Early Stage Investor

OWNERS MANUAL

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Your blueprint for making millions in the world's fastest growing businesses

INVESTORPLACE

What were you doing in 1992?

The Soviet Union had just collapsed. Bill Clinton defeated George Bush in the presidential election. *Roseanne*, *Home Improvement*, and *Cheers* were huge TV shows. The roaring 90s were just getting started. And a new technology called the "Internet" was being introduced to America.

Now imagine that around that time, you **truly** understood how this new technology would change the world.

Imagine you could see the major new industries that would fan off the Internet's creation in a dozen different directions, like spokes on a wheel.

You could see how people would buy hundreds of millions of computers… and hundreds of millions of software packages to operate those computers. You could see the huge amount of infrastructure that would be needed to carry vast amounts of Internet traffic… how online retail and online media would blossom... and all the other things we take for granted in the 21st century.

If you had that knowledge in 1992, you might have invested in Cisco Systems (CSCO), the world's leading maker of networking gear… the "plumbing" the Internet needs to function.

You could have picked up $1,000 worth of Cisco stock after its IPO. Less than 10 years later, that $1,000 stake would be worth as much as $1,264,000 (a 1,264-fold return).

You might have also purchased shares in Dell Computer, which became one of the world's top computer makers. Just $5,000 placed into Dell stock in the early 90s would have grown into as much as $4.5 million (a more than 90,000% gain).

You might have also picked up shares of Microsoft (MSFT), which became the world's leading computer software maker. The stock gained 9,556% during the 1990s.

An investment of just $5,000… turning into millions of dollars.

It's the kind of monster investment return that can set up you and your family for decades. It can allow you to buy vacations… cars… homes… and just about anything else you want.

Those kinds of investment gains are possible when you invest in businesses and technology that change the world. The greater the change, the greater the gains.

<u>Knowing all this is hugely important right now</u>.

As you read this, we sit on the verge of a transformation very similar to what we saw in the 1990s. Right now, there are a handful of innovations in their early stages that will change our world in a way the Internet did in the 1990s… the way railroads did in the 1800s… and the way the automobile did in the 1900s.

Informed investors stand to make gains similar – possibly even larger – than those made during the Internet boom. I believe there is a small group of industries that are virtually guaranteed to grow 100-fold… 500-fold… even 1,000-fold in the coming years… while delivering their early investors life-changing capital gains.

If you know what's about to happen, you'll look back at this time with a perspective few people ever attain. Instead of looking back with regret and knowing you "missed out," you'll look back with fond memories and satisfaction. This can be the time you lay your first stone in a financial dynasty.

The investments you make over the next few years can secure your financial freedom for the rest of your life. What's coming is that big… and that transformational.

You hold in your hands a "How to Guide" for taking advantage of it. My goal in creating this guide and all the issues you'll receive as a member of *Early Stage Investor* is to provide you with true insight on what is around the corner… what businesses and technologies will change the world… and most importantly, my job is to get you into the next Cisco… the next Microsoft… the next Amazon… the next Facebook… etc.

In the pages that follow, you'll learn all about my strategies for uncovering and profiting from The Next Big Thing. Let's get started…

Everything is About To Change…
Thanks to The Law of Accelerating Returns

Think of the extraordinary change someone born in 1900 could have seen over a long life.

As a child, they would see horses in city streets… and grow up to see those streets full of cars.

They would see the invention of the radio… the airplane… the fax machine… air conditioning… personal computers… and the list of big changes goes on.

<u>I believe those of us who live the next 30 years will see a similar set of changes</u>.

We'll see the world change more rapidly than any other group of people in history.

The way we work, play, travel, bank, receive healthcare, and entertain ourselves will look completely different than they look now.

Large new industries will be created at a pace we've never seen before.

These new industries will demolish old industries at a pace we've never seen before.

And it's all thanks to **The Law of Accelerating Returns**.

If you're on the right side of this law, you're virtually guaranteed to make a fortune.

If you're on the wrong side of this law, you could lose your job and the value of your investment portfolio could crater.

Here's how it works…

Accelerating returns – which is also called "exponential progress" – differs from conventional progress in a MASSIVE way…

You see, conventional progress – the kind of advancement ingrained in the minds of most people - is like going for a walk…

You take one step, you advance one step.

After taking ten steps, you are ten steps away from where you started.

Pretty simple, right?

Well, exponential progress – the kind taking place in technology labs and businesses RIGHT NOW – radically changes the equation…and radically accelerates the pace of change we see in the world.

<u>Exponential progress is progress that multiplies in power and scope with each step</u>.

Exponential progress is progress that "snowballs" and builds on itself. It ensures that each new step is larger than the one that comes before it.

Specifically, the progress made in a step is DOUBLE the amount of progress made in the step that came before it.

For example, if you make exponential progress while taking a walk, you take one step.

Now double that…

… and your second step is the equivalent of two regular steps.

Now double that…

… and your third step is the equivalent four regular steps.

Now double that…

… and your fourth step is the equivalent of eight regular steps.

