

Twitter Thread by CFA Society India

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Much awaited session at Kolkata by Utpal Seth, Rare Enterprises, on "Dimensions of Mistakes in Investing", to be moderated by Varun Goenka.

#MAW



Utpal Sheth starts with a tribute to Rakesh Jhunjhunwala

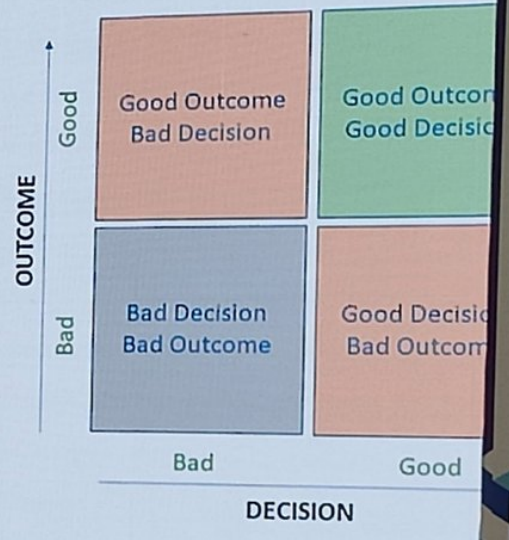


Utpal Sheth lays out the context for today's session - Mistakes are rarely discussed!

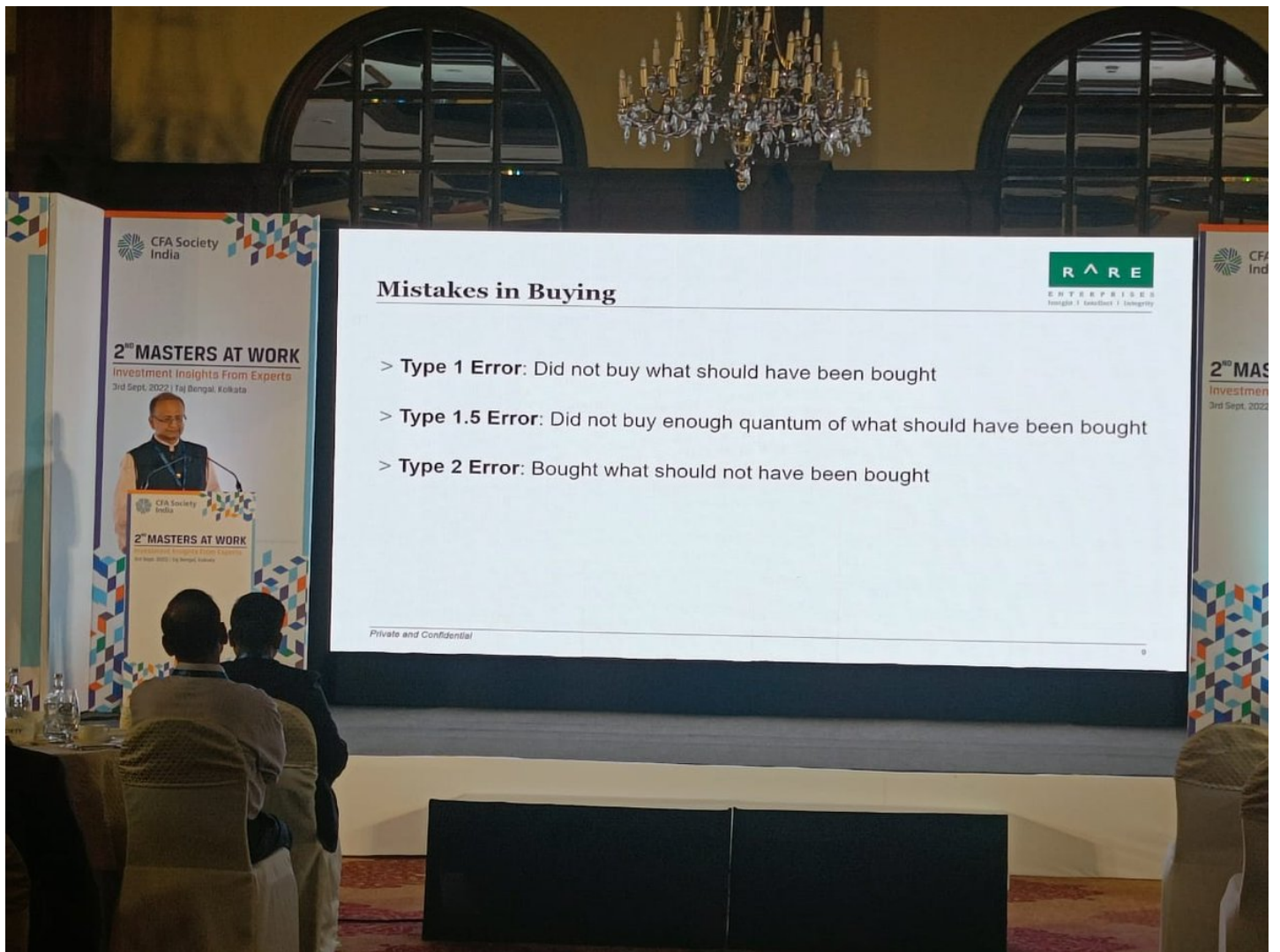
Outcomes don't define mistakes. They are known through a process of deep introspection & multiple iterations. The opportunity cost of not embracing mistakes is very high.

