When to Sell

Cy Lynch
Vice-Chair, BetterInvesting
Board of Directors

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Why This Class

- Selling is inevitable
- Toughest decision for long-term investor
- BetterInvesting tools less helpful for selling than for buying

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Class Overview

- The Big Picture
  - Reasons to sell
  - Selling fallacies
- Lending Focus to the Selling Decision
  - Overview techniques and tools to aid the decision
  - Look at considerations for disciplined selling decisions
  - Review examples
- Additional considerations

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Why is Selling Tough?

- BI Tools focus more on buying
- BI teaching focuses on buying
- Hard to admit mistakes
  - Don't like to take losses
- Falling in love with winners
- **Lack of a disciplined approach to selling**

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Reasons to Sell

- Personal factors
  - Wealth expending phase contrasted with wealth accumulating
- To improve portfolio
  - Projected return
  - Quality
  - Both
- Mistakes
- Fundamental change in business prospects

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Selling Don'ts

- Don't sell because the price hasn't moved
- Don't sell on temporary bad news
- Don't sell merely because of paper loss or profit
  - Tax loss selling and portfolio improvement may be valid
- Don't use "guaranteed loss orders" (aka stop loss)
  - Trailing stop when price is being driven by momentum might be exception

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Lending Focus to Selling

- Goals for selling
  - Protect gains
  - Minimize losses
  - Manage portfolio volatility and quality; and
  - Improve overall total return over the long-term

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Lending Focus to Selling

- Same broad selling criteria as for buying decision
- Quality and Value
- Just in reverse
  - –Quality declines
  - –Value declines (measured by potential return)

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Lending Focus to Selling – BI Tools

- Stock Selection Guide
  - –**Periodic updates** help identify candidates for selling when appropriate
  - –**Update before selling** (especially if for overvaluation only)

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Lending Focus to Selling – BI Tools

- Stock Selection Guide
  - –Quality matters first, Value matters most
  - –Value Criteria
    - Focus on potential return
    - Current P/E ratio compared to historical or projected average (Relative Value)
      - –Can impact confidence in return projection
      - –Not best valuation measure
    - Price zone
      - –Fatally flawed, don't use

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Lending Focus to Selling – BI Tools

- Quarterly Growth Trend Graph and Data Table in SSG^{PLUS} (aka PERT-A)
  - –Tendency toward short-term focus
    - Beware of rigid "rules"
  - –Can help, but remember to ask:
    - Are declines in growth rate normal (e.g., maturing company)?
    - Are growth and profitability still above my projections?
    - Temporary or long-term problems
    - Does management have a reasonable plan to address the issue?

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Lending Focus to Selling – BI Tools

- Online Tools – Portfolio Summary Report
  - –Portfolio at a glance
  - –Shows dollar-weighted Potential Return and other metrics
  - –Facilitates "Portfolio-Centered Decision-making"

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Lending Focus to Selling – Quality

- Made a mistake – Company never accomplishes your business expectations
  - –Usually growth or profitability projections
  - –Could be a product launch, new market entry, etc.
- Business deteriorates
  - –Fails to meet projections with no reasonable plan to correct
- Dividend cut – One writer says, "Run away"

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Lending Focus to Selling – Quality

- Key Question
  - –Are problems temporary or terminal?
- Factors to consider:
  - –Are problems company-specific?
  - –Does management recognize and acknowledge problems?
  - –Does management have a plan?
- How long is long enough to wait?

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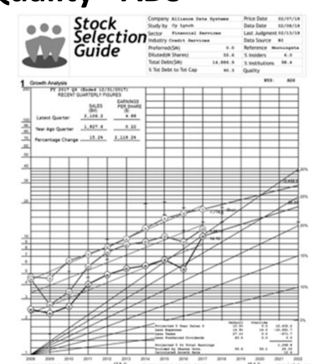
Selling Based on Quality - ADS

- Growth Stock Outlook Feature in April 2018



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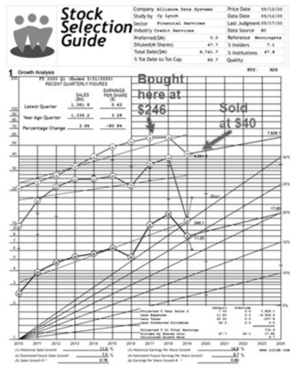
Selling Based on Quality - ADS

