

13 Characteristics of **The Perfect Stock to Buy** from Peter Lynch One up on Wall Street

“Search for businesses that any idiot can run, because sooner or later one will”

Peter Lynch

Peter Lynch discusses 13 characteristics of the perfect stock to buy:

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1) It sounds dull – or even better, ridiculous

The first thing is that the simpler the business is, the better. It also should have a boring name. His favorite stock name is Pep Boys – Many, Moe and Jack. Not a name that would turn the heads of Wall Street investors or news outlets.



Another example; he invested in Consolidated Rock and nobody cared about it. Then, only when it changed its name to Conrock and later to Calmat, Wall Street started to take notice.

So, we have to look at a boring business in a boring industry with a boring name.

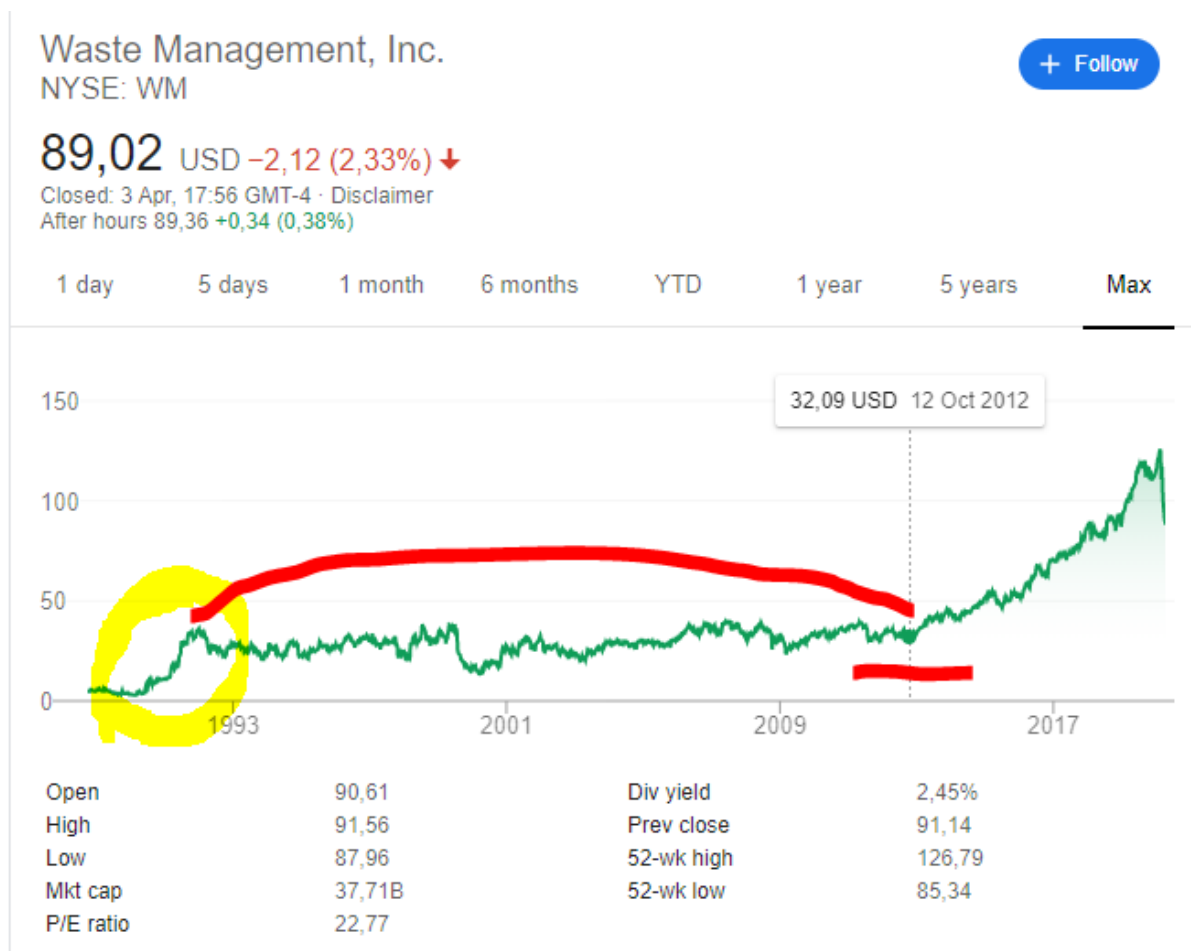
The key here is that a boring name will not get recognized by Wall Street until earnings are extremely good which gives you the opportunity to buy a good business before others rush in.

2) It does something dull

Dull name, dull business. Now why does Lynch promote investing into dull businesses? Well, the smartest minds all want to work at Apple, Google, Amazon, Tesla while dull businesses that we all need are often overlooked from a job, competitive and especially investing perspective.

If a boring company with a boring name has a good balance sheet, good earnings, it will get discovered by Wall Street one day, but you'll have plenty of time to accumulate and then sell to the trend followers later.

Waste Management (WM) has a dull business, but there was time to accumulate for a few years in the 1980s before it got recognized in the early 90s. Then the market forgot about it and only recognized it as a good business again over the last 7 years.