By the time you get to the 10th step, your step is the equivalent 512 steps!

And by the time you get to the 20th step, your step is the equivalent of 524,288 steps!

The Second Half of the Chessboard

Here's an old legend that helps illustrate the power of exponential growth…

Hundreds of years ago, a king invited a traveler to play a game of chess.

The king loved chess, and very much wanted a challenge. The king told the traveler that he could name his reward if he won the game.

In response, the traveler modestly asked for some rice. He asked the king to give him a single grain of rice on the first square of the chessboard and then give him double the amount – two grains – and place it on the next square and give him double that amount – four grains – and keep doubling the amounts for each square on the chessboard.

The king lost the game.

Being a man of his word, he called for a bag of rice. The king placed one grain on one square, two grains on the next one, four grains on the next one, eight grains on the next one, and so on.

By the 16th square, the king felt the numbers were getting very large. He owed the traveler 32,868 grains of rice on that square.

Soon, the king realized that because of exponential growth, he could not fulfill his promise, for on the 21st square, he would need to put down over 1,000,000 grains of rice.

By the 31st square, he would need to put down over one billion grains of rice.

And finally, on the 64th square, the king would need to put down 18,000,000,000,000,000,000 grains of rice, which was more rice than the kingdom could produce in over 100 years.

That is the power of exponential progress.

By the time you get to the second half of the chessboard, each stage of growth produces massive change relative to the early stages.

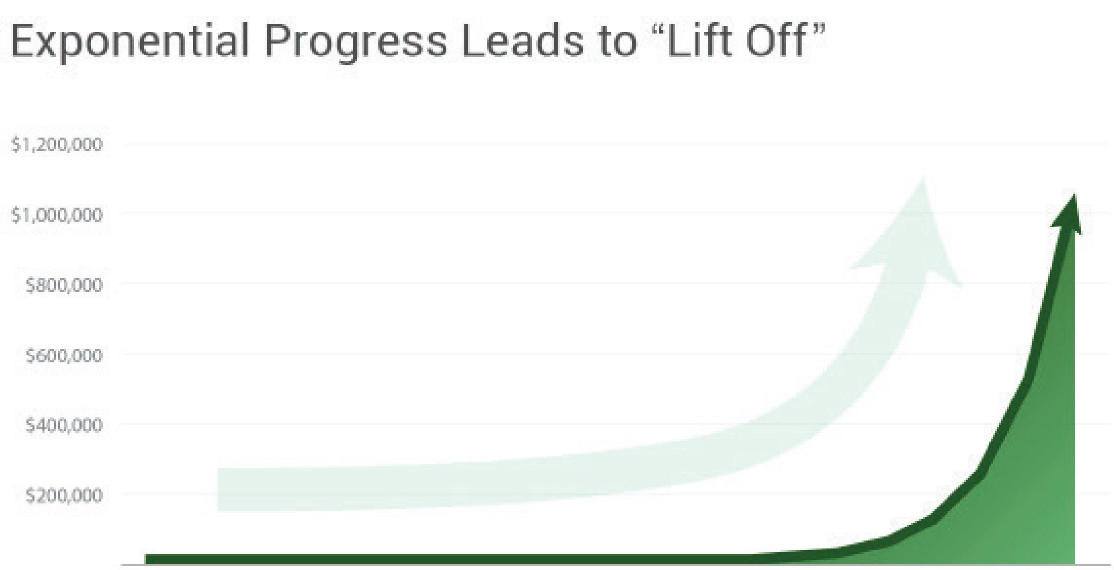
Again, exponential progress is progress that "snowballs"… each step in the advancement is double the one before it.

Knowing the difference between linear growth and exponential growth instantly sets you apart from your fellow investors and give you a huge advantage over them. It can literally make you millions of dollars over the coming years.

When a small number grows at an exponential rate, the first stages of growth aren't incredible. The growth shown on a chart does not soar upward during the early stages.

The extraordinary growth happens at an "inflection point" in time…when the exponential growth begins to snowball and makes things change at stunning rates.

This is the "lift off" point you see on the chart below:



Over the last four decades, advancements in computing power, data storage, telecommunications gear, and other technologies have followed a trajectory like you see on the left side of the chart.

This is because they started at very low levels. But after many years of advancing at exponential rates, the technologies I just listed are entering the "lift off" phase.

This is why many technologists say that when it comes to computing power, we are crossing over to "the second half of the chessboard."

Computing power is advancing at incredible – and accelerating – rates. At the same time, the cost of computing power is plummeting.

An Incredible Story of Progress

A great example of how fast our world is changing is the story of "ASCI Red."

In 1996, the ASCI Red Supercomputer was the world's first computer to reach the speed of 1 teraflop. It cost $55 million to build. It occupied a footprint about the size of a tennis court.

In 2014, Sony released its PlayStation 4 video game console. The PlayStation 4 had almost twice the computational power as ASCI Red. It could fit in a backpack. And its price tag was less than one thousandth of ASCI Red's.

