THE HILLSIDE FACTOR(Y) FOCUS: THE RED ZONE

Over time but particularly during a surging stock market like this, we would like to constantly remind ourselves of our disciplines so as to stay away from unnecessary risks or compromising quality. These are the factors that literally represent absolute no-go areas to help us "kill" an investment thesis. Below are a few of them.

Unproven business economics

Someone recently brought up Celsius Holdings to our attention for our bi-annual webinar. The company positions itself as the front runner for healthy alternative to more conventional energy drinks and has impressively doubled its market share in each of the last three years. However, profits barely show up on the company's financial statements. Hence, we'd like to pass on the stock before it shows us the money -

Loss of competitiveness

Alongside attractive business economics, a proven success in maintaining or even gaining competitiveness in front of customers over time is also critical. We exited our investment in Check Point last year due to its consistently losing market share to major peers. One tip here – when the management shies away from discussing market share while major competitors talk a lot about it, watch out.

Misalignment of interest

Corporate executives are paid for their jobs through shareholders' money. But we prefer to see them motivated by the long-term shareholder return instead of the compensation package. There have been many outstanding businesses that we have passed on due to a lack of meaningful insider ownership or of strong evidence for an owner mindset – Diageo (the largest British spirits company), Domino's Pizza (world's no. 1 pizza brand), and Chemed (the leading operator of end-of-life hospice care and plumbing services in North America), just to name a few.

Excessive debt

It is really difficult for a company without any debt to go bankrupt. Another economic/financial crisis will visit us at some point, although we have no clue of when. What we do know is that once the downside is protected, the upside will take care of itself over the long run. Don't hold your breath waiting for a traditional bank to appear in our portfolio.

Binary outcome

A binary-outcome scenario in the business world can be described as something turning out to be either a huge success or a total failure. Video-game development and drug discovery usually fall into that category. We tend to feel suspicious of such business models due to a low degree of predictability.

It is worth mentioning that we may miss out on some high-returning opportunities by staying miles away from the red zone (as exemplified above) and we are perfectly fine with this. Our foremost job is to invest to not lose money instead of speculating on the "hope" for substantial gains.

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