It Just Takes a Few Small Steps To Start

Follow Those Stocks You Bought

by Kenneth S. Janke, Sr.

There are times when a stock is purchased and everything seems to go wrong. With the benefit of hindsight, it becomes clear that a mistake has been made. None of us like to admit to making investment mistakes, but it does happen on occasion. That's a part of investing.

One of the problems I have seen, especially among members in an investment club, is that no one, especially the person who recommended the stock initially, wants to admit that an error in judgment may have occurred. The company may be facing all kinds of problems, yet the partner who presented it may still be inclined to support the investment and paint a rosy picture.

In many investment clubs, the person who originally presents a stock as a potential investment often is expected to follow it and make periodic reports on the company and its performance at subsequent meetings. The problem is that there may be a bias in those reports. Not wanting to admit to a mistake can result in defending the stock, even if the company's fundamentals appear to be changing, or in some cases even if it teeters on the brink of bankruptcy.

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One of the suggestions I make to investment clubs is to immediately assign the stock to a member other than the one who made the original study. It has been my experience that more information and viewpoints will be presented to the club this way. In addition, the member who originally presented the stock will probably follow it as well, resulting in at least two members having a strong interest in the stock. It's always good to have more than one perspective.

Role of Portfolio Manager

The role of the vice president, or assistant presiding partner, can be to serve as the portfolio manager. That doesn't mean the vice president has to follow all of the stocks, rather that he or she has the responsibility to assign stocks to different members and make sure reports are made. In the Mutual Investment Club of Detroit, the vice president schedules the updates of studies each month, with the assignments appearing in the minutes that are distributed to every member. A new Stock Selection Guide study is required by the member following the stock, so the discussion goes beyond product information and "stories" about the company. What I particularly like about this system is that assignments are made on a rotational basis — three stocks per meeting, with the next three members on the club roster (going alphabetically) getting the assignment.

Beginning investment clubs may have a tendency to buy a new stock every month and after two years of operation, hold up to 20 different issues. It's not uncommon to see that the largest holding is 15 shares of one stock. It is understandable that a new investment club wants to study a different industry every month and to learn as much as possible. I'm not against that, because investment clubs are a wonderful learning experience. Still, building a significant position in stocks held should also be a goal. I have recommended that new clubs adopt a policy of reviewing the portfolio every three months. No new stocks are presented at the review meetings. At those meetings, which can be scheduled to coincide with releases of quarterly figures, the club has an opportunity to add to holdings that appear to be in the "buy" zone. The result is a more manageable portfolio size and a meaningful number of shares held.

Part of the argument for buying so many new stocks is diversification. Just because Value Line lists 89 separate industries, doesn't mean a portfolio has to have that many different stocks to attain diversification. While there are several views on what determines proper diversification, most seasoned investors would agree that having 12 to 15 well-chosen stocks in a portfolio can go a long way in spreading risk.

Of course, there's a great deal more to portfolio management. But perhaps these ideas can serve as helpful hints to put more portfolio management into your monthly meetings.

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