This simple story shows you how computers are getting much more powerful, much faster, much smaller, and much cheaper.

This has huge implications for our world.

Although computers and telecommunications gear have changed our world over the past 30 years, they are set to change it a lot more.

Remember, our "new economy" – our software, our smartphones, our apps, our websites, our email – rests on a foundation of computing power.

Computing power makes all these things possible:

- "Face Time" video calls with loved ones
- Email
- Managing the hi-tech factories that make our cars
- Smartphones that can take pictures
- Electronic medical implants
- Electric cars
- YouTube videos
- Systems that keep our power grid up and running
- Useful spreadsheets at work
- Advanced record keeping
- Making travel plans with Uber and Airbnb
- And thousands of other things.

After years of relatively modest advancement, computing power is now entering the "lift off" stage.

This key ingredient of our modern world is exploding in power and speed. This will change the world at ever increasing rates.

This rapid increase in the rate at which the world is changing has stunning business and investment ramifications.

The world around is changing at never-seen before speeds… and catching many people off guard.

Over the last few decades, it took on average about 20 years for the typical Fortune 500 company to reach a market capitalization of $1 billion.

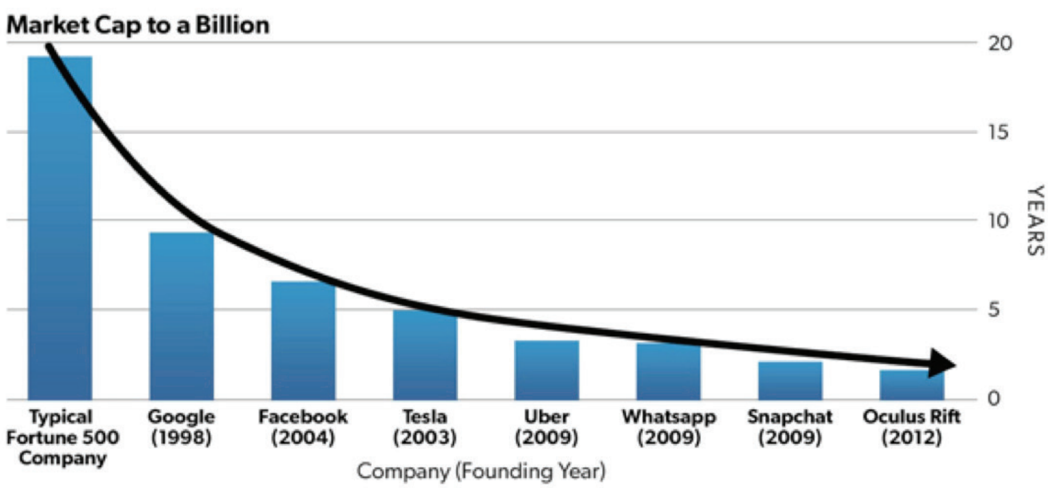
In 1998, Google reached $1 billion in market cap in just eight years, which was considered incredible.

By 2004, Facebook had done it in just five years.

By 2009, Uber had done it in under three years.

In 2012, virtual reality firm Oculus did it in under two years.

The chart below displays the amount of time it took for companies to hit a billion-dollar market cap.



As you can see, it's taking less and less time to generate incredible wealth.

Investors are enjoying the benefits.

Facebook shareholders who bought at the IPO enjoyed a 200% return on their investment in just four years.

Early Tesla investors made over 2,000% gain. Early Google investors made over 2,400% gains.

By now, you can see how the time it takes for massive change is getting "compressed."

Industries are being transformed in a short time.

New industries are springing up at a rapid and ever increasing pace… while old industries are being demolished at a rapid and ever increasing pace.

As Uber soared to a billion-dollar valuation, the old taxi industry was devastated. It lost hundreds of millions in revenue.

As Apple's iPhone dominated the smartphone market, the losing competitor, Blackberry, saw its share price plummet more than 90%.

These incredible industry shifts used to take 20-plus years to play out.

Now, they are playing out in less than 5 years.

And it's all thanks to the Law of Accelerating Returns… all thanks to exponential progress.

It Only Takes One: How to Make Millions with the "VC" Approach

What would you do with an extra million dollars in cash?

Retire tomorrow? Buy a new house? Buy a Ferrari? Put it in the bank and massively increase your financial freedom?

Sure, it's nice to daydream about having an extra million dollars in the bank. But I'm asking you this question because it's a real life situation the financial bankers of early-stage companies – venture capitalists – often find themselves in.

When it comes to extreme wealth creation, few endeavors can compare to being an owner of a small company that grows large.

As I mentioned in the start of this handbook, an early investor in Microsoft could have made over 9,000% during the 1990s. That type of gain turns every $5,000 invested into $450,000.

It only takes one of these big hits to make a huge amount of money in early-stage companies.

And that is why it is critical that you approach the companies we recommend in this service with a "venture capitalist" mindset.

What are venture capitalists? And how do they earn such massive returns?