- "Sold" from Growth Stock Outlook Portfolio in August 2020 BI Magazine
- 6 straight quarters of falling sales growth (5 were negative)



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Lending Focus to Selling – Value

- Two broad approaches
  - Focus on single stock:
    - Potential stock return significantly below that of market
    - Significantly higher return in potential replacement stock of equal or higher quality
  - Portfolio-centered approach
    - Consider portfolio as a "team," all cooperating on a combined potential return
    - Consider potential return for all holdings, not just one at a time
    - Doesn't usually impact sales driven by poor or declining quality

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Focus on Single Stock

- Potential stock return significantly below that of market
- Not easy: Philip Fisher asks, "How can anyone say with even moderate precision just what is overpriced for an outstanding company with an unusually rapid growth rate?"

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Focus on Single Stock

- Potential metrics:
  - Compound Annual Return on SSG (most important)
  - Sell zone (not reliable by itself)
  - U/D ratio < 1 (not reliable by itself)
  - Current P/E ratio significantly above historical
    - Consider with projected total return
    - Consider as confidence factor, not hard "rule"
- Also consider:
  - Core vs. non-core holding
  - "Blue chip" vs. more speculative

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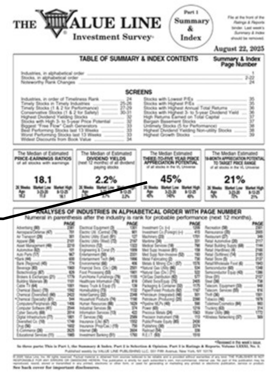
Finding Projected Market Return

- From Value Line (VLMAP)

The Median Estimated
THREE-TO-FIVE YEAR PRICE APPRECIATION POTENTIAL
of all stocks in the VL Universe

45%

26 Weeks Ago	Market Low 3-23-20	Market High 8-12-25
45%	145%	45%



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Finding Projected Market Return

- Calculating VLMAP
  - Formula:
    (Potential Future Value / Current Value) ^ .25 – 1
  - Use 100 plus "Appreciation Potential" from VL as Future Value
  - Use 100 as Current Value
  - (145 / 100) ^ .25 – 1 = 9.73%

Search Google for CAGR calculator

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Finding Projected Market Return

- Calculating VLMAP
  - Formula:
    (Potential Future Value / Current Value) ^ .25 – 1
  - Use 100 plus "Appreciation Potential" from VL as Future Value (100+ 45 = 145)
  - Use 100 as Starting Value
  - (135 / 100) ^ .25 – 1 = 9.73%

The Median Estimated
THREE-TO-FIVE YEAR PRICE APPRECIATION POTENTIAL
of all stocks in the VL Universe

45%

26 Weeks Ago	Market Low 3-23-20	Market High 8-12-25
45%	145%	45%

Search Google for CAGR calculator
Today: https://cagrcalculator.net/

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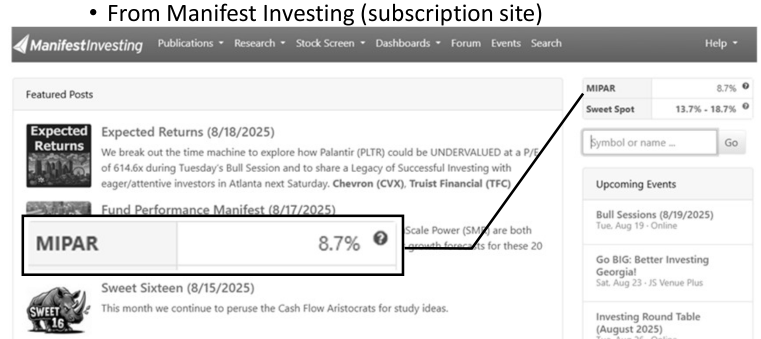
Finding Projected Market Return

- From Manifest Investing (subscription site)



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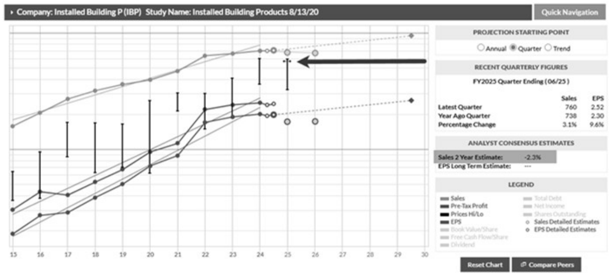
Focus on Single Stock – Non-Core

