

# THE HIDDEN TRUTH OF STOCK MARKET



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# PART I



# CHAPTER 1

**WILL YOU BE RICH IF YOU  
JUST BUY AND HOLD?**



One of the mainstream beliefs in the stock market is that you can just buy a good stock, go hibernate for 8 to 10 years and you will wake up as a millionaire. This seems a bit exaggerated as the ideal concept is to persuade everyone to ignore the market volatility and hold the stock for a long horizon and trust that everyone will eventually be a winner.

Well...if you do believe this, good luck with your money.

Indeed, if you would have bought Public Bank Berhad (one of the largest banks in Malaysia, and almost every Malaysian Chinese's favourite bank) shares 20 years ago and hold it until today, your investment will increase 991% (including dividends).

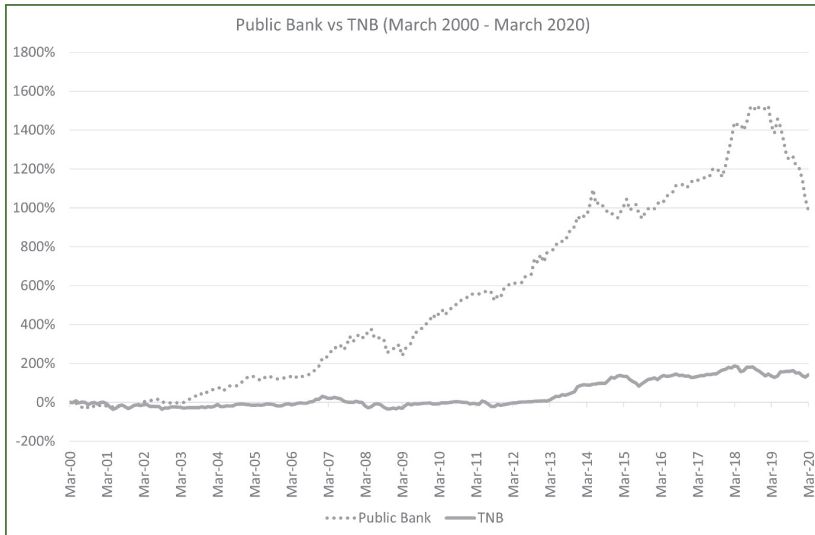
It seems that the theory of "just buy and hold" is valid.

What if the stock you had bought 20 years ago is not Public Bank but Tenaga Nasional Berhad (TNB, the largest electricity company)? How much you would earn?

The answer: 142%, including dividends.

This is way lower than the total returns in Public Bank stock!!

## THE HIDDEN TRUTH OF STOCK MARKET



Source: Bloomberg

What will happen if the stock you bought 20 years ago is Perwaja (a Malaysian steel company)?

You have no chance of recovering any of your losses, not even a single penny! This is because Perwaja was delisted in 2017. Some may argue, how could we compare the fundamental of Perwaja with TNB or Public Bank?

I cannot doubt such an argument, but this is not the message I want to convey. What I am trying to tell everyone is that the “just buy and hold” method can hardly be a successful strategy in Malaysia due to two main reasons:

### ***Firstly, companies will change.***

Whether you are a fundamental or value investor, the gist is always to analyse a company from its financials, industry outlook,

track record, cost control, corporate governance, management integrity, etc, to reduce the probability of making a wrong decision. Still, things change every single day, from technology (such as Apple) to a super boring industry (such as TNB). The company will not always remain static.

This could be due to internal rivalry, technology disruption, mismanagement, or deteriorating outlook of the industry. Nobody or shall I say only a handful of people, will be able to tell a company's prospect over the next 10 to 20 years. Nevertheless, a lot of them do think they have mastered it. Therefore, when one does not continuously monitor the company's development nor review his/her investment and naively think profit will come automatically, this is no different from believing that he/she can live happily ever after without caring for their partner.

***Secondly, companies cannot grow forever.***

During school exams, it is easy for one to improve his/her exam marks from 40 to 60 and from 60 to 80. The difficulty starts to kick in when we want to score 90 from 80, and it is even harder to reach 95 or even 100. Not only that the content is deeper, but it is also true that we are getting closer to the ceiling (100 marks).

The same goes for investment. For the strategy of "just buy and hold" to work, we need the company to show improvement continuously and tirelessly. Of course, there must be sufficient capacity to grow. However, Malaysia's population and income growth set a limit on how much profit a company can make domestically.