Venture capitalists are the early backers of startup companies. They are the grand slam home run hitters of the investment world. They don't look to make 300% on their investments. They look to make 3,000%... even 30,000%. Make just one great venture-capital investment and you'll probably never have to worry about money.

Venture capitalists have funded nearly every mega-hit technology company you know today: Google (now Alphabet), Facebook, Twitter, Uber, Airbnb, Pintrest, and the list goes on and on.

Before the public learned about these innovative businesses, venture capitalists were there, performing due diligence and making early investments. By the time regular stock market investors hear about your average technology winner like Google, venture capitalists have made more than 2,000% on their original investments.

And while we don't recommend non-public companies in this research service, we still very much employ a venture capital mindset. We are looking to hit grand slam home runs. We are looking to make hundreds, even thousands of percent returns in the world's best early-stage public companies.

The Early Stage Investor's Analytical Model: A Recipe for 1,000%+ Gains

As a reader of Early Stage Investor, it's critical that you know we use a unique five factor analytical model to evaluate early-stage technology companies.

In my experience, the biggest early-stage technology stock winners tend to have five key qualities that define their businesses. While not every single winner has all five qualities, most do. And the more of these qualities you see in an early-stage tech company, the greater your chances of investment success.

I like to frame our model as a series of five questions. Every company we risk our hard earned capital on must answer the questions to our satisfaction… or have a clear path to producing good answers:

Question #1: Are you hunting elephants or hunting mice?

Every company – no matter what industry it is in – has a critical choice to make.

Will it try to conquer a giant market, a medium market, or a small, niche market?

For example, Amazon, Google, and Facebook all went after giant markets. Amazon went after books and then retail. Google went after the search market. Facebook went after the broad-use social media market.

In contrast, a company that sells software to the legal industry is in a niche market. That kind of "niche" market is dwarfed by the markets I described above.

Although niche market companies can do well, as early stage "venture capital" investors, we're much more interested in owning companies that are going after massive or potentially massive markets. We want to hunt elephants, not mice.

It often takes the same amount of planning… the same amount of creative thinking… the same amount of man hours… the same amount of back-office expenses… and the same amount of marketing creativity to prosper in a $100 billion market as it does a $1 billion market.

You might as well do all of that work and thinking in the pursuit of a huge prize instead of a small prize.

This is why we are on the hunt for companies that are going after giant or potentially giant markets. Don't get me wrong. We will occasionally invest in small companies going after smaller markets. Many small companies have struck it rich in smaller markets and delivered 1,000%+ returns to investors (we see this happen most often in the biotech industry). But typically, I prefer to invest in companies going after giant markets.

Question #2: Is the company's technology CLEARLY better or MUCH cheaper than its competitor's technology?

Almost everybody has lived through a "systems change" horror story sometime in their professional lives.

Most of these horror stories go like this: A company someone works for or owns decides to switch to a different software system, different phone system, different website, or a different payroll system, etc. Although the company selling the new system promises everyone that the change will be quick and easy, it turns out to be a miserable slog that causes tons of problems.

Since so many people have lived through a "system change" horror story – and since people are naturally resistant to change – any new way of doing anything must be CLEARLY better or MUCH cheaper than the current (aka, "old") way of doing things.

That's why as early-stage technology investors, we can't risk our capital on companies with products and services that are "just a bit better" or "just a little cheaper " than products and services already on the market and in use. Those companies are very unlikely to change the behavior of potential customers… and very unlikely to succeed.

Instead, we want to own innovative companies with new products and services that are CLEARLY better or MUCH cheaper than what is already out there. It's often said that a new technology must be 10 times better or just 10% of the cost of existing technologies in order to get people to change.

Remember, people hate change. That's why any company we back with our capital must be doing something that is CLEARLY better or offering a similar product or service that is MUCH cheaper than its competitors.

Question #3:
Is the business scalable?

Scalability.

It's one of the most repeated words in Silicon Valley for good reason. A business must have scalability in order to grow large in a short time (aka, "Make you lots of money quickly").

Scalability is the ability of a business to massively grow revenues while minimally growing the costs associated with producing those revenues.

For example, a lawn mowing business is not scalable. If you own a lawn mowing business and want to double in size, you'll have to buy twice as many lawn mowers as you have now and you'll have to hire twice as many lawn mower operators as you have now. Because of this, your revenue cannot soar far beyond your costs.

On the other hand, you have businesses like Facebook and Twitter. These businesses are very scalable. It took a lot of work in the early days to create the technologies and businesses behind Facebook and Twitter, but once they were created, these two businesses could add new users and increase their advertising revenues much, much faster than they increased costs. Their market values exploded higher as a result.

Software companies are very scalable as well. A software company like Microsoft will spend money and time creating and developing software like Microsoft Office. But once it has the product created, it can produce and sell additional copies of the software at minimal cost. The revenues can rise much faster than costs.

Don't get me wrong: owners of non-scalable businesses (like a lawn mowing business) can grow very wealthy. Many people have done so in the past. Many people will do so in the future. But if your goal as an investor is to own shares of businesses that can make you a lot of money quickly, then you must focus your attention and capital on scalable businesses.

