Beating The Street

Peter Lynch

The Miracle of St. Agnes

(Chapter appears to be a rationalization that stock picking works)

p.23 75% of mutual funds fail to perform as well as market averages

p.26 St. Agnes portfolio build by seventh-graders outperformed the S&P 500 and most fund managers for the two years 1990-1991

p.27 Keep it simple: "Never invest in any idea you can't illustrate with a crayon." (Peter's Principle #3)

The Weekend Worrier

p.36 "The key to making money in stocks is not to get scared out of them."

"The person who never bothers to think about the economy, blithely ignores the condition of the market, and invests on a regular schedule is better off than the person who studies and tries to time his investments, getting into stocks when feels confident and out when he feels queasy."

p.44 "Moreover, if you had paid close attention ot the negative tone of most of our "whither the economy" sessions over the past six years, you would have been scared out of your stocks during the strongest leg of the greatest market advance in modern history, when investors who maintained their blissful ignorance of the world coming to an end were merrily tripling or quadrupling their money."

"The best way not to be scared out of stocks is to buy them on a regular schedule, month in and month out..."

p.45 Have conviction about the long run: "Faith that America will survive, that people will continue to get up in the morning and put their pants on one leg at a time, and that the corporations that make the pants will turn a profit for shareholders."

A Tour Of The Fund House

p.48 Instead of choosing stocks, we now have to choose mutual funds

p.49 Lynch favors stocks over bonds

"The reason that stocks do better than bonds is not hard to fathom. As companies grow larger and more profitable, their stockholders share in the increased profits. The dividends are raised."

p.50 Companies will raise dividends, but never raise the interest rate on their bonds

p.51 Allocate as much towards stocks as you can tolerate

p.57 Bonds vs. bond funds: just buy actual bond issues and bypass the fund fees

Reference to a study where individual bonds outperformed bond funds

p.59 Reference to the number of active managers that underperform

"The fact that so many funds with investments in the stocks that make up the averages can manage to do worse than the averages is a modern paradox."

Some potential causes for why active managers underperform

p.60 Active managers have a very difficult time beating the market

"All the time and effort that people devote to picking the right fund, the hot hand, the great manager, have in most cases led to no advantage."

p.62 Magellan was a capital appreciation fund, meaning it could buy any securities that the manager wanted and wasn't constrained to any philosophy or style

p.64 Advocates using a mix of index funds and actively managed funds

p.68 Using past performance as an indicator of future performance is futile
p.69 Index funds have a major advantage in that their fees are lower
p.72 Convertible funds and convertible bonds: bonds that pay a small coupon, but can be converted into stock at a pre-determined conversion price
p.73 Closed-end funds
p.74 International stock
p.76 Difficult to find European companies that consistently increase earnings (compared to American companies)
p.77 Overvalued Japanese market

Managing Magellan The Early Years

p.84 Lynch inherited the Magellan Fund in 1977, but it wasn't open to new investors until 1981. The shutdown wasn't done to accumulate performance, but because there were no interested buyers
p.87 Original goal of the Magellan Fund:
"The goal of Magellan Fund is capital appreciation through investing in relatively attractive common stocks found primarily in five categories: small and medium-sized growth companies, companies whose prospects are improving, depressed cyclicals, high yielding and growing dividend payers, and finally companies where the market has overlooked or underestimated the real value of the firm's assets...at some point in the future, foreign stocks could represent a substantial portion of the fund."
p.88 "...if it's sold on a stock exchange, we'll buy it."
"Rather than being constantly on the defensive, buying stocks and then thinking of new excuses for holding on to them if they weren't doing well (a great deal of energy on Wall Street is still devoted to the art of concocting excuses), I tried to stay on the offensive, searching for better opportunities in companies that were more undervalued than the ones I'd chosen."
p.89 Turnover was over 300% for the first 4 years of tenure
p.100 "My top 10 stocks in 1978 had p/e ratios of between 4 and 6, and in 1979, of between 3 and 5. When stocks in good companies are selling at 3-6 times earnings, the stockpicker can hardly lose."

