

# *Company Size vs. Expectations*



## *Mini Investment Class by the OKI Tri-State Chapter*

*Courtesy Cincinnati Model Investment Club  
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# *Market Cap*

- **All of the news media and almost all of Wall Street uses “Market Cap” for size.**
- **“Small Cap”, “Mid Cap”, “Large Cap”**
  - **Market Cap is Price per share times number of shares**
  - **Price goes up 10%, Market Cap goes up 10%.**
  - **Price goes down 10%, Market Cap goes down 10%**

# *Better Investing Size*

- **Because of its dependence on price, a volatile number, we Better Investors do not use Market Cap to measure size.**
- **Better Investors use sales to measure size.**
  - **“Small”, “Mid-sized”, “Large”**
  - **More sales, bigger company.**

## *Boundaries on Size*

- **SMALL**
  - Sales < \$400 Million
  - 70% of all companies in Reuter's screen
- **MID-SIZED**
  - \$400 Million sales < \$4,000 Million
  - 20% of all companies in Reuter's screen
- **LARGE**
  - Sales over \$4,000 Million
  - 10% of all companies in Reuter's screen



## Life Cycle of a Successful Company

Graph from "Fundamental Investing: An Introduction" by Bob Adams, Gary Ball, and Seymour Zeenkov.

# *Start-Up Company*

- **Starts with no sales.**
- **Early sales are “missionary” sales.**
- **Most fail.**
- **Most of the rest fail to grow.**
- **Very big rewards if successful (“IPO”).**
- **Very risky.**

# *Small Companies*

- **Simple market:**
  - **One or two products.**
  - **Little or no competition.**
- **Few pay dividends (no yield).**
- **Need to read MD&A\* to double and triple check quality of management.**
- **Look for well-managed growing small companies with over 15% historical growth rates.**

\* Management Discussion and Analysis found in the Company Annual Report



# *Mid-Sized Companies*

- **Uncomplicated Market.**
  - **Several products.**
  - **Some competition.**
- **Some pay dividends (low yield).**
- **Need to read MD&A to double check quality of management.**
- **Look for well-managed growing mid-sized companies with 10% to 15% historical growth rates.**

# *Large Companies*

- **Complicated Market.**
  - Many products.
  - A lot of competition.
- **Pay a lot in dividends (high yield).**
  - Reinvesting dividends helps our return.
- **Need to read MD&A to double check quality of management.**
- **Look for well-managed growing companies with 5% to 10% historical growth rates.**

# *Diversify by Size*

- **Some have suggested that we invest:**
  - **25% in small companies**
  - **50% in mid-sized companies**
  - **25% in large companies**
- **Percentages are by value**
  - **Price times number of shares in the portfolio.**

# *Small Company 'Problems'*

- **Small companies do not have many shares, hence price is very volatile.**
  - **Fundamentals can be growing for years before the price catches up.**
- **Not all small companies are well managed.**
- **Most small companies fail.**
- **Well-managed small companies tend to become mid-sized companies.**

## *Biggest Small Company Problems*

- **Finding a small company that is well managed and has high growth rates is very difficult.**
- **Keeping a small company when some bad news causes the price to crash.**
  - **Is the bad news temporary or serious?**

## *Mid-Sized Company 'Problems'*

- **Mid-sized companies do not have many shares, hence price is volatile.**
- **Not all mid-sized companies are well managed.**
- **Most mid-sized companies are unable to maintain growth rates.**
- **Well-managed mid-sized companies tend to become large companies.**

# *Large Company 'Problems'*

- **Large companies have many shares, hence price is not as volatile.**
- **Not all large companies are well managed.**
- **Growth for large companies is very difficult.**
- **Where to invest profits?**
  - **Usually pay large dividends, buy back stock, or buy other companies.**

# *Summary*

- **Small Companies – 25% of portfolio**
  - High risk, high rewards.
- **Mid-Sized Companies – 50%**
  - Medium risk, medium rewards.
- **Large Companies – 25%**
  - Low risk, low rewards.
- **In all cases, keep your eye on management and the fundamentals.**



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