Question #4:
How big is your moat? Do you have a big competitive advantage?

The brilliant investor Warren Buffett has helped make the term "moat" one of the most popular words in the investment world. And for good reason. You want every company in your portfolio to have as much moat as possible.

"Moat" is how resistant a company's business model is to outside competition. The name comes from the time when a wide moat could keep people inside a castle safe from invaders.

Free market capitalism is survival of the fittest. As soon as one company is successful in one area, dozens of competitors will rise up to imitate it or decapitate it. Today's big winner can be tomorrow's roadkill.

That's why a critical part of our analysis process is studying a company's competition. We study their products, services, patents, marketing strategies, people, and distribution networks. We always want to own companies that are several steps ahead of the competition.

These days, a key part of studying any technology business's moat has to factor in the 800-pound gorillas of the industry. I'm talking about Amazon, Google, Facebook, Microsoft, Intel, and other giant businesses.

These companies have incredible resources on hand at all times. They have the biggest research & development budgets. They have the most political power. They can pay top people the most money. They have the biggest distribution networks. A giant like Facebook can easily allocate $2 billion towards a new project, which is more than your average small cap tech company's entire market value.

When one of the 800-pound gorillas decides to get into a particular industry, it's always a major concern for the current smaller players.

Don't get me wrong. David often beats Goliath in business. American history is full of stories of upstarts thriving despite attacks from larger companies. But no analytical process of early-stage tech companies would be worth its salt if it didn't study the potential threats from the giants.

Question #5:
How much are you worth?

Figuring out what an early-stage company is worth is one of the most difficult tasks in all of finance. This is because most early-stage companies earn little to zero profit.

For example, some small tech and biotech firms generate almost zero revenue because they are basically science projects. They've raised money from investors and are spending it on research and development. They hope their work will lead to a breakthrough and huge sales.

Of the early-stage companies that do generate sales, many of them plow the money into growing the business, leaving no profit at the end of the year.

Because of all this, using conventional valuation metrics like the price-to-book value or the price-to-earnings (P/E) ratio are often useless when it comes to valuing early-stage businesses. This means that conventional stock screens are also pretty much useless for uncovering potential early-stage winners.

I believe this is a great thing for us. Most people prefer doing things the easy way. Since uncovering and valuing early-stage companies is harder than valuing conventional businesses with conventional earnings, less people do it.

So much of our analysis comes down to old-fashioned detective work. Instead of using cookie cutter valuation metrics, we base our valuations on how assets are being valued in specific industries, potential market sizes, and the quality of innovations.

I spend thousands of hours per year speaking with industry experts… attending conferences… personally testing products and services… evaluating business plans… poring over balance sheets… and studying industry reports.

After all that work, I arrive at the valuations I place on companies… and of course look to buy them at discounts. It's just as much art as science, and it will never fit inside a conventional stock screener.

One key thing here to know: Depending on conventional metrics like the price-to-earnings ratio won't help you with early-stage companies. Avoiding companies with high price to earnings ratios (or no earnings) will cause you to miss out on many early-stage winners. Just because a company looks expensive based on earnings doesn't mean it can't be a great investment.

How to Buy Early-Stage Companies Like a Pro

We'll build our wealth investing in smaller companies that go on to become bigger companies – and their share prices get a lot bigger, too. As I mentioned, it's a venture capital-like approach, which is why the potential upside is so big. Because we'll be owning smaller companies, from time to time we may need to be a little more strategic in how we buy and sell. We do that through limit orders.

Every time I recommend a stock to you, I will give you the highest price you should pay – a buy limit. I base these limits on a variety of factors – including valuation, sector growth, company growth, the chart and more – and I encourage you to take them seriously to maximize your returns.

Smaller companies are sometimes not as liquid as bigger stocks, meaning they have fewer shares that trade on the open market. When that is the case, the stock's price can move quickly if all of us in Early Stage Investor try to buy or sell a stock around the same time. Part of it is simple supply and demand. The price goes up when investors are buying. Part of it is also the market makers, or specialists as they are called. These are the people that facilitate the transactions between buyers and sellers. They will see the increased number of buy orders hitting and mark the price up. That's how they make their money, and they don't need to take any of ours.

Limit orders are the way we protect ourselves. We specify the maximum we are willing to pay for a stock we are buying, and we specify the minimum we are willing to take for a stock we are selling. That way we buy or sell on our terms and not somebody else's.

These are easy to set with your broker, and they are especially important when it comes to lower-priced stocks. For example, if I recommend you buy a stock that is trading for $2.75 and a flurry of buy orders runs it up to $3 or higher, that's already a 10% difference, which is the market's average gain for an entire year.

Let me pause for a moment to say that I know we are investing for big gains over a period of a year or probably longer, so to some degree we need to be flexible with pricing and realize that some of these fluctuations are inevitable. If we end up selling that $3 stock for $9, even a 10% difference on our buy price is acceptable.