3) It does something disagreeable

Examples used are grease removers from auto parts, plastic fork makers etc. Again, something no Wall Street analyst would look into.

I like to look at miners, an industry everybody hates because it is dirty, difficult and volatile. However, if you are reading this, the equipment you are using has been made by metals mined somewhere in the world. The electricity came to you through a copper line etc...

Disagreeable but necessary.

4) It is a spinoff

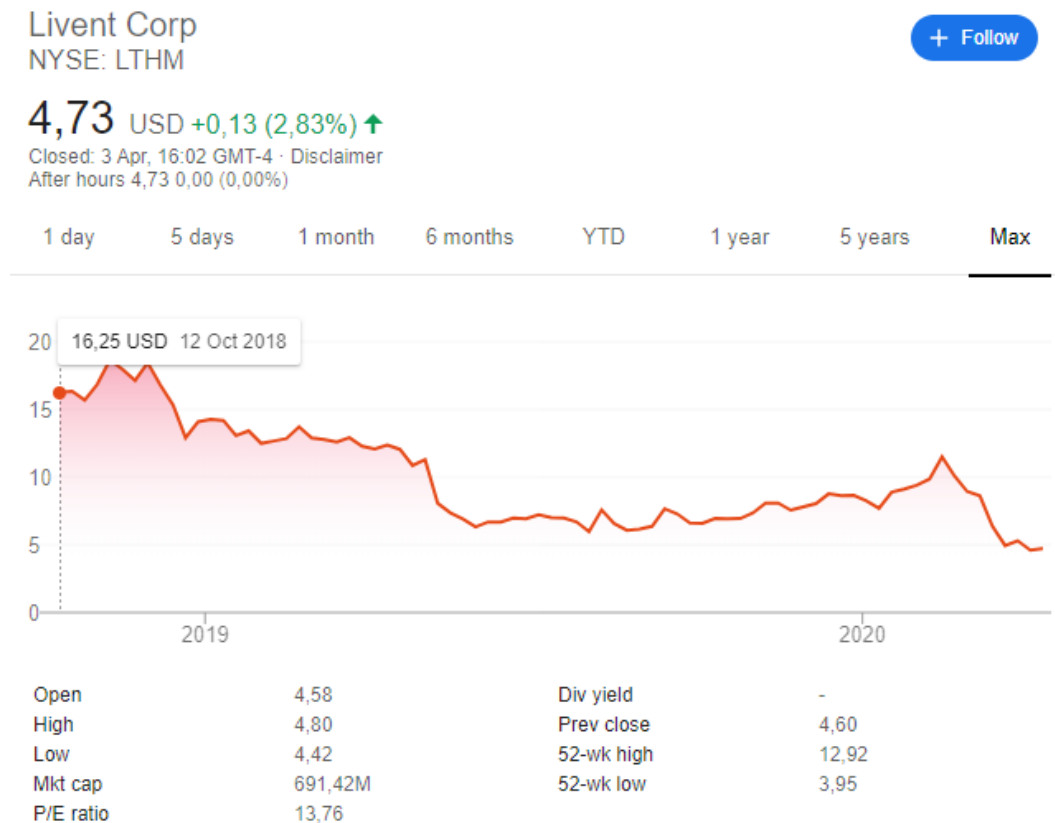
Spinoffs are companies that are separated from the parent company and left to operate independently. Shareholders of the parent company keep their share in the parent company but also get a new share in the new company. One example is lithium miner Livent that was spun off from FMC corporation in 2018 so that Livent can focus solely on producing lithium.

Another example is Toys "R" Us that spun out of Interstate Department Stores.

The thing with spinoffs is that those are usually smaller companies and there is no incentive for analysts to follow them. Shareholders that got the new shares don't know what to do with the shares because the business model is usually different (therefore the spinoff) and the pressure is often on the sell side where the stock drops. For example, FMC pays a nice dividend while Livent won't be paying dividends for a while as it is investing heavily in the

lithium cycle. Many investors ask themselves why hold onto a stock that is going down and institutions often sell too because is little money for them.

Therefore, spinoffs are another unloved segment to look for good businesses and find them before Wall Street does.



When it comes to spinoffs, if you dedicate yourself, you can have more info than Wall Street and understand when earnings might turn up much earlier.