Context for Mistakes

- > Success is usually talked about, not mistakes. Returns are talked about but not the **quality of returns**. Mistakes are rarely discussed
- > Mistakes are not known at a snapshot of time, but over a period of time. Especially in investing, **mistakes are magnified by time**
- > Mistakes are known through a process of deep **introspection and multiple iterations**
- > Relationship between **Outcomes and Decisions is not linear**
- > We live in a dynamic world, where business models are evolving; technology and platforms are causing disruption. So embracing mistakes is crucial. **Opportunity cost of not embracing mistakes is very high**



When speaking of mistakes in investing, we often speak of 'Type 2 errors', and at times of type 1 errors. Utpal speaks of Type 1.5 error - not buying / selling with conviction!



Utpal discusses their process with mistakes - and quotes Rakesh Jhunjhunwala - making mistakes isn't a crime, repeating them is. Discusses mistakes at RARE Enterprises with the audience with ease.

One needs to think of portfolio balance very deeply. Sizing the bet depends on the degree of conviction and degree of evidence. Recommended book: "Thinking in Bets"



On thinking about investment mistakes - 3 key steps - identification, attribution and rectification. Attribution of mistakes needs time and thought - one need not wait to attribute mistakes for rectification!

Buying right is tough. The probability of making a good investment is low - due to the chance of making a mistake in any of the 5-8 parameters we use for evaluation. The key is to identify the right jungle (Megatrend) and the right company within that (Gorilla).



Probability of Making Good Investments is Low

Joint Probability	Business	Management	Valuation	Governance	Financials	Total
Scenario 1	80%	70%	80%	70%	60%	14%
Scenario 2	70%	60%	50%	60%	50%	6%
Scenario 3	60%	50%	45%	50%	50%	3%

- > Despite getting major parameters right, the probability of making a good investment is **significantly lower** than one would imagine (~6%)
- > Every buy decision needs to be evaluated in **absolute** terms as well as **relative** to (a) cash, (b) other opportunities in the portfolio, and (c) other opportunities in the investment universe
- > For a 15 stock portfolio, **only 1-2 stocks will be good investments**. Which means over a 50-60 year investment life, one needs to keep iterating the remaining stocks to eventually get to the right portfolio of stocks

Discusses in detail examples of mistakes in buying

Type 1 (didn't buy): Bajaj Finance

Type 1.5 (didn't buy enough/sold partly): CRISIL

Type 2 (bought incorrectly): A2Z Infra Engineering

Important: Parameters in discussion were on their framework - Identifying the Megatrend (see next tweet) they were part of, and whether they were Clear leader, Near leader, and Emerging leader

Important: Megatrend buckets used by Rare Enterprises: Consumption, Globalisation, Financial deepening, Digitalisation, Outsourcing and Formalisation, and Renewable Energy.

Now discusses Mistakes in selling:

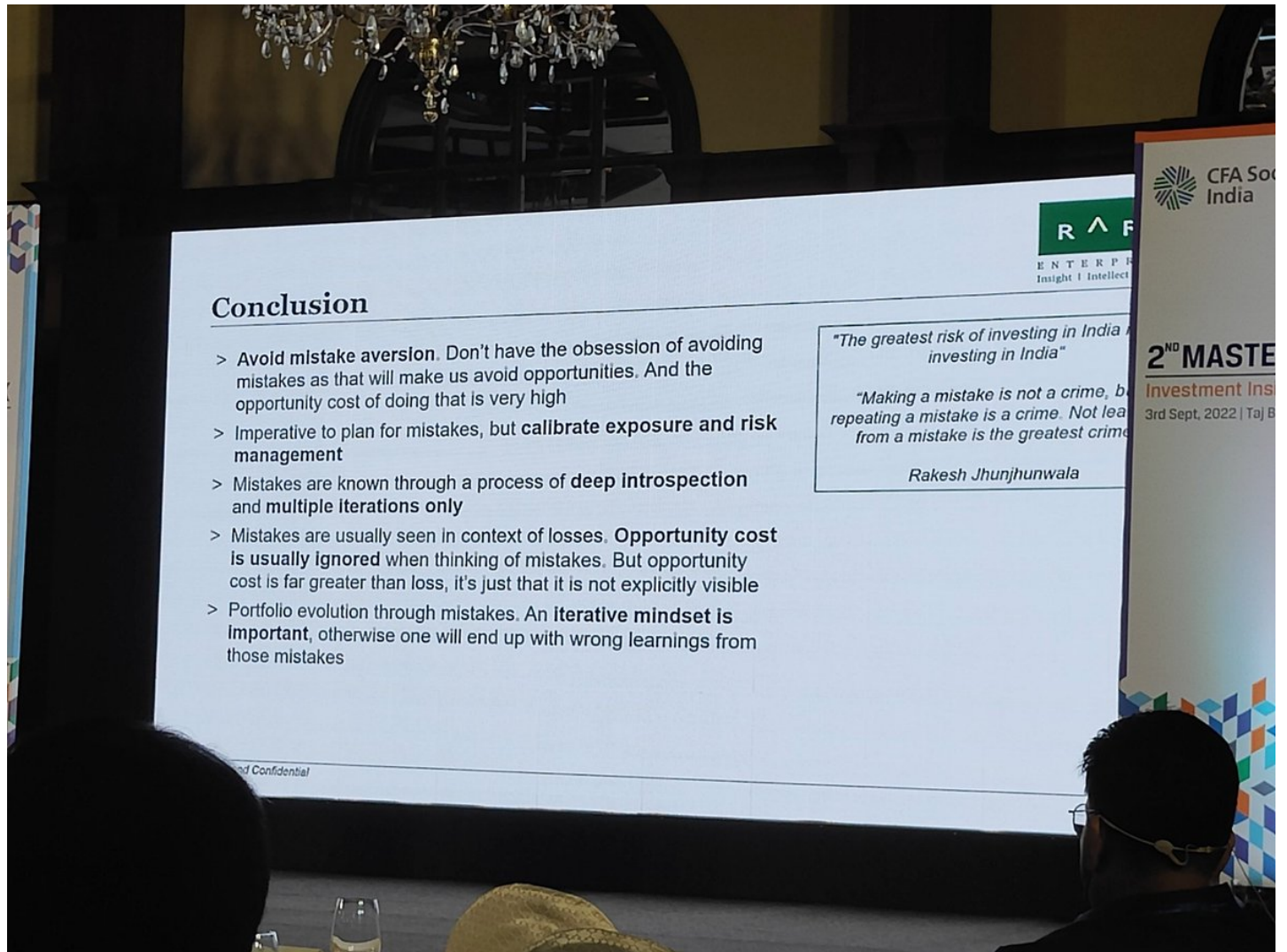
Type 1 (Didn't sell right): Bilcare Limited

Type 1.5 (didn't sell enough): Praj Industries

Type 2 (Sold too early): Relaxo Footwear

These hurt much more, and they have had much to learn from these.

Utpal concludes his presentation with quotes from Rakesh Jhunjhunwala and Jeff Bezos, and adds: Embrace your mistake, let mistakes not affect the balance of your mind, and have a risk Management framework to enable peace of mind.



We now head to the Q&A session, moderated by [@VGoenka82](#)



Q: Attitude that helped him achieve heights

A: Learning attitude and adaptability. Hopes to have a learning attitude to the last day, and ensure that it's not an 'ivory tower learning' - it's important to implement and execute (hence adaptability and resilience).

Q: How to think about portfolio sizing, given the low joint probability of being right?

A: Buy decisions need not be at one point in time. Gradually build conviction - and continue buying - even if at higher levels. Refers to [@mjmauboussin](#)'s Probability adjusted Investing.

Speaks on the importance of the right culture in identifying companies that could create terminal value. You can replace the machinery, the product and all else. You can't buy culture!

Q: How to build the right investment team.

A: one needs to have the right environment, empowerment, and right leadership. Complementing skills and behaviours should be present - balance between accelerator and brakes.

Closing remarks from Utpal: Keep learning, keep adapting and keep investing. Don't be afraid of mistakes, protect your state of mind, it's a fulfilling journey. Has had a good time interacting with youngsters here and looks forward to more such at the #MAW conference.