Still, I absolutely hate paying more for a stock than I need to, and I'm sure you feel the same way. Conversely, I also hate selling a stock for significantly less than what I know we can get for it. Limit orders will help us strike the proper between maximizing our returns while also keeping the long-term view in mind.

In addition, not overpaying is smart risk management. We know that not every stock we buy is going to work out for us, and getting in at a good price limits the downside risk on the ones that don't.

Okay, back to limit orders. Here is what you will need to know to set your orders:

Price: I will always give you a buy limit for a new stock, so you will set that as your limit order price. That is the maximum you will pay for a stock we're buying, so the order will fill at or below that price. The reverse is true for a sell. We may sell some stocks at wherever they are trading that day – which is a market order – but other times we will draw a line in the sand and accept nothing less than a certain price. With a sell limit order, we will only sell when the stock is at or above the price we want.

Duration: You can set a limit order to last just for the rest of that trading day (called a "day order" appropriately enough) or until you cancel it. This is called a Good-Til-Canceled order, or GTC for short. I want you to use GTC orders. We may need to be patient on occasion for a stock to hit our price, but it will be worth it.

Despite their name, GTC orders aren't literally good until you cancel them. They expire after a period of time, and that time varies from broker to broker. They typically remain in effect for at least 30 days, and I've seen some at 180 days. I don't expect we'll need that much time, but it is something to be aware of. In the rare event that we do have an order in place that long, you may need to extend it or re-enter it upon expiration.

Also, if you buy large blocks of shares in a company, usually 100 or more, you may find that your order gets filled in chunks. This is called a partial fill, and you do have the power to override that by setting the order as "all or none." Partial fills are fine, and I recommend you stick with those.

That's an introduction to limit orders and how we'll use them. If you don't have much experience with limit orders, don't worry. Once you've done one, the rest will be a piece of cake.

In the end, strategic use of limit orders can impact your returns on a trade more than you might think. Add that up across multiple trades and over time and the extra money you have in your account can be significant.

How to Size Your Positions Like a Pro

All too often, investors get excited about a company's prospects, think about all the money they'll make, and buy some stock. They don't spend two seconds thinking about an absolutely critical component of investment success.

That component is called "position sizing."

Position sizing is the part of your investment strategy that determines how much of your portfolio you place into a given stock, ETF, mutual fund, or bond.

For example, suppose an investor has a $100,000 account. If he buys $3,000 worth of stock in a company, his position size would be 3% of his capital. If he buys $10,000 worth of stock, his position size is 10% of his capital.

Position sizing is MUCH more important to your investment success than any one single stock position.

Smart position sizing is one of the important ways investors can protect themselves from what's called a "catastrophic loss."

A catastrophic loss is a loss that erases a big chunk of your investment account. It's the kind of loss that can end a career… and even a marriage.

The catastrophic loss typically occurs when an investor takes a much larger position size than she should. She'll find a stock that she is very excited about, start thinking of all the profits she could make, and then make a giant bet.

She'll place 30%, 40%, 50% or even more of her account in that one stock. If that stock plummets in value, the account takes a huge hit.

The obvious damage from a catastrophic loss is financial. If an investor with a $100,000 account suffers a catastrophic 75% loss, he is left with $25,000. It takes most people years to make back that kind of money from their job.

The less obvious damage a catastrophic loss can inflict is mental trauma. It's crushing to know that you blew a big portion of your wealth with such a dumb move.

People can get knocked out of the investing game forever.

To avoid catastrophic losses, your first line of defense is to size your positions correctly. Most experienced investors will tell you to never put more than 4% of your portfolio into any one stock. Others will tell you to never put in more than 5%.

When investing in volatile, early stage companies position sizes should be smaller... like half a percent of your portfolio… or 1% of your portfolio.

This concept is critically important to your success, so I'll state it again for emphasis: We are investing in early-stage companies, which have a higher failure rate than established businesses.

That's why it's critical to size your positions intelligently. A good rule of thumb is to never put more than 1% of your portfolio into an early-stage company.

How to be Right Just 33% of the Time and Still Make a Fortune

To the average investor, a 33% “win rate” on stock buys is a depressing thought.

Having a high “win rate” – like “8 out of 10 stock picks are winners” - is important to average investors.

However, the best venture capitalists and professional traders don’t place any emphasis on “win rate.” They know that with a good strategy, you can be right just 33% of the time and make a fortune in stocks.

Early-stage stocks are among the riskiest securities on the market. They are more volatile and have higher failure rates than established businesses like Walmart and Coke. That’s just the nature of the game… and that’s why the payoffs in early-stage investments can be so huge.

Because early-stage companies can produce such gigantic capital gains – and because they have higher failure rates than established businesses - it’s vital to understand a key money management principle used by the best venture capitalists.

As an early-stage investor, you’re not going to achieve success on 100% of your investments. You probably won’t achieve success 75% of the time… or 66% of the time.

And that’s fine.