Just take one of my friend's favourite beverage – boba tea. In the beginning, people have to queue under the hot sun to pur-



chase it. A lot of brands flooded the market and I saw a lot of catchy names (some even shared homonyms to curse words). One thing for sure, the glamorous outlook of all these boba tea franchises will fade away one day and shops will close due to bad sales. A few years ago, one of the fast-growing fitness centre franchises - Gym H - closed down quietly (overnight, of course), and this could largely be due to market saturation.

Warren Buffett once said: “if you don’t feel comfortable owning a stock for 10 years, you shouldn’t own it for 10 minutes.” Many like to use this famous quote to justify the “just buy and hold” theory, but many miss the point on the kind of companies that Warren Buffett invests in.

In 2020, the top 5 stocks that Warren Buffett’s Berkshire Hathaway owns:

- Apple Inc, bought in 2016;
- Bank of America, bought in 2011;
- Coca Cola, bought in 1988;
- The Kraft Heinz Company, bought in 2013;
- Wells Fargo, bought in 1990

As you may observe that these companies are not only strong in the United States market, but also have a great international market share. In other words, they are the beneficiary of the globalization trend.

Companies that Warren Buffett owns are strong domestically and able to continuously penetrate foreign markets. This explains why MNCs always want to enter emerging markets because they understand the limitations of relying on the domestic market.

Back to Malaysia – How many Malaysian companies have the ambition to expand their business overseas and become the top tier leader in the Southeast Asia market?

This is why being a long-term investor in Malaysia is a test of effort because the “just buy and hold” strategy can be easily nullified. You won’t want that to happen, do you?

Thus, we should pay more attention to the intrinsic value of the company and buy it when it is undervalued by the market. Forget about the market volatility and whether or not we are practising the “just buy and hold” strategy.

This is the gist of long-term investing.

A horizontal strip of a green banknote, likely a 100 Euro note, is shown as if it has been torn from a white background. The word "CHAPTER 2" is printed in large, bold, white, sans-serif capital letters across the center of the banknote strip.

# CHAPTER 2

**WHICH IS MORE IMPORTANT?  
ENTRY OR EXIT POINT?**



Along the learning journey of stock investing, people often admire those who can sell at an all-time high and hoping that they can replicate it. Hence, people put a lot of focus to analyse what would be the best profit-taking strategy so that they can maximise their investment returns, some even think that they can time the exit point. However, is it true?

Let's take an example, you bought the stock of Company C at the price of MYR3.00, and after figuring the reasonable P/E ratio, you concluded your target price is between MYR6.00 and MYR7.00.

After 6 months, Company C had delivered tremendous earnings for two quarters consecutively and it's now known as the best stock that everyone in town should own. The share price moved to MYR6.20, what will you do?

You review your investment thesis and realise that the results are not only better than your initial projection but it seems a little too optimistic than what you would expect. Before you dive into thinking "Should I take profit?", there are a few reference points that you need to consider:

1. What is the difference between your projection and the actual results? Is it better or status quo?
2. If the actual result is exceptionally better, can this last, and for how long?
3. If it can last longer than expected, then you may consider raising your target price. However, if the glory days are short-lived, is the current valuation reasonable for you or is it overly optimistic?

For those whom have read some investment books before, you may find these reference points familiar. However, do allow me to walk you through the thought process and tell you why many fail to execute this well.

***On the first point: What is the difference between your projection and the actual results? Is it better or status quo?***

Using Company C as an example, when the share price rose to MYR6.20, you realised that the market acceptance of the new product that Company C rolled is just average and even the profit margin doesn't deviate far from your estimation. Thus, you may consider taking profit.

If the demand for the new product is overwhelming and the profit margin is higher than expected, you need to enter the second reference point.

***On the second point: If the actual result is exceptionally better, can this last, and for how long?***

After further analysis, you found out that the profit margin was boosted by lower raw material prices over the past few months. However, raw material prices are recovering to the historical level, and it will erode Company C's profit margin in the next one to two quarters. Hence, the "margin advantage" that the company enjoys will fade away very soon and you should take profit.

***On the third point: If it can last longer than expected, then you may consider raising your target price. However, if the glory days are short-lived, is the current valuation reasonable for you or is it overly optimistic?***

Let's say now Company C found a way to control their raw material prices, which was totally unexpected by you at the onset, and you will need to revise your exit price upward, perhaps from between MYR6.00 to MYR7.00 to between MYR7.50 and MYR8.00. Nevertheless, you need to pay close attention to how Company C is able to control its costs.

If it was done by acquiring a raw material company, are they the first mover?