- Cyclical industry
- Big price run up
- Slowing growth, in large part due to industry pressures



Fundamental Company Data	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Growth (%)	Forecast (%)	5 Yr Est
Historical Sales ($M)	663	863	1,133	1,336	1,512	1,653	1,969	2,670	2,779	2,94	17.9%	6	3,956
Historical EPS ($)	0.85	1.23	1.30	1.75	2.28	3.27	4.01	7.74	8.61	9.10	32.8%	5.8	11.92
Pre-Tax Profit ($M)	42	60	56	72	93	131	155	303	333	346	29.1%		

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Focus on Single Stock – Non-Core

- Projected return below that of the market (7.7%)
- Relies on relatively high projected PE (reduces confidence)
  - Current PE is 30x, same as projected
- Price near all-time high

5. FIVE-YEAR POTENTIAL

A. CURRENT YIELD

Indicated Annual Dividend / Current Price = 3.16 / 266.77 = 0.0118 = 1.2%

B. AVERAGE YIELD - USING FORECAST HIGH P/E

Avg. % Payout / Forecast High P/E = 23 / 30.0 = 0.8%

AVERAGE YIELD - USING FORECAST AVERAGE P/E

Avg. % Payout / Forecast Average P/E = 23 / 19.50 = 1.2%

C. COMPOUND ANNUAL RETURN - USING FORECAST HIGH P/E

Annualized Price Appreciation	6.0%
Average Yield	0.8%
Annualized Rate of Return	6.8%

30x

COMPOUND ANNUAL RETURN - USING FORECAST AVERAGE P/E

Annualized Price Appreciation	-2.7%
Average Yield	1.2%
Annualized Rate of Return	-1.5%

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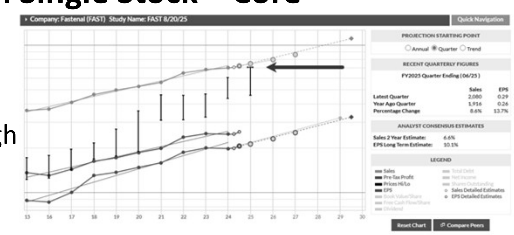
Focus on Single Stock – Core

- Industrials Sector, very high-quality company that's consistent through range of economic conditions
- Long history, "Up, straight & parallel"



Fundamental Company Data	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Growth (%)	Forecast (%)	5 Yr Est
Historical Sales ($M)	3,869	3,962	4,391	4,965	5,334	5,647	6,011	6,981	7,347	7,546	8.4%	9	11,962
Historical EPS ($)	0.44	0.43	0.50	0.66	0.69	0.74	0.80	0.94	1.01	1.00	10.9%	9.5	1.64
Pre-Tax Profit ($M)	826	790	873	987	1,044	1,133	1,208	1,440	1,522	1,508	8.3%		

Evaluate Management	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	21.3%	19.9%	19.9%	19.9%	19.6%	20.1%	20.1%	20.6%	20.7%	20.0%	20.3%	
% Return on Equity	28.7%	26.2%	28.5%	32.4%	30.6%	29.6%	31.1%	34.1%	33.3%	31.9%	32.0%	
% Debt To Capital	16.8%	16.8%	16.5%	17.8%	18.1%	19.2%	17.3%	20.2%	13.8%	11.8%	16.5%	

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Focus on Single Stock – Core

- Projected return less than one-half of market (7.7%+)
- Below "risk free" return of 10-yr. US Treasury (4.3%)
- Current PE at 10-yr high of 48x
- Price at all-time high

5. FIVE-YEAR POTENTIAL

A. CURRENT YIELD

Indicated Annual Dividend / Current Price = 0.88 / 49.90 = 0.0176 = 1.8%

B. AVERAGE YIELD - USING FORECAST HIGH P/E

Avg. % Payout / Forecast High P/E = 70 / 33.0 = 2.1%

AVERAGE YIELD - USING FORECAST AVERAGE P/E

Avg. % Payout / Forecast Average P/E = 70 / 27.50 = 2.5%

C. COMPOUND ANNUAL RETURN - USING FORECAST HIGH P/E

Annualized Price Appreciation	1.6%
Average Yield	2.1%
Annualized Rate of Return	3.8%

33x

COMPOUND ANNUAL RETURN - USING FORECAST AVERAGE P/E

Annualized Price Appreciation	-2.0%
Average Yield	2.5%
Annualized Rate of Return	0.5%

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Portfolio-Centered Decision-Making

- In a nutshell
  - Focus on portfolio as a whole, not individual stocks
  - Make buy, accumulate, sell decisions based on the decision's impact on portfolio as a whole
    - Quality
    - Value/Potential return
- Impact on selling
  - If portfolio return >= target, sale not needed
  - If portfolio return < target, sale needed

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Portfolio-Centered Decision-Making

Where to invest $1000?

