Podcast Transcript

This is the transcript of Direk Khanijou's conversation with Vimol Kogar on the WTF Show on October 24, 2020.

This transcript has been edited for readability.

YouTube: https://youtu.be/fSEyVlcvR1o

Apple Podcast: https://podcasts.apple.com/gb/podcast/mojo-of-the-markets-direk-khanijou/id1537756394?i=1000498076037

Spotify: https://open.spotify.com/episode/2CV5iGi2BM0xDOVpzreiEl

Simplecast: https://wtf-show-with-vimol-kogar.simplecast.com/episodes/mojo-of-the-markets-direk-khanijou

VIMOL KOGAR: Hello and welcome to the WTF Show. Today we have Direk Khanijou. Welcome to the WTF Show, Direk.

DIREK: Thank you, it's a pleasure to be here.

Tell us a little bit about yourself before we start.

I'm a pretty normal guy. I was born and raised in Bangkok. I went to Shrewsbury International School from Year 6 – 13. I had a great time there. I was on the football team and very much into distance running. After Shrewsbury, I went to UCL. I was there for 3 years and I had a great time at university. Met a lot of interesting people. Learnt a ton. And I discovered Warren Buffett when I was at UCL. That was a big turning point in my life.

After UCL, I came back to Bangkok. The first couple of years were kind of difficult. I was bouncing from job to job and eventually got a job at a real estate company in Bangkok. I was the business development manager. It was a great learning experience. It was like drinking from a firehose. Met tons of interesting people. Worked on some very big deals. Eventually, I felt it was time to join my Dad at the family business. I haven't looked backed since. There's a Turkish proverb that I really like: "no road is long with good company."

The reason you are on the show today is you have a public profile. You seem to know more than the other guys about how to circumnavigate investments. Am I right?

I hope so!

What can you tell us about that?

The website is called rbxinvestments.com. I started the website in 2015 out of my flat in London. Initially it started off as a way for me to journal my investment thoughts. It was like an online journal. Over the years it has grown from that. I didn't have a masterplan when I started it. I look at my website as my serendipity vehicle. It is like an online CV. A chance for me to share what I've learnt along the way and help investors who are starting out today.

Let's say I am an investor and I had 1 million baht. How do I start? The only thing I know is I go to Bualuang in Bangkok Bank and they give me some advice. If I want a relationship with RBX Investments – how do I start?

Right now we are not managing outside capital. Few people have asked me but I have turned them down. The reason I have turned people down is because I want people who are very much in sync with my investment philosophy.

RBX Investments is a long-term, concentrated, value investor. We are very research driven. We own businesses for years and hopefully decades. Right now we are not managing outside capital. I am happy to discuss my investment philosophy.

Yes, please do.

My investment philosophy has evolved over time. There are two ways to invest: 1) you can buy discounted pies and 2) you can buy growing pies. When I was starting out I was very focused on buying cheap stocks – stocks with low P/B, low P/E. I realized that it wasn't a fun way to invest. These were usually pretty crappy businesses and these businesses were cheap for a reason. When you own a bad business, it's a bit like holding an ice cube. The ice is melting in your hand. The value is being eroded over time.

Today, I am only looking to invest in great businesses or what I like to call "business masterpieces." I am looking for a wonderful business, run by a wonderful group of people and I am trying to buy that business at a fair price and own it for the very long term. Life is just more fun when you do that.

Do you want to give us an example of a business like that?

In February 2019, I put out a presentation outlining my thesis on Apple and why Apple was compelling investment and why it was a business masterpiece. The numbers were just so obvious. Back then Apple was – I'm adjusting the numbers here a bit – it was a $700 billion company. It had $100 billion of net cash on the balance sheet. In effect, you were buying the business for $600 billion. It was making about $60 billion a year in free cash flow. So you were getting a 10% free cash flow yield on day one invested capital. And the company was also buying back 6-7% of its shares per year. So your ownership in the company was going up by 6-7% per year without laying out a single extra dollar. Apple is an iconic brand.