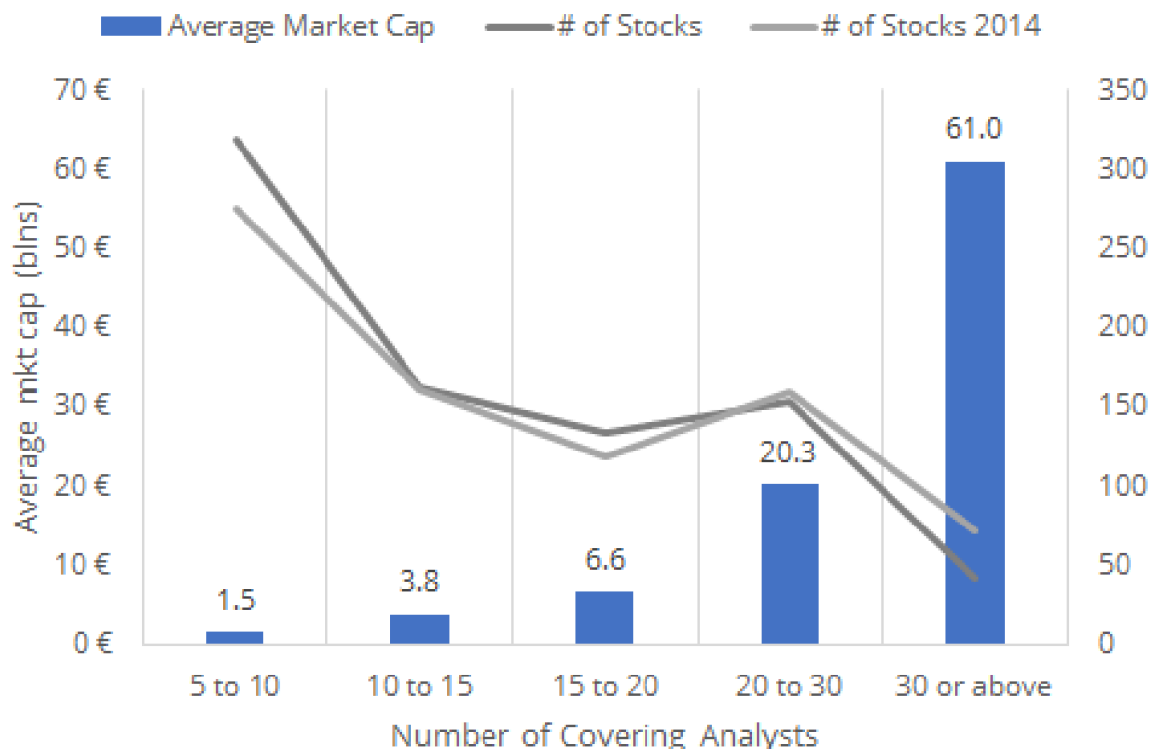
So, you might find interesting buys within the spinoff world.

5) The institutions don't own it, and the analysts don't follow it

An analyst's job is to drive traffic and business to his employer, usually an investment bank. Now, which would you like to hear more about: Google, Apple, Amazon, Netflix or La Doria, Surgutneft and Turisthotel? Well, you are familiar with the former and therefore more likely to be interested. Consequently, analysts focus on what they can easily sell, not on what might be the best investment. They have a limited amount of time and have to reach as much exposure as possible in that time.

Further, regulations and saving make it costly for banks to follow many stocks. The consequence is that smaller businesses aren't followed at all.

Pan EU Analyst coverage vs Market Cap



Number of analysts per company in relation to market capitalization. Source: [FT](#)

Further, with the mania of index fund investing, there is less and less money for analysis. This creates an opportunity for those that are willing to do research.

I often find myself listening to conference calls and there are no analysts present. This means it is up to just me to see what kind of investment is that.

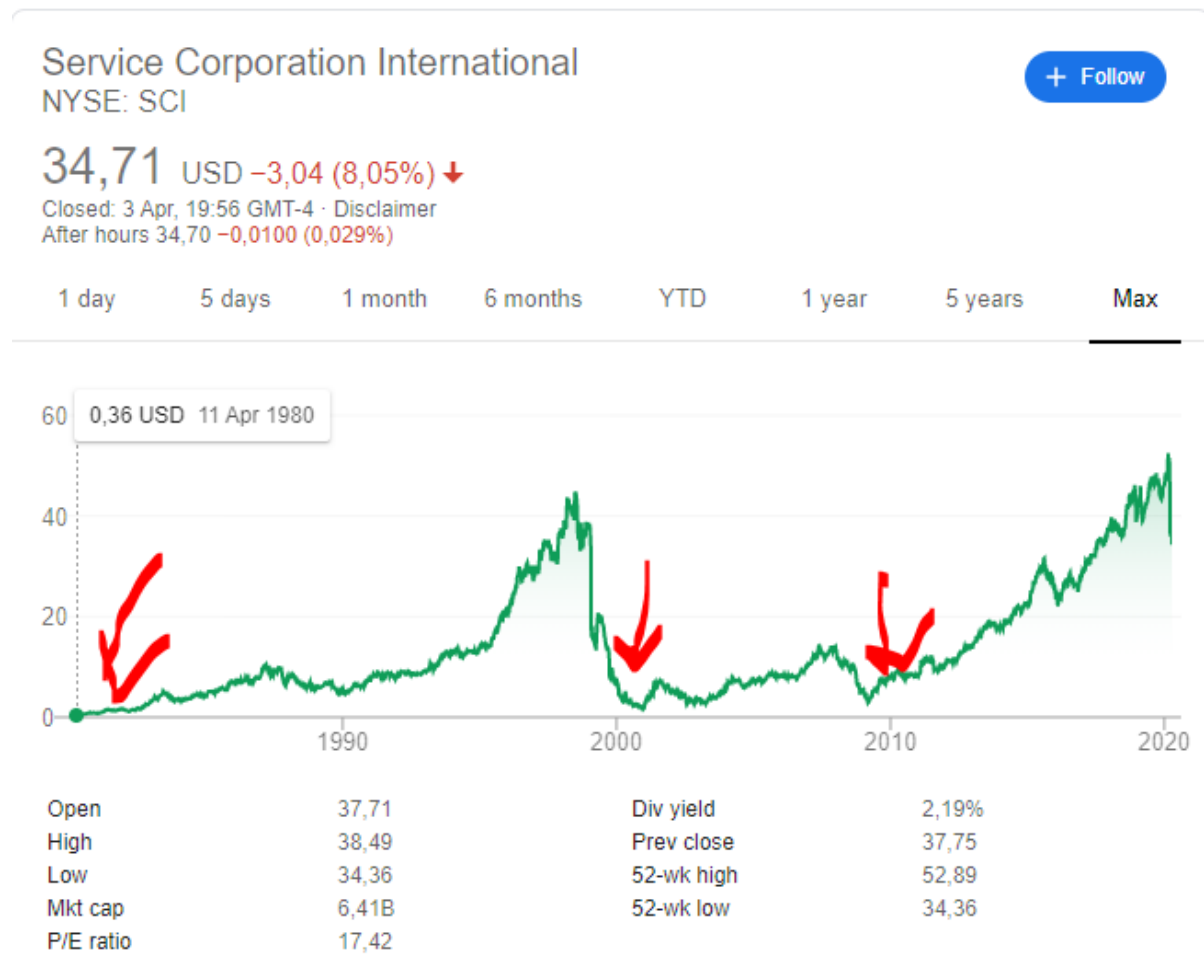
6) The rumors abound – It's involved with toxic waste and/or the mafia