- Total Return (TR) in range (15.7%)
- Rank by TR
- Choose highest TR
  - Unless it hurts diversification

Report Options

Summary PERT Diversification

Report Details

Show All entries

				Portfolio Total Value	$176,227.17	Portfolio dollar-weighted average		US/DS: 3.3	%Total Return: 15.7	
Ticker	Company	Price	Shares	Total Value	% of Portfolio	Buy Below	Sell Above	US/DS	% Tot Ret	Rec
TSM	Taiwan Semiconductor	85.37	200.0	17,074.00	9.7	105.20	197.60	6.0	25.4	Buy
CTSH	Cognizant Tech Solns	59.49	200.0	11,898.00	6.8	78.50	132.80	12.3	23.0	Buy
ELV	Elevance Health	450.74	60.0	27,044.40	15.3	461.10	818.00	3.2	18.1	Buy
MA	Mastercard	375.24	75.0	28,143.00	16.0	373.30	670.20	2.9	17.4	Hold
BKNG	Booking Holdings	2687.33	9.0	24,185.97	13.7	2489.70	4235.40	2.3	13.7	Hold
FAST	Fastenal	54.81	350.0	19,183.50	10.9	49.00	76.90	1.8	12.7	Hold
TJX	TJX Companies	78.43	350.0	27,450.50	15.6	73.40	113.00	2.2	12.3	Hold
SYK	Stryker	303.54	70.0	21,247.80	12.1	246.50	361.90	1.0	7.7	Hold

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Portfolio-Centered Decision-Making

Where to invest $1000?

- **TR below goal of 15.0% (at 14.5)**
- Don't want additional TSM or buying more won't bring TR up enough
- Can't find a stock to add enough TR either
- **What would you sell?**

Report Options

Summary PERT Diversification

Report Details

Show All entries

				Portfolio Total Value	$143,345.37	Portfolio dollar-weighted average		US/DS: 2.8	%Total Return: 14.5	
Ticker	Company	Price	Shares	Total Value	% of Portfolio	Buy Below	Sell Above	US/DS	% Tot Ret	Rec
TSM	Taiwan Semiconductor	85.37	100.0	8,537.00	6.0	105.20	197.60	6.0	25.4	Buy
CTSH	Cognizant Tech Solns	59.49	100.0	5,949.00	4.2	78.50	132.80	12.3	23.0	Buy
ELV	Elevance Health	450.74	40.0	18,029.60	12.6	461.10	818.00	3.2	18.1	Buy
MA	Mastercard	375.24	50.0	18,762.00	13.1	373.30	670.20	2.9	17.4	Hold
BKNG	Booking Holdings	2687.33	9.0	24,185.97	16.9	2489.70	4235.40	2.3	13.7	Hold
FAST	Fastenal	54.81	350.0	19,183.50	13.4	49.00	76.90	1.8	12.7	Hold
TJX	TJX Companies	78.43	350.0	27,450.50	19.1	73.40	113.00	2.2	12.3	Hold
SYK	Stryker	303.54	70.0	21,247.80	14.8	246.50	361.90	1.0	7.7	Hold

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Other Considerations

- Generally resist selling part of a position
- Exceptions:
  - Under portfolio-centered approach, selling part is enough to bring return back above target
  - Price appreciation results in stock making up too much of portfolio
  - "Trimming" holding with substantial appreciation to capture gains while wanting to retain holding

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Other Considerations

- Taxes
  - Irrelevant in retirement accounts
  - Don't let tail wag the dog
  - Long-term loss to offset short-term gain (if makes sense for other reasons, too)
  - Ditching close call mistakes
    - About to go long-term
    - At year end, "fall cleaning"

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Wrap-Up

- Buy and hold doesn't mean "buy and forget"
- "Sell" isn't a dirty four-letter word
- Focus on portfolio, not individual stocks, when looking at value
- Don't be afraid to admit mistakes

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Questions or Comments

- CELynch@att.net

Thank You!

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