

18. Bear-proofing - investing in stocks you know and can support

In a bull market it's possible to make money even if you invest in businesses you know nothing about and which you haven't researched. Bear markets come down hard on such a casual approach.

As a general rule, it's sensible to **invest in companies whose business model you understand**. The added advantage is if you understand it, there's a good chance the management will too! In Warren Buffett's words: "You should invest in a business that even a fool can run, because someday a fool will".

- Look for simple, understandable businesses whose sources of profit and revenue are clear, with brand names you know.
- Look for shares whose businesses you can check out for yourself - by visiting their stores or consuming their products or services.
- Look for companies whose accounts and accounting policies are clear and transparent.
- Read a company's annual report and accounts before committing to it.
- Avoid companies whose management remuneration is excessive relative to the profits the company makes.

When investing in **smaller companies**:

- Look for companies whose senior managers have a significant proportion of their own money invested in the business (i.e. through direct shareholdings, not share options).
- Look for companies with the solid backing of some larger investors.
- Check out local businesses, especially if you have friends and acquaintances working for them or having dealings with them.
- Look for businesses where any specialist knowledge you have enables you to understand them better.

Investing in this way is not about profiting from 'inside' information. Rather, it is about gaining an insight into **what makes the company tick**: whether the company is doing well; whether management is respected; whether the workforce is happy, and so on.

Using **specialist knowledge** to assess an investment has the drawback that you may be too close to an industry to be dispassionate about its prospects and market rating, but equally it can help you spot the good companies from the also-rans.