Nowadays [waste management stocks](#) are hot, 7 years ago those were not liked. Same for casino stocks etc. What is the current unliked, unloved industry that we all need to use or are using?

7) There's something depressing about it

What can be more depressing than mortality and burials. However, one of the best stocks for Lynch was Service Corporation International (SCI). The stock was a 100 bagger from 1980 to 1998, a 10 bagger from 2001 to 2007 and then again, a 15 bagger from 2011 to 2020. It is fascinating how stocks get in and out of favor with Wall Street.

Lynch mentions how Wall Street simply wasn't interested in the company for long, whatever the management did. Funny, after some bad news in the 1990s, in 2001 I think it was Pabrai that was buying big because Wall Street's interest quickly faded given the stock performance.



8) It is a no-growth industry

The market is crazy about growth, no number matters as the top line and as long as you grow, you'll find capital to expand while the earnings losses will always be considered temporary. However, Lynch likes to think the opposite way and the only thrilling thing for him with growth stocks is watching it go down.

Lynch's book was written in 1989 and his list goes as following:

- 1950s it was carpets
- 1960s it was electronics
- 1980s it was computers

We know 1990s it was the internet and lately we have seen cannabis, lithium etc. all debacle.

ACB - Aurora Cannabis Inc.**\$0.80** ▲ **0.0006 (0.07%)**

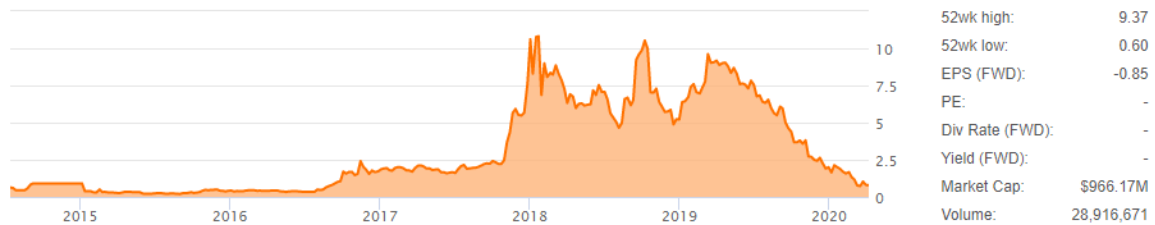
NYSE | 4:00 PM 4/7/20 15 minute delayed price

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Summary Ratings Key Data Earnings Dividends Value Growth Profitability Momentum Peers

1D 5D 1M 6M 1Y 5Y 10Y MAX Advanced Chart



The issue with growth sectors and stocks is that all the best minds go into that area, and therefore it is hard to make a profit due to high competition.

Some companies will become dominant like it has been the case for Amazon, but many similarly promising companies went bust in the past.

The nice thing about a boring, dull, disgusting, no growth industry is that it doesn't attract the brightest minds, it doesn't have much competition and it can focus on making money and growing within the no-growth industry.

The best business minds from Wharton want to work for big tech companies or Goldman, not for a burial company.

9) It's got a niche

A niche means no competition! Those are businesses that are required but it doesn't pay for competitors to come in. It is either too small of a market or you have an exclusive franchise. Such a niche allows you to increase prices and that is what increases earnings over time.

What is Buffett's largest investing mistake?

Well, you might be surprised, but it is a company called Berkshire Hathaway because it didn't have a niche or moat how Buffett likes to call it. Everybody can get into the textile business. Buffett quickly figured niches or moats are what it takes and expanded to newspapers and other great businesses that made him who he is now.

A company that operates in many niches is [3M, recently analyzed in a video](#). It is difficult for someone to compete within all these products and do it at scale as 3M is doing it.