When you invest like a venture capitalist, you can be right just 33% of the time and still make HUGE returns.

Some simple math shows us how it works…

Let’s look at a hypothetical investment example.

On December 1st, you structure a “venture capital” portfolio of 12 promising businesses. You hold them for a year. The returns of these 12 stocks are listed to the right.

Stock 1	-41%
Stock 2	-99%
Stock 3	-61%
Stock 4	385%
Stock 5	142%
Stock 6	-55%
Stock 7	64%
Stock 8	-36%
Stock 9	280%
Stock 10	-45%
Stock 11	-22%
Stock 12	-38%
Average gain:	**40%**

In this example, four went up and eight went down. You were right 33% of the time. But because you hit just a few big winners, you made a great average return of 40% across the 12 positions.

Over the past 60 years, the legendary trader George Soros has made more than $20 billion in the financial markets. Soros is a genius at knowing how government actions affect markets. He’s skilled at finding industries poised to boom. But there's a simple mindset that's more responsible for Soros' success than either of those things. Soros once summed it up like this:

"It's not whether you're right or wrong that's important, but how much money you make when you're right and how much you lose when you're wrong."

Soros didn't focus on how often he was right. He focused on making his successes big and meaningful… and making sure his mistakes were small and manageable. That's what we need to do as well.

I get how people feel the need to be right. I like to be right as much as anyone. In my early years as a stock broker, I had a boss once ask me "do you want to be right or rich?" I did not answer him, but I knew immediately what the correct answer was. I try to reduce my downside risk as much as possible. But the simple fact is that early-stage companies carry risk. I know I'm not going to be right 100% of the time.

The good news is, when you make sure to win a lot when you're right, and only lose a little when you are wrong, you can be right just 33% or 50% of the time…and still make **huge** profits in early-stage companies.

How the "Buy a Basket" Approach Works

Another way we can reduce risk, be wrong once in a while and still make a fortune is by using a technique I call the "buy a basket" approach.

During an industry's early stages, we often see dozens of companies working furiously to become the winner of whatever epic business race they are in.

In the early days of the internet, lots of companies tried to create the best online store… the best email system… the best search engine, etc. In the early days of the automobile industry, more than 100 carmakers tried to become the industry leader.

During the early stages of an industry, it's virtually impossible to consistently pick the one or two companies out of dozens that will emerge as the winner(s) in 10 years' time. Placing all your chips on just one or two companies is often an extremely risky way to invest in the sector.

Instead of placing an all-or-nothing bet, I prefer to "buy a basket" when I can.

Putting all your money in a single company can pay off big if it "threads the needle" and comes out on top. But investing in one company exposes you to significant downside risk. If there is a major problem at your chosen company (like a technology problem, an accounting scandal, or a crazy management decision), you could suffer a big loss.

That's why I like the "buy a basket" approach.

When I say, "buy a basket," I mean pick three to six of the best companies in a sector – and buy all of them.

By purchasing a basket of the best companies, you get lots of upside potential, but a good measure of diversification and downside protection. You avoid the risk of losing big on one concentrated bet.

When you buy a basket of three to six companies, you'll probably wind up holding some losers. But the winners will more than make up for them, providing you with an outstanding "blended" return.

To be clear, when I say, "buy a basket," I DO NOT mean "buy an ETF."

ETFs can be useful investment vehicles. But when you buy most ETFs, you end up buying over 40 companies. You end up owning a lot average or crappy companies. You get the bad with the good… which dilutes your returns.

That's why I see "buy a basket" as an excellent middle-of-the-road approach.

It's not always possible to buy a basket in a sector. Sometimes, there aren't many good individual companies trading at good prices in a sector at the same time.

But when it's possible to do so, buying a handful of high-quality companies is a great way to invest in an industry during its early stage. We get exposure to high-quality businesses, but we avoid single-company risk.

Why Not Seeing a Stock Quote Every Day Can be a Great Thing

Many investors can't stand the thought of going a week or even a day without checking stock quotes. They're addicted to the constant checking in on changing stock prices.

I'll admit, I frequently check on the markets and my stocks. But when it comes to investments in early-stage companies, NOT having access to stock quotes can be a great thing.

The very nature of a private company is that it does not have a publicly traded stock. The value of that private company may change from month to month, but you won't see it reflected in any regular share price quote. The value is what knowledgeable insiders and shareholders know it to be.

If you can't access an up-to-the-second quote on an investment, there's less pressure to get upset over every 5% or 10% or 20% decline in the share price… so there's less mental pressure to panic and hit the "sell" button.

Consider the story of privately-held Uber. As I write this, the company is a dominator of the ride-sharing space. But it has taken many bumps and bruises along the way. The journey to the top of the heap for any company is typically very volatile.

If Uber was public during its rise, I'm sure many investors would have freaked out during one of its many periods of difficulty and sold shares. However, since Uber was private during the rise, no conventional stock quotes were available.

This was a good thing for many investors. It helped them hold onto their shares and make many multiples of their original investment.