Magellan The Middle Years

p.102 "The earliest version of the Quotron required that you type in a stock symbol and push the enter button before the current price would appear. Otherwise, the screen was blank. Later versions, which you've probably seen, display an entire portfolio and the prices for all the stocks, which are updated automatically as the day's trading progresses. The blank screen was a better system because you couldn't stare at it all day and watch your stocks go up and down, as many contemporary fund managers do. When I got a newfangled Quotron, I had to turn it off because it was too exciting."
THOUGHT: Lynch managing the noise of media by turning off the Quotron
"It was fun to buy and sell, but I would have been better off using the extra 50 minutes to call two more companies. This one of the keys to successful investing: focus on the companies, not on the stocks."
p.104 Fidelity had fund managers do their own research instead of relying on analysts. Fund managers could not blame a third party for their failures
p.105 Swapping info and ideas with colleagues
p.107 Turnover dropped from 300% to 110% when Magellan was made available to the public
p.108 "From watching the ups and downs of the various industries, I learned that whereas it was possible to make two to five times our money in cyclicals and undervalued situations

p.109 "Pep Boys, Seven Oaks, Chart House, Telecredit, Cooper Tire--now I was beginning to see that some of my favorite stocks did have something in common. These were companies with strong balance sheets and favorable prospects but most portfolio managers wouldn't dare buy them. As I've mentioned before, a portfolio manager who cares about job security tends to gravitate toward acceptable holdings such as IBM, and to avoid offbeat enterprises like Seven Oaks, the aforementioned servicer with a plant in Mexico."

p.110 Bought T-Bonds in 1982 because the yield exceeded expected returns on stocks

p.114 From his appearance on Lou Rukeyser's Wall Street Week:
"Instead, I said that I divided the Magellan portfolio into two parts: the small-growth and cyclical stocks, and the conservative stocks. "When the market heads lower, I sell the conservative stocks and add to the others. When the market picks up, I sell some of the winners from the growth stocks and cyclical stocks and add to the conservative stocks." Any resemblance between my actual strategy and this attempt to explain it to 8 million viewers on the spur of the moment is purely coinciddental."

p.115 "One of the many ironies of my career is that when Magellan was a small fund I concentrated on bigger stocks, and when it became a bigger fund I found myself concentrating on the smaller stocks."
"Bargains are the holy grail of the true stockpicker."
"We see the latest correction not as a disaster, but as an opportunity to acquire more shares at low prices."

Magellan The Later Years

p.116 Magellan at one point had close to 900 stocks, and Lynch was accused of being the largest closet indexer ever

p.120 Huge gains in a few huge positions made Magellan profitable

p.122 Magellan held about 10 to 20 percent of assets in foreign stocks

p.132 Magellan was more volatile than average stock
"Perphaps there's some poetic justice in the fact that the stocks that take you the farthest in the long run give you the most bumps and bruises along the way."

p.135 Top returning stocks for Magellan Fund: Fannie Mae, Ford, Philip Morris, MCI, Volvo and General Electric
"Although I couldn't possibly have bought enough shares in a small company to have it affect Magellan's bottom line, 90 to 100 of them put together could and did make a difference."

p.136 Small company stocks that contributed to returns: Rogers Communications, Telephone and Data Systems, Envirodyne Industries, Cherokee Group and King World Productions

Art, Science, And Legwork

p.147 The January effect, buying stocks from the low list during tax-selling season in November and December and holding them through January, is especially powerful with small companies

Peter's Princples

1. When the operas outnumber the football games three to zero, you know there is something wrong with your life. (p. 7)
2. Gentlemen who prefer bonds don't know what they're missing. (p. 16)
3. Never invest in any idea you can't illustrate with a crayon. (p. 27)
4. You can't see the future through a rearview mirror. (p. 41)
5. There's no point paying Yo-Yo Ma to play a radio. (p. 58)

6. As long as you're picking a fund, you might as well pick a good one. (p. 59)
7. The extravagance of any corporate office is directly proportional to management's reluctance to reward the shareholders. (p. 86)
8. When yields on long-term government bonds exceed the dividend yield of the S&P 500 by 6 percent or more, sell you stocks and buy bonds. (p. 110)
9. Not all common stocks are equally common. (p. 117)
10. Never look back when you're driving on the autobahn. (p. 127)
11. The best stock to buy may be the one you already own. (p. 129)
12. A sure cure for taking a stock for granted is a big drop in the price. (p. 131)
13. Never bet on a comeback while they're playing "Taps." (p. 138)
14. If you like the store, chances are you'll love the stock. (p. 152)
15. When insiders are buying, it's a good sign--unless they happen to be New England bankers. (p. 169)
16. In business, competition is never as healthy as total domination. (p. 182)
17. All else being equal, invest in the company with the fewest color photographs in the annual report. (p. 190)
18. When even the analysts are bored, it's time to start buying. (p. 200)
19. Unless you're a short seller or a poet looking for a wealthy spouse, it never pays to be pessimistic. (p. 234)
20. Corporations, like people, change their names for one of two reasons: either they've gotten married, or they've been involved in some fiasco that they hope the public will forget. (p. 246)
21. Whatever the queen is selling, buy it. (p. 257)