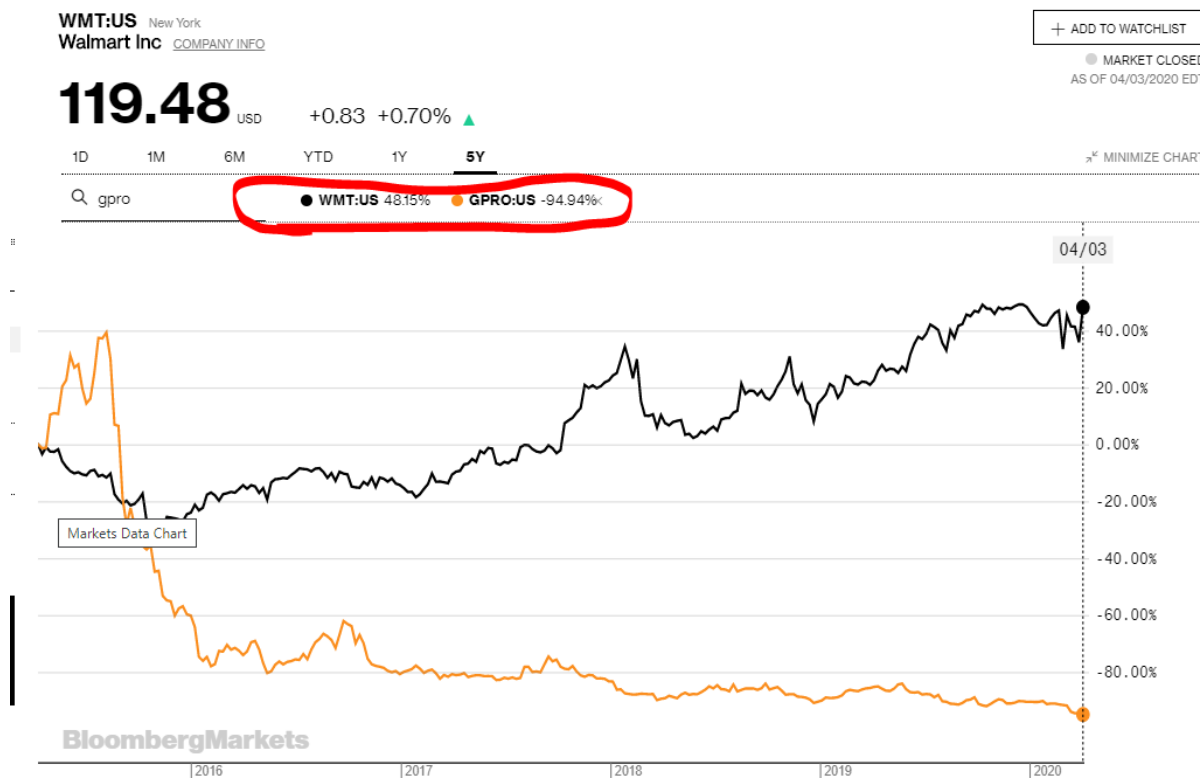


10) People have to keep buying it

When you buy a stock that produces things people don't really need, you can make money on it but you are taking a risk.

When you buy a stock that makes things people will keep buying no matter what, you are investing.

A simple example is the comparison between Walmart and GoPro stock.