If its competitors start to replicate its strategy (which is always the case), the cost advantage that Company C has will diminish soon. It is quite straightforward – When your competitor is able to reach the same cost structure, very likely a price war will happen and eventually bring down the margin of the entire industry. Though you may choose to hold the stock of Company C, future developments will be more complex and unpredictable.

If Company C just happened to be lucky on the margin (and this is perhaps a one-off gain), you should take profit.

The above mentioned is the entire thought process of profit-taking. Though each seems enough, we may still stumble while executing and here's why:

On the first reference point, you clearly knew that there's nothing to shout about the profit margin of the new product as it was probably higher than your expectations. However, you chose to keep the stock, in hopes that the uptrend will last longer.

Let's now move to the second reference point. Given that the good profit margin that Company C enjoys now may only sustain for another one to two quarters, taking profit should be

the right thing to do. Still, we may continue to hold on to the stock, praying that the temporary good margin can last longer. Some may even think that the current share price has not fully reflected all catalysts.

Finally, we are at the third reference point. We will turn overly sanguine on the competitive advantage of Company C by ignoring the fact that other competitors are catching up quickly. We may also face problems with the target price revision, jacking up too much and not being reasonable. Even without revising our target price, we may think that the share price should move to MYR7.00 since we had set the target price range between MYR6.00 to MYR7.00. With so much good news happening, we simply assume that we have the odds, and the higher range of target price will materialise.

Some may think “Yes, this is exactly what happened to me!” but what’s the real reason that stops us from taking profit?

My answer to that: High entry point.

There are a lot of moments where we hang on to the stock and try to brainwash ourselves like “We are not there yet!”, “The momentum is still strong!”, “It’s going to breakthrough!” We hope that the share price climbs higher in perpetual, but nothing is forever, not even Forever 21.

Most of the time, our “reasonable” target price would not happen, and things may go south, resulting in eroding all our unrealised profits. Worse still, if it goes from profit to loss.

On the surface, a weak exit strategy is the reason for our investment mistake. When further analysed, a “high entry point” could be the root cause.

Let me share my experience. I used to work at Mid Valley (one of the most popular shopping malls in Malaysia), so I know almost all shops and if there are any renovations or new walkway structures, etc. After working on my financial model and analysis, I think that the fair value of IGB REIT (the mall operating REIT of Mid Valley and The Gardens Mall) is between MYR1.90 to MYR2.00. Despite knowing that my purchase price is somewhat on the high side, I chose to buy it.

The good news is – It did not take too long for the price to move to MYR2.00 after I bought it. Adding the distribution income (similar to dividend pay-out), my investment return is now better than I expected.

Yup. To no one's surprise, I did nothing until the Covid-19 pandemic became a concern.

Due to the Covid-19 pandemic and Movement Control Order (MCO) implemented by the Malaysian government, all shopping malls' daily operations must stop, except for essential businesses. Mall operators acted quickly by waiving their tenants' rental. Hence, all mall operators are losing their rental income, car parking income, exhibition income, profit sharing, and other sources of income. Hence, the price of IGB REIT fell. After revisiting my investment thesis, I concluded that it would take quite some time for IGB REIT to recover during this time of great uncertainty. I decided to close my position. All profits and dividends were wiped out.

In fact, there were opportunities for me to exit with a decent return before MCO was implemented (at least twice) but I just let them go. Perhaps I fell in love with the stock, but essentially, my losses were due to my high entry point.



Given that high entry point, the upside potential is limited. Therefore, when the share price is neither high nor low, people tend to hang on longer than expected and hope that the market magically pushes the share price to a higher level. However, this is a low-probability incident.

If my entry point is sufficiently low, I can stay away from this kind of dilemma, take profit, and stop dreaming that someone would come to the rescue with their own money.

Remember, the stock market is a place full of emotions. When everyone is pessimistic, stocks get undervalued. When everyone is optimistic, stocks get overvalued. Pessimism and optimism are random events, hence, we should learn how to read the market sentiment before deciding on our investment actions.

***When you enter at the time everyone is sorrowful,  
you need everyone to calm down.***

***When you enter at the time everyone calmed down,  
you need them to be optimistic.***

***When you enter at the time everyone is optimistic,  
you need them to be insane.***

***When you enter at the time everyone is insane,  
you need them to be high.***

In other words, when you enter at a low price, you have the upper hand. You can choose to exit when the market calms down, turns optimistic, insane, or high. The choice is yours now. Notwithstanding, if you enter at the wrong time, your exit options are limited and there will be larger uncertainties.

Hence, stop focusing on profit-taking, put more effort into getting a low entry point that is more realistic.

Your profit is determined by your entry point!