There are two parts to Apple: Products and Services. Within the Products segment you have things like the iPhone, Mac, iPad, AirPods. Within Services you have Apple Music, App Store, iCloud etc. The gross margin on Products is 32% and the gross margin on Services is 64% - so double of that. Services is a very good business. Its high margin, growing and recurring. In the end, I decided that this was a great business. This is not a hardware company whose margins are destined to decline. I think it was a no-brainer investment at that time.

Do you have another example of something more current?

Recently I put out a presentation on Progressive which is an auto insurer in the United States. If you're interested you could read that article – I think it's over 10 pages.

Progressive is a very well run auto insurer. The way you look at an insurer is to look at its combined ratio. A combined ratio of 100 tells me that it is underwriting at breakeven. Above 100 means it is underwriting at a loss. Below 100 means it is underwriting at a profit. Progressive's goal is to underwrite at a 96 combined ratio – it's trying to make a 4% pretax underwriting gain. It has an excellent long-term track record. I really like the management team, the culture of the company and I like the price at which it's selling at.

Is that listed on the NYSE?

Yes, ticker PGR.

A lot of people like to talk about what they did right. Let's talk about what we did wrong. I make more mistakes than anybody else. I don't think you could beat me on that one. I would like to talk about fundamental mistakes that first generation investors make. What are the common mistakes?

How much time do you have? Mistakes are great. It's a great way to learn. I think there are two ways to learn 1) learn from your own mistakes and 2) learn from the mistakes of other people. That's a less painful way to learn and my preferred way of learning. You can do that by reading a lot.

A lot of mistakes I see investors make is that they haven't educated themselves on investing. They are kind of rushing into it. Before I got started in investing I read over 100 books on investing. I wanted to make sure that I was ready. Read up a ton on investing. Once you are ready, open a real money portfolio. And when you open that portfolio, do not ever invest using borrowed money. Do not lever up. Do not trade options. Do not short stocks. Do not deal in derivatives.

Do you recommend that we buy debt?

In today's interest rate environment, I do not recommend bonds. History has shown that over the very long term stocks do outperform bonds.

Walk us through the type of books you read. Who are your favorite authors? Just a little bit from that angle please.

The book that really set me on this path was – it's actually my Dad's book – he gave me his copy of Benjamin Graham's The Intelligent Investor. After reading that book a light bulb went on in my head. It was my Road to Damascus moment. I found enlightenment. I thought that this was the way to invest and I am going to go down this rabbit hole.

After discovering Ben Graham, I discovered Warren Buffett.

What does Ben Graham teach us?

Three main lessons from Ben Graham. One, when you buy a stock you are actually buying fractional ownership in a business. A stock is not a piece of paper to be traded back and forth. You are an owner of the business now. If the business does well, you as the owner will also do well.

Two, you should always invest with a margin of safety. Figure out what something is worth and try to pay a lot less for it – leaving yourself a large margin of safety. Don't ever pay full price.

Third, you should look at stock prices as coming from this guy called Mr. Market. Sometimes Mr. Market is very euphoric and sometimes he is very depressed. So stock prices are all over the place. You should take advantage of fluctuations in stock prices.

Ben Graham also talked about the difference between investing and speculating. As an investor you are trying to profit from what the business is going to do – the results of the enterprise. As a speculator, you are trying to profit from movements in the stock price. That's the difference.

Mr. Buffett said that the true test of whether you are an investor or not is if you would be happy if the stock market were to close for the next 10 years and you didn't get a quote on your holdings.

That's an interesting way to look at it. The Oracle of Omaha seems to inspire a lot of people. I think he's moving a little bit into cash?

Yes, he's sitting on record amounts of cash right now. The problem he has is that he's running a very big company and he can only look at very big businesses. Smaller ideas just won't move the needle anymore. You and I don't have that problem.

Does it make sense to hold cash? The big finance companies and investors tell you that cash melts.

I think he's holding cash because he's not seeing good ideas right now. I don't think he wants to hold cash. Cash has option value on every single asset class. So when things do get really chaotic I think Mr. Buffett would step in.