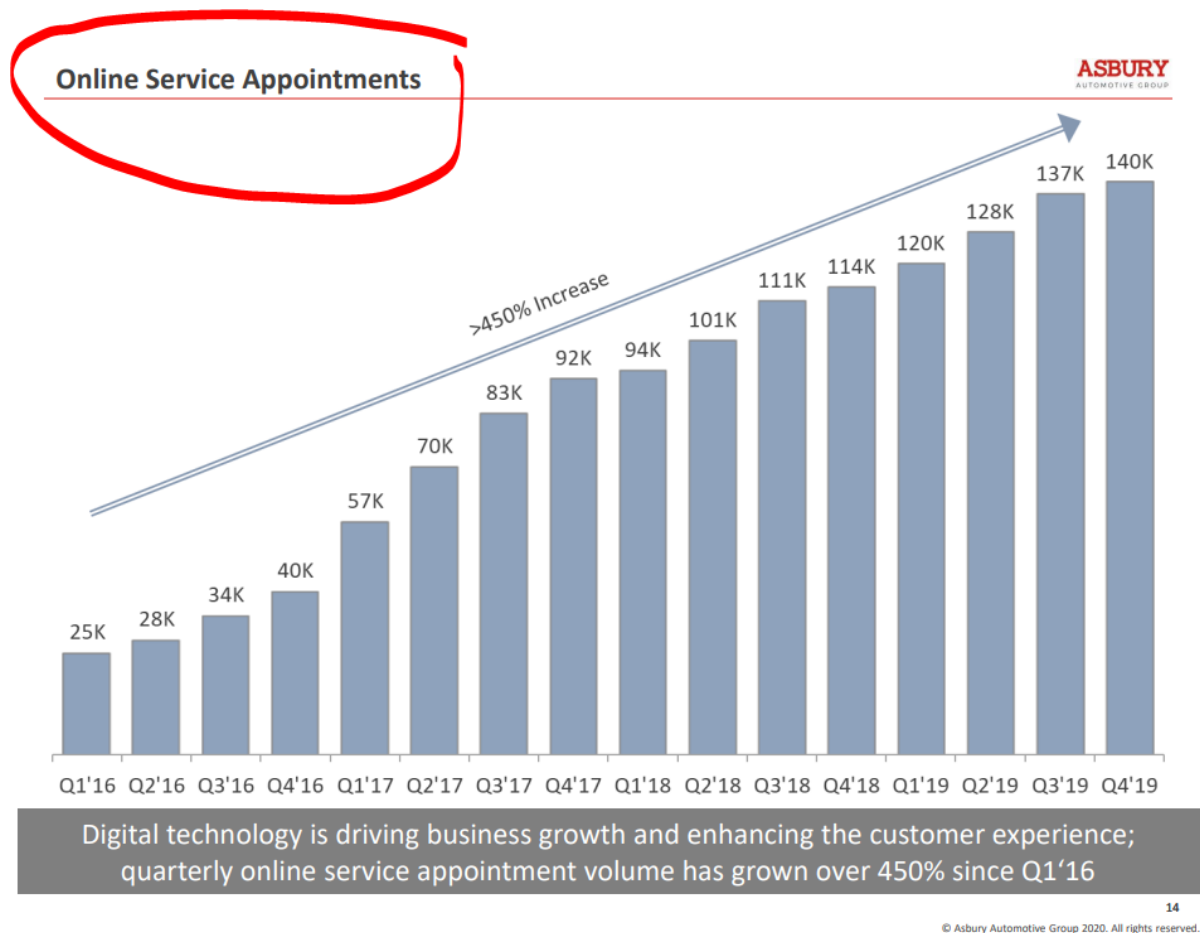


People need Walmart for whatever they are buying there, but they don't need one after another GoPro camera. The investing result over 5 years tells the whole point.

11) It's a user of technology

Many are attracted by the new technology companies competing for market share. But the best investment might be the company that uses the technology to lower its costs and increase margins.

An example can be self-service checkouts or simply online selling where a company manages to grow with lower costs. Another example can be a car dealership that offers an automated online booking. Look at Asbury Automotive online booking growth.



Asbury Automotive – Source: [Investor relations](#)

12) The insiders are buyers

In general insiders are net sellers of the stock. If they are buying like crazy, it means only one thing; the stock is likely to go up.

However, by insiders, don't think about the CEO. It is a marketing purchase when he does it. But, if middle management take their money and buy stocks, things might get interesting.

You can track insider purchases for the company you are interested in by looking at SEC Form 4 filings.

LAWS & REGULATIONS › SEC & REGULATORY BODIES

SEC Form 4: Statement of Changes in Beneficial Ownership Overview

By [ADAM BARONE](#) | Updated Apr 14, 2019

What Is SEC Form 4: Statement of Changes in Beneficial Ownership?

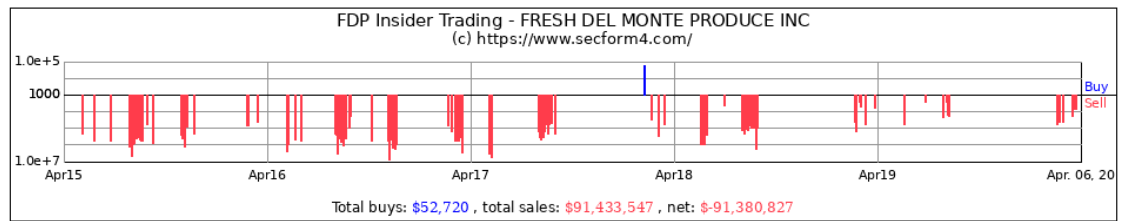
SEC Form 4: Statement of Changes in Beneficial Ownership is a document that must be filed with the [Securities and Exchange Commission](#) (SEC) whenever there is a material change in the holdings of company insiders. Insiders consist of directors and officers of the company, as well as any shareholders, owning 10% or more of the company's outstanding stock. The forms ask about the reporting person's relationship to the company and about purchases and sales of such [equity securities](#).

The filing of Form 4 relates to Sections 16(a) and 23(a) of the [Securities Exchange Act of 1934](#), as well as Sections 30(h) and 38 of the [Investment Company Act of 1940](#). Disclosure of information required on Form 4 is mandatory and becomes public record upon filing.

Source: [Investopedia](#)

You can also track it by looking at the website <https://www.secform4.com/>

I have taken a look at one of my past positions (FDP) and it seems the management is just selling, selling and selling. Might not be important as people sell for various reasons. However, buying is the big indicator.



