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Introduction

• Who am I
• Who is in the audience
• What will we be learning
What We Won’t Discuss

• Interest rates
• The economy
• Politics
• Apple
Investing Tips

• Know what you own
• Take a long-term view
• Don’t get too attached
Owning Part Of A Business

- Stockholders own a percentage of a business
  - What does that mean?
- How to think like a business owner
- Think about market trends in your business
SEC Filings

• 10K
• 10Q
• Proxy Statement
• 8K
• Form 4
• 13F, 13D
Interesting Facts

- Company insiders
- Small firm effect
- Magic Formula
- Value vs growth
- Slow growth vs fast growth
- Holding Period
Top Executives Know Their Company The Best

Average Annual Return of Firms with Insider Buying Grouped by Insider Identity (2003 – 2010)

Source: Catalyst Mutual Funds
Large Purchases Are The Most Meaningful

Average Annual Return of Firms with Top Executive Buying Grouped by Number of Shares Purchased (2003 – 2010)

Source: Catalyst Mutual Funds
Insider Buying Example: Keurig Green Mountain (Ticker: GMCR) *For illustrative purposes only.*

**Insider Signals**

1. In the Fall of 2013, multiple insiders purchase over $1.5 million worth of GMCR stock
2. Some of these insiders made very well-timed transactions in the past

**Buying & Selling**

1. Buy stock around $65-70/share after insider buying signal
2. Partnership with Coca-Cola announced after market close on February 5th
3. Sell after announcement ($120)

**Chart**

Corporate insiders at GMCR buy stock months before deal with Coca-Cola is announced. GMCR insiders have strong track record timing stock.

*For chart above, ^GSPC refers to S&P 500 Index.*
University of Michigan Insider Buying Study

U of M Study Finds 3.7% Market Outperformance

<table>
<thead>
<tr>
<th>Year</th>
<th>Market Following Insider Trading</th>
<th>Following Insider Buying</th>
<th>Net (+/- Market) Following Insider Buying</th>
<th>Following Insider Selling</th>
<th>Net (+/- Market) Following Insider Selling</th>
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<tr>
<td>1994</td>
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<tr>
<td>Average</td>
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<td>22.1%</td>
<td>3.7%</td>
<td>15.9%</td>
<td>-2.5%</td>
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Smaller Can Be Better

Growth of $1 between 6/30/1926 and 12/31/2013

The smallest stocks averaged a 12.9% return vs. 9.8% market average.

Kenneth R. French, ©2014 Center for Research in Security Prices (CRSP), the University of Chicago, Booth School of Business, 6/30/1926 – 12/31/2013
Diversification Benefits Improve In Down-markets


Smaller stocks have a lower correlation with the S&P 500. This means that they add diversification benefits to a portfolio of larger stocks. On top of that, in a down market, when most stock prices are declining, small stocks provide further capital preservation protection.

Source: Factset, Dow Jones U.S. Micro Cap Index
Smaller Stocks Have Their Share of Risks

- **Volatility:** Smaller stocks have larger price swings than larger stocks, which is why investors should be ready to buy and hold through a full market cycle. In a portfolio that includes larger stocks, smaller stocks actually decrease overall volatility.

- **Liquidity:** Smaller stocks trade less frequently and in smaller volume. That being said, a study by Roger Ibbotson revealed an average annual return premium of 5.34% for the lowest liquidity quartile of the 3,500 largest US companies stocks over the highest liquidity quartile of the same stocks, from 1972 to 2011.*

- **Fraud:** Investors must perform thorough due diligence in order to avoid pump-and-dumps and companies with no business models in this space.

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*Liquidity as an Investment Style, Roger Ibbotson, Financial Analysts Journal Volume 69 Number 3 ©2013 CFA Institute*  
Joel Greenblatt:
• Ivy League professor
• Hedge Fund Manager
• Author

The Formula:
• Beats the market 96% of the time
• Has averaged +30% returns
Magic Formula for Investing

1. Establish a minimum market capitalization.
2. Exclude utility and financial stocks.
3. Exclude foreign companies (American Depositary Receipts).
4. Determine company's earnings yield = EBIT / enterprise value.
5. Determine company's return on capital = EBIT / (net fixed assets + working capital).
6. Rank all companies above chosen market capitalization.