantage in being able to move quickly. And the smaller the investor's portfolio, the bigger advantage they have.

Equally, Lord Lee suggested that individuals should resist giving their money to professional fund managers and instead back their own judgement in the stock market. He said there are only two things needed for successful investment: patience and common sense.

2. A strategy is essential

One of the overarching themes that emerged from the interviews is how important it is to have a strategy, whatever form it takes. Despite their differences, all of the strategies focused on two or more of the most powerful drivers of stock market returns: the ***quality*** of a company and its financial profile, whether its shares are good ***value*** and the strength of the ***momentum*** in its earnings and share price.

A carefully crafted set of rules not only helps to focus them on what they believe is important in a stock, it also gives them resilience when times get tough.

All of them conceded that there were times when their strategies wouldn't work. This is arguably one of the biggest pain points for individual investors in the stock market. So the ability to take confidence from a sound underlying strategy (and the knowledge that it will bounce back from periods of underperformance) is essential.

3. Keep it simple

One of the striking messages about investing from Robbie Burns and Minervini was to keep things simple. Both investors claimed that the outside world seemed to think their systems and strategies were far more complicated than they really were.

Burns took pride in showing me just how simple his set-up was, with just one monitor and a few open tabs. He was also insistent that he didn't trade very often, noting that when in doubt about a situation, it's generally better to just do nothing.

For Minervini, the tendency for investors to flit between strategies is a big risk. He advised that individuals should make a commitment to one discipline and then spend time learning it thoroughly and become expert at it, rather than just dabbling with different styles.

That view was echoed by Mark Slater, who believes that a firm strategy is essential. He said that having a methodology was essential, otherwise there's a risk that investing just becomes punting.

4. Beware of yourself

Emotions and psychology were recurring themes during the interviews. Burns was adamant about the perils of confirmation bias, while Slater warned of the risks of price anchoring.

As a deep value investor, Nick Kirrage faces the classic challenges of buying potentially troubled stocks. But he relishes the fact that his strategy requires him to be mentally tough. He said that psychologically, it means signing up to, and fully embracing, a set of criteria.

For Giles Hargreave, one of the biggest errors is to sell a good stock too soon. He says the temptation to snatch a profit should be resisted at all costs. And while he insisted that he only rarely falls into that trap, it makes him fell sick whenever he does.

One of the best summaries was offered by Minervini, who was clear about the need for personal discipline. He said the main thing needed is a set of rules, without which you're going to be operating from your emotions, your hunches and the seat of your pants.

5. Cut your losers fast

There was universal agreement that selling losing positions is essential. Keith Ashworth-Lord said that the key in circumstances where you've got it wrong is to admit it, rectify it and then try and learn from it.

Slater went as far as saying that the process of selling a poor performer was liberating for him. He said that cutting a loss was often extremely cathartic because it ends the pain and means you can divert cash into something better.

Hargreave said that while he gets more right than wrong, he's quick to get rid of holdings when they do go wrong. He said it's important to cut losers and run winners and maximise the good ones.

Minervini's view is that investors need to manage the risk that they'll likely be correct only about 50 percent of the time. He said the goal of stock trading is to make more money on your winners than you lose on your losers.

6. Manage taxes carefully

For the UK based individual investors - Burns and Lord Lee - tax efficient wrappers have been crucial to their long-term success. In particular, they both stress the importance of Individual Savings Accounts (ISAs), which shelter invested funds from capital gains and income taxes.

Back in 2003 Lord Lee became one of the UK's first ISA millionaires and, for him, the wrapper can have a huge impact. He said the compounding effect of reinvested dividends in an ISA can have a massive impact over a period of time.

7. Portfolio management is crucial

Not all of the portfolio management strategies explored in the interviews are realistic for individual investors. After all, with more than 200 positions, Hargreave's Special Situations fund is very widely diversified. But an important feature of his approach is his focus on buying the best quality companies that he can find. He starts by buying relatively small stakes and the builds them up gradually as he becomes more familiar with them.

By contrast, Ashworth-Lord conducts detailed research up front, long before actually buying a stock. And when he does finally buy it, he monitors it carefully. With high conviction in his holdings, he believes that 30 companies in a portfolio is more than adequate diversification. This is exactly what you'd expect from a fund that echoes the approach of Warren Buffett.

The use of stop-losses was another recurring theme in the interviews. While automatic stops are not used by fund managers, all three private investors think they are a good idea. For Lord Lee, stops have been a tool that he's applied only latterly in his investment career. But for Minervini, they are central to his strategy.

For Burns, his use of stop losses has changed over time, but he still sees them as important. He uses stop-losses as an emergency exit, just in case something terrible happens. But on a new trade he is much more likely to close the position very quickly if it begins to fall in price.

Creating your own investment framework

The key lesson from the investors in this book is how important it is to develop a personal investment strategy. Whether it's deep value, fast growth and momentum or high quality (or a combination of all three), building a personal investing framework is essential. With a strategy, it's easier to have the confidence and discipline to invest in good times and bad.

But building a strategy doesn't necessarily happen overnight. Another shared view from the eight investors was that investing is a lifelong pursuit that benefits from constant improvement. In fact, they all agreed that making mistakes, and learning from them, had helped shape not just their strategies, but their resilience and discipline in facing future challenges. For those of us looking on, those experiences provide some valuable lessons about what it really takes to profit from the stock market over the long term.