Goto page 0, 1, 2, 3, 4, ... 12, 13, 14, 15, 16, Next

Common stock purchase or sale:

Transaction Date	Reported Date Time	Company	Symbol	Insider Relationship	Shares Traded	Average Price	Total Amount	Shares Owned	Filing
2020-03-25 Sale	2020-03-27 5:14 pm	FRESH DEL MONTE PRODUCE INC	FDP	Bezerra Eduardo Guarita CFO	245	\$31.29	\$7,666	1,928 (Direct Indirect)	View
2020-03-23 Sale	2020-03-25 5:58 pm	FRESH DEL MONTE PRODUCE INC	FDP	Gold Elana VP Chief Marketing Officer	201	\$34.64	\$6,963	299 (Direct)	View
2020-03-18 Sale	2020-03-20 5:40 pm	FRESH DEL MONTE PRODUCE INC	FDP	CHAMPION MADELEINE L Director	563	\$33	\$18,579	27,127 (Direct)	View
2020-03-02 Sale	2020-03-04 9:24 pm	FRESH DEL MONTE PRODUCE INC	FDP	SAUTER HANS VP	155	\$28.32	\$4,390	2,633 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:23 pm	FRESH DEL MONTE PRODUCE INC	FDP	Gordon Marlene VP	182	\$28.32	\$5,154	1,616 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:23 pm	FRESH DEL MONTE PRODUCE INC	FDP	Cerioli Annunciata VP	185	\$28.32	\$5,239	1,012 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:22 pm	FRESH DEL MONTE PRODUCE INC	FDP	Jeifetz Martha V. VP	155	\$28.32	\$4,390	941 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:22 pm	FRESH DEL MONTE PRODUCE INC	FDP	Lutty Helmuth VP	159	\$28.32	\$4,503	3,125 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:21 pm	FRESH DEL MONTE PRODUCE INC	FDP	Bezerra Eduardo Guarita CFO	175	\$28.32	\$4,956	1,169 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:20 pm	FRESH DEL MONTE PRODUCE INC	FDP	Dumas Danny VP	168	\$28.32	\$4,758	3,312 (Direct Indirect)	View
2020-03-02 Sale	2020-03-04 9:20 pm	FRESH DEL MONTE PRODUCE INC	FDP	Zakharia Youssef COO	1,477	\$28.32	\$41,829	12,493 (Direct Indirect)	View
2020-02-25 Sale	2020-02-27 6:42 pm	FRESH DEL MONTE PRODUCE INC	FDP	CHAMPION MADELEINE L Director	1,332	\$29.94	\$39,880	27,690 (Direct)	View
2020-02-25 Sale	2020-02-27 6:42 pm	FRESH DEL MONTE PRODUCE INC	FDP	BERTHELOT MICHAEL J Director	615	\$30	\$18,450	18,922 (Direct)	View
2020-02-21 Sale	2020-02-25 8:53 pm	FRESH DEL MONTE PRODUCE INC	FDP	SAUTER HANS VP	122	\$28.5	\$3,477	2,278 (Direct Indirect)	View
2020-02-21 Sale	2020-02-25 8:53 pm	FRESH DEL MONTE PRODUCE INC	FDP	Dumas Danny VP	91	\$28.5	\$2,594	2,926 (Direct Indirect)	View

FDP insider activity – Source: <https://www.secform4.com/>

Also, when the management is selling, the big purchase from the CEO is just marketing.

Common stock purchase or sale:

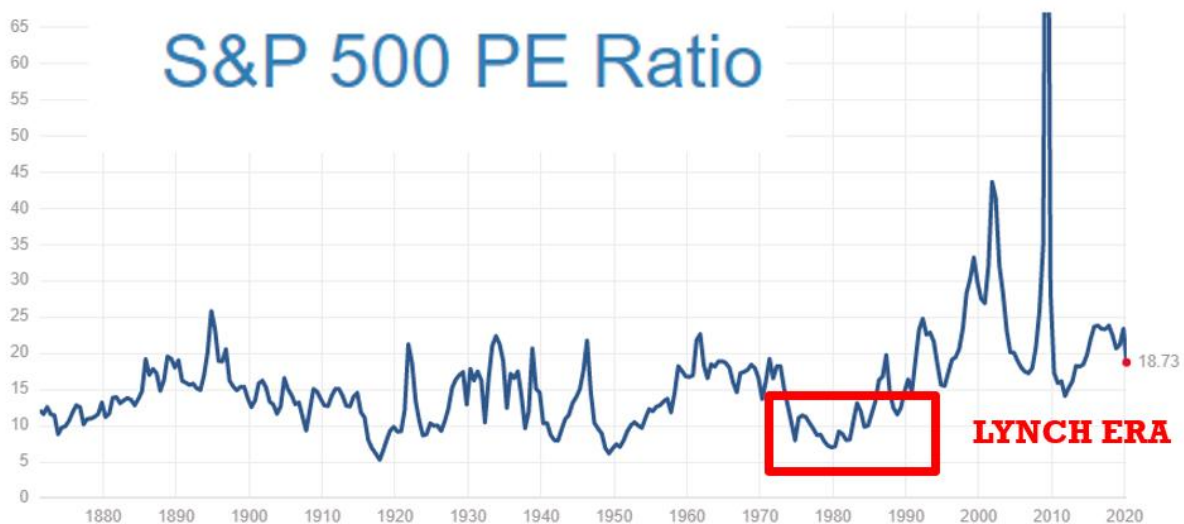
Transaction Date	Reported Date/Time	Company	Symbol	Insider Relationship	Shares Traded	Average Price	Total Amount	Shares Owned	Filing
2020-03-17 Sale	2020-03-19 9:22 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$440	\$66,002	11,432 (Direct)	View
2020-02-21 Sale	2020-02-25 8:51 pm	Tesla Inc.	TSLA	Taneja Vaibhav CAO	1,934	\$902.2	\$1,744,915	1,925 (Direct)	View
2020-02-20 Sale	2020-02-24 9:50 pm	Tesla Inc.	TSLA	Gracias Antonio J. Director	77,152	\$892.6	\$68,869,670	509 (Indirect Direct)	View
2020-02-20 Sale	2020-02-24 9:25 pm	Tesla Inc.	TSLA	Baglino Andrew D VP	4,000	\$891.9	\$3,567,712	3,805 (Direct)	View
2020-02-18 Sale	2020-02-19 8:33 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$842.2	\$126,333	10,694 (Direct)	View
2020-02-14 Purchase	2020-02-19 8:20 pm	Tesla Inc.	TSLA	ELLISON LAWRENCE JOSEPH Director	1,250	\$767	\$958,750	3,001,250 (Indirect)	View
2020-02-14 Purchase	2020-02-19 8:02 pm	Tesla Inc.	TSLA	Musk Elon CEO 10% Owner	13,037	\$767	\$9,999,379	34,098,596 (Indirect)	View
2020-02-03 Sale	2020-02-05 9:48 pm	Tesla Inc.	TSLA	Guillen Jerome M President	1,500	\$712.7	\$1,069,086	9,236 (Direct)	View
2020-01-17 Sale	2020-01-21 8:49 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$507.6	\$76,141	10,844 (Direct)	View
2020-01-02 Sale	2020-01-06 6:47 pm	Tesla Inc.	TSLA	Guillen Jerome M President	2,000	\$427.5	\$854,935	9,236 (Direct)	View
2019-12-17 Sale	2019-12-19 8:10 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$379	\$56,848	10,994 (Direct)	View
2019-12-02 Sale	2019-12-04 8:25 pm	Tesla Inc.	TSLA	Guillen Jerome M President	2,000	\$329.4	\$658,800	8,973 (Direct)	View
2019-11-22 Sale	2019-11-26 8:49 pm	Tesla Inc.	TSLA	Jurvetson Stephen T Director	17,223	\$332.4	\$5,725,683	0 (Indirect Direct)	View
2019-11-18 Sale	2019-11-20 8:36 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$352.3	\$52,848	9,701 (Direct)	View
2019-11-13 Sale	2019-11-15 8:32 pm	Tesla Inc.	TSLA	Taneja Vaibhav CAO	452	\$350.8	\$158,563	1,020 (Direct)	View
2019-11-12 Sale	2019-11-14 9:05 pm	Tesla Inc.	TSLA	Musk Kimbal Director	64,285	\$350.1	\$22,503,769	134,048 (Direct)	View
2019-11-01 Sale	2019-11-05 9:01 pm	Tesla Inc.	TSLA	Guillen Jerome M President	2,000	\$316.3	\$632,640	8,973 (Direct)	View
2019-10-30 Sale	2019-11-01 7:48 pm	Tesla Inc.	TSLA	Baglino Andrew D VP	2,366	\$313.3	\$741,159	3,288 (Direct)	View
2019-10-25 Sale	2019-10-29 7:49 pm	Tesla Inc.	TSLA	Guillen Jerome M President	8,000	\$305	\$2,440,000	8,973 (Direct)	View
2019-10-17 Sale	2019-10-21 9:33 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$262	\$39,300	9,851 (Direct)	View
2019-09-17 Sale	2019-09-19 8:40 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$242.5	\$36,371	10,001 (Direct)	View
2019-08-19 Sale	2019-08-21 8:46 pm	Tesla Inc.	TSLA	Kirkhorn Zachary CFO	150	\$224	\$33,600	9,812 (Direct)	View

13) The company is buying back shares

Lynch is positive about buybacks, but these days, like with anything good over time, the situation isn't that positive anymore, at least not in all cases.

The logic between buybacks is simple. The company buys stocks on the market, removes them from circulation and the remaining shareholders divide everything on a smaller denominator.

The thing is that in the Lynch era, stocks were extremely cheap and practically all the buybacks were done below book value, at an extremely low valuation and with earned cash that wasn't easily invested elsewhere at higher returns on capital.



S&P 500 PE ratio was mostly below 10 when Lynch was investing Source: [Multpl](#)

A PE ratio below 10 means that the company was getting a return of above 10% when it was buying its own shares on the market.

Today, companies like Boeing (BA) spend billions on buybacks no matter the stock price. BA was buying stocks back even if the PE ratio was above 20, implying a business return of below 5% and despite the fact that the book value was going lower and lower due to more and more buybacks at a stock price above the actual book value.



BA's book value and stock price – Source: [Macrotrends](https://www.macrotrends.net)

I THINK THE MESSAGE IS SIMPLE – IF EVERYBODY IS EXCITED ABOUT A STOCK – IT MIGHT NOT BE THE BEST INVESTMENT

These are the most traded and popular stocks with a European discount broker. Lynch would stay away from the coolest stocks.