Tell me about the CEOs of the companies you invest. For example, Tim Cook at Apple. Elon Musk is one of my favorites. What do you think of the relationship should be between CEOs and their companies?

I think the CEO should view himself as a fiduciary of the shareholders' money. This is not his company. The shareholders own the company. I like CEOs who adopt an owner mindset. I think Tim Cook adopts an owner mindset.

What's interesting is that there are only 3 CEOs in the world who have created over a trillion dollars in shareholder value: Jeff Bezos, Tim Cook and Satya Nadella at Microsoft.

When I'm looking at a CEO, I'm looking for three things. I want him to have lots of energy, intelligence and total integrity. If he doesn't have total integrity then I want him to be dumb and lazy. You don't want to partner with energetic crooks. You're not going to do well. So I want the CEO to adopt an owner mindset, see himself as a fiduciary of shareholders' money, have good operational skills and good capital allocation skills.

Correct me if I'm wrong, Elon Musk's bonuses are based on the value of the shares. If the shares hit X – then he should get a Y bonus. Doesn't that focus too much on the value of the shares in the stock market as opposed to the performance of the company in the medium and long term?

That is a very strange compensation structure. I don't have much to say about Elon Musk other than that he's a very smart guy. I have read the book by Ashlee Vance. Any guy who can land two rockets at the same time should be taken seriously.

There's a quote I like: "Don't underestimate the man who overestimates himself." That might be Elon.

Even if Tesla does not work. What he's done is that he has lit a fire under the bellies of all the automakers. He has forced GM into EVs. He has forced all these car companies to start innovating again.

Let's talk a little bit about what we shouldn't invest in – whether its gold or cryptocurrencies. Tell me what you think we should move away from.

> That's a great question. There's a saying I like: "all I want to know is where I am going to die so that I don't go there." Invert the question. Figure out what not to invest in and what's left are the things you should invest in. In terms of stocks, you want to eliminate all the bad businesses and things that are difficult to understand.
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> For example, there are 50,000 public companies in the world. I think I understand 50 of them. So there are only 50 companies in my investable universe. That's it. I understand only 0.1% of the companies in the world. And that's okay. It is all about how realistically you define your circle of competence and how well you stay within it.
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> There are certain industries that I don't invest in. For example, anything commodity related, healthcare, pharmaceuticals, biotech.
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> I think gold has value because people give it value. Like a painting. It does not produce anything. It does not pay a dividend. In fact, there is a carry cost to owning gold because you have to store gold. If you think that you might sleep better because you own a little bit of gold – then by all means own the gold. Personally, I don't view gold as an investment. For me, an investment is something that throws off cash. Gold just doesn't throw off cash.
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> Same thing with cryptocurrencies. It hasn't been around that long. I think the people who bought cryptocurrencies are gambling. I don't think it's an investment. But again, to each their own.

Cryptocurrencies remind me of when I was I college. Salman Rushdie came along and we read the book. Nobody understood the book. Yet people were on the streets having protests. I really couldn't understand what he was trying to say. I find it similar to cryptocurrencies. A lot of people pretend to understand what's

going on with cryptocurrencies. Do you think the ordinary person who puts money in cryptocurrencies understand the pitfalls?

No. If you don't understand cryptocurrencies you are thinking about it correctly. That's an area that I'm just not interest in. In fact, I wrote an article warning my friends about dangers of investing in cryptocurrencies. This was in late 2017. The article was called "I've seen this movie before." I compared cryptocurrencies to past bubbles.

There will always be bubbles. In the 1920s in America, auto stocks were all the rage. In the 1960s, conglomerates were all the rage. In the 1970s we had the Nifty Fifty – blue chip stocks – Kodak, Polaroid, Xerox – buy these stocks at 50x earnings and hold them forever. Obviously that didn't work. In the 1980s we had the boom in biotech IPOs. In the 1990s we had the dot com stocks. 2006/7 real estate and housing. The flavor of the day in 2017 was cryptocurrency. And maybe last year it was cannabis. I think if you avoid whatever is hot and popular right now – that's usually a good way to go.