It works the same way with real estate investments. It's good that people can't get daily quotes on the value of their real estate holdings. It helps them ignore short-term noise and focus on long-term wealth creation.

When it comes to investing in early-stage public stocks, employing the venture capital or professional real estate investor mindset will help eliminate any emotional decisions to sell. When emotions are removed from investing, the success rate increases exponentially.

How Coffee Cans Can Help You Get Rich in Stocks

Do you remember coffee cans?

Now that our days are filled with Starbucks trips and single serve "K cups," it's easy to forget that large coffee cans were once fixtures in millions of American homes.

Here's what I'm talking about…

It might sound funny, but coffee cans can teach us <u>an extremely powerful</u> investment lesson. Coffee cans are behind an enlightened way of thinking that could help you get rich in the kind of stocks we cover in *Early Stage Investor*. Having "coffee can knowledge" is truly one of the differences between the rich and the poor.

The coffee can story is most famously recounted by Robert Kirby, an investment manager from days past.

Kirby wrote that, "*The coffee can portfolio concept harkens back to the Old West, when people put their valuable possessions in a coffee can and kept it under the mattress.*"

The coffee can method of portfolio management is simple: You buy high quality businesses with promising futures.

But instead of doing what many folks do – which is check on share prices every day, fret constantly about the portfolio's short-term performance, and trade in and out of shares – you do nothing but sit on the portfolio for years.

You stuff your shares in a figurative coffee can, put the can in the cupboard, and don't look at it for long stretches of time.

The coffee can idea came to Kirby while he was at investment firm. He had a client whose husband, a lawyer, had died. The client inherited the stock portfolio, which she brought to Kirby. Kirby writes:

I was amused to find that he had been secretly piggybacking our recommendations for his wife's portfolio. Then I looked at the size of the estate. I was also shocked. The husband had applied a small twist of his own to our advice: He paid no attention whatsoever to the sale recommendations. He simply put about $5,000 in every purchase recommendation. Then he would toss the certificate in his safe-deposit box and forget it.

By ignoring any "sell" advice and socking the shares away, the husband had allowed a kind of wealth creation magic to happen…

Sure, there were some losers in the portfolio, worth less than $2,000. But he had several large holdings worth more than $100,000 each. And get this: *there was also one giant holding worth more than $800,000.* That holding was born from a small investment in Haloid, which became a large amount of Xerox shares.

This utterly inactive portfolio approach stands in stark contrast to how most individual investors manage their money. They jump in and out of stocks, take profits too early, get too impatient, worry over meaningless day-to-day stock movements, and check price quotes all day.

Most folks would be better off managing their stocks like the lawyer from Kirby's story: **Buy good, promising companies and sit on them**.

I can't tell this story without also mentioning a client study the huge investment firm Fidelity supposedly conducted years ago. Fidelity studied client accounts that had the best returns. It found that the top performing accounts were owned by folks who forgot they had an account at Fidelity.

I don't know if this study actually took place, but I wouldn't be surprised if that's the case at most investment firms and brokerages.

In *Early Stage Investor*, we take the venture capital approach to investment. We buy small, promising businesses with the potential to massively increase in value.

However, those massive increases in value don't happen overnight.

And sitting tight with the coffee can approach in mind is often the most useful thing we can do on any given day.

I have had my own personal experiences that helped me understand and believe in the merits behind the coffee can approach.

In 2003 at the ripe age of 27, I started my first investment firm, Penn Financial Group. I couldn't have done it without my first client, a former consultant at my prior company who had told me he would be my first client if I ever went out on my own. I took the gamble and have never looked back.

With only a few clients, every investment was that much more important. One of the first stocks I ever bought for my Penn Financial Group clients was a little-known surgical robotics company called Intuitive Surgical (ISRG). At the time, in early 2004, the stock traded around $15 per share ($5 split adjusted).

In a few short weeks, it rallied to around $20 (pre-split), and the position was quickly up over 30%. Annualized out, we were looking at a big triple-digit gain.

Even though I believed the company was in its infancy stages, I felt the quick +30% was too much to risk losing, and I decided to bank the profit and make my clients happy. And yes, they were very happy… at the time.

In the next 15 years, Intuitive Surgical became the global surgical robotics leader. Adjusted for a stock split in 2017, the stock increased from the $5 entry in 2004 to a high of $589 in April 2019. That is a 117X return.

Every $5,000 invested in Intuitive Surgical in 2004 would have been worth nearly $600,000. Every $10,000 would have been close to $1.2 million.

I wish I had utilized the coffee can approach in 2004.

It is never too late. And if you continue to follow my investment strategy in *Early Stage Investor*, odds are good we'll find a few more Intuitive Surgicals in the coming years.

Summing Up

By investing in the best early-stage companies, we invest in companies that will change the world. We're looking to get in early on the next Microsoft… the next Facebook… the next Google. It only takes one of these winners to radically increase your net worth. By using the strategies and mental tools I've covered in this report, you'll own the future… and reap the rewards,

Regards,

Matt McCall
Early Stage Investor