

Introduction

129 business models

'Between every individual and his tomorrow a veil is drawn. There are ways by which this veil can be penetrated to some extent.'

Laurence Sloan, author of *Everyman and his Common Stocks*.

Mankind has three main goals in life: seeing the future, amassing wealth and living forever. They are recurring themes in novels and films, as well as in people's private lives and thoughts. This book occupies the space of the first two of these, as it should enable an investor to see the future performance of a company and, in doing so, increase his wealth. Living forever is left to others.

This book is different from other investment books because it breaks new ground by assessing the business models of companies and sectors. It provides critical tools that enable an investor to assess whether a company's business model leads to strong competitive advantage and if it is in a sector that, in turn, also has strong competitive advantage. It casts a keen eye on the economic cycle, the ultimate arbiter of an investor's success or failure. Other important tools are growth at a reasonable price, technical analysis, scuttlebutting, accounting for growth and investment axioms. The 129 business models are used to analyse companies and sectors. For example, a company may be in a favourable sector but has frittered away this tailwind through incompetence. Likewise, it may be superbly run and very profitable in spite of being in a dreary sector. These tools are designed to unearth the very best companies to outperform in a bull market. They should also thrive in a bear market and minimise the chance of a profit warning. Thus, the investor has a real advantage over those who lack this knowledge.

Summary of this book

The first four chapters are the most important.

Chapter 1. Business models: investing in companies with strong competitive advantage

This chapter is the core of the book and examines 64 business models. The aim is to choose companies that have sound business models. This is achieved by having low costs and/or doing something different that adds value to the customer. The result is strong competitive advantage, leading to superior profits.

Chapter 2. Business models: investing in sectors with strong competitive advantage

Having selected companies with sound business models, the next step is to ensure that they are in attractive sectors by examining 65 business models leading to strong competitive advantage. Both the company and the sector should have the ability to mould the economic world their way rather than being under the power of others. We also examine companies and sectors that should be avoided. If a company does not have a sound business model in a sector with strong competitive advantage then it can be readily dismissed. If it does pass the test, then further consideration can be justified, as discussed in the remaining chapters.

Chapter 3. Shifting deck chairs on The Titanic

The company's attractions are further strengthened by being in a favourable place in the economic cycle. Buying and selling at the right stage of the cycle and moving between different asset classes is a prime determinant of investment success. Ignoring the economic cycle is like pointlessly shifting deck chairs on The Titanic to obtain a better position, oblivious of the iceberg ahead.

Chapter 4. Which sectors to buy and sell during the economic cycle

Each of the sectors is scored according to its recession resistance and competitive advantage. Having identified those that offer the greatest investment opportunity, they are then assessed according to when they should be bought and sold during the economic cycle.

Chapter 5. Growth at a reasonable price

The share must offer growth at a reasonable price. Seek to invest in established companies that have a reasonable PER combined with profits growing strongly and at a sustainable rate.

Chapter 6. Technical analysis of the company and sector

The trend in the price graph is your friend, so aim to buy shares that are rising and sell those that are falling. The relative strength of the share is a proxy for technical analysis and is a very important tool.

Chapter 7. First-hand experience of the product or scuttlebutting

First-hand experience of the product or ‘scuttlebutting’ can be very useful in detecting early warning or success signs that the City has not spotted.

Chapter 8. Accounting for growth

In a world of spin and declining financial morality, it is important to understand what the financial results really mean and how to avoid companies which ‘account for growth’ in order to mislead the unwary.

Chapter 9. Investment axioms

The investment axioms, or rules, summarise a total of 1,000 years of trading experience from 35 of the greatest investment gurus. These valuable lessons should enable you to avoid pitfalls and enhance your gains.

Conclusion

This book sets out six tools to help investors choose shares that outperform. These tools are wrapped up in a simple table to rate a company’s attractiveness overall.

Summary

This methodology may seem a tall order in choosing to buy and sell shares but a familiarity with these tools is invaluable in asking the right sort of questions. For example, if you rely on a professional advisor, such as a broker, ask him the next time he recommends a share: what is the business model of the company and sector and do they have strong competitive advantage? Is this share well positioned in the economic cycle? Does it offer growth at a reasonable price? Is the share price in an up trend? Is there any accounting for growth? Do not be surprised if there is deathly silence at the other end of the phone, in which case you should go elsewhere.

A moderate grasp of this methodology should enable the private or professional investor to correctly evaluate a company in 15 minutes and dismiss the vast majority in much less time. This is how long an evaluation can take Warren Buffett, who uses business model analysis to avoid commodity businesses and invest in companies with strong competitive advantage.