What if I started my portfolio on Monday and I put $10,000 on the FANG stocks – Facebook, Amazon, Netflix, Google. They seem to be safe. And they seem to understand the pulse of the future. Facebook has been eating market share almost every single year. Google is on the verge of an anti-trust suit. It seems that a blind investor could go into these stocks and still see an upside. Am I right or wrong?

I really don't know. That's too hard for me to figure out. What I do know is that these are all fantastic businesses. I don't think they require much capital to run, they generate very high returns on capital, they're drowning in cash and they got great management in place.

But investing is not about identifying good assets. It's about identifying good assets at good prices. These companies are certainly good assets but are they available at good prices? I don't know.

In 2000 Microsoft was the most valuable company in the world. I think its market cap was $600 billion but it was only making about $10 billion in free cash flow. So for the next 16 years the stock went nowhere even though the business was chugging along. The entry price does matter.

What's your plan for the future? Are you going to write a book? I'm curious to know how you are going to publicize things in the future?

I really don't have a masterplan right now. I just want to pump out good content for my readers. Share what I know. And if readers find that interesting, I'm more than happy to talk to them about it.

I think writing online is a superpower. It's an easy way to turbo charge your career and to show people that you are passionate about your work. It is like an online CV. I highly recommend writing online. Instead of being a content consumer try to be a content creator. I think we've seen a shift in that direction.

Tell a little bit about recent books you have read.

I try to read a lot. I divide my readings into two piles – annual reports/financial statements and books/biographies. I am big on business biographies. That's a great way to learn. Reading a book is like downloading somebody's brain for less than 1,000 baht. Why wouldn't you do that?

Investing is one of the few professions where you can really learn by just reading annual reports, books, having a portfolio. A recent book that I just finished is Shoe Dog by Phil Knight, the co-founder of Nike. Amazing book. Another book that I enjoyed is called The Almanack of Naval Ravikant. Naval is a VC. I like Naval because not only is he a brilliant investor but he is happy and successful. And that's a very rare combination. I highly recommend that book. The author has made it available online for free.

Our show is called the WTF Show. It's essentially a youth empowerment show. I'd like you to tell me if you think you've had a WTF moment in the last 5 years. Something that made you pivot your life in a certain direction. Was there a moment like that?

A big moment was discovering Ben Graham, Warren Buffett and all the other great investors out there. That was a big turning point. I think people underestimate the power of compounding. Small incremental actions in the right direction over a very long period of time. PIPER or Perpetual Incremental Progress Eternally Repeated is the formula for success in any field. If you want to learn a new language – it's PIPER. That's the secret. That is what I've tried to do. Focus on small daily actions every single day and just do it for a very long period of time. And hopefully it compounds over time.

For example, if you are getting 1% better every single day. How much better would you be at the end of the year? 37 times. That's amazing.

A lot of youth coming back in 2019/20 into the labor market. With the pandemic, jobs are not easily available. We have kids at home who are looking for jobs on the internet and are a little bit lost. Can you give them advice?

Absolutely. I think adversity, especially early on in life is a blessing. I would start writing online. If you don't know what to write about, start by curating links and articles about the topics that you are interested in. The American rapper Soulja Boy. This is how he started his career. He would put playlists together and he would post it on this website called Sound Click. Eventually he started slipping his songs into the playlists and that's how his career took off. If you don't know what to write about, start by curating links and articles. And share it on your social media platforms.

Another creative way of finding a job is to offer to work for free for one month. No strings attached. Make a list of the people you want to work for. Mail them an envelope with your CV, cover letter and why you would be a got fit for the company. And offer to work for free – tell them no strings attached. One month. If you like me, you keep me, if not, we part ways, no problem. I think that would work.

I'm so happy today you joined the WTF Show. I want to give you the last word. It's a pleasure talking to you today. You seem to have a different point of view than others that I know. You've put yourself out there on RBX Investments. I hope that grows for you. I hope you monetize that at some point.

Thank you for having me on your show. It is an honor and I am deeply humbled. There's a quote by John Lennon and I think it sums up everything that's going on pretty well. He said: "Everything will be okay in the end. If it's not okay, it's not the end." Thank you.