SIMPLE IS BETTER

JIMIT ZAVERI 12/30/16 LUCKY IDIOT

SIMPLE IS BETTER – ISSUE -3 – EXPECTATION V/S REALITY

In my previous issues, I had talked about the power of compounding, essential points to keep in mind for getting benefits from the power of compounding. Now, in issue 3, I am going to talk about distinguish between expectations and reality.

The majority of our acts is results of our expectations. We take many steps for fulfilling our expectations. Expectations always play a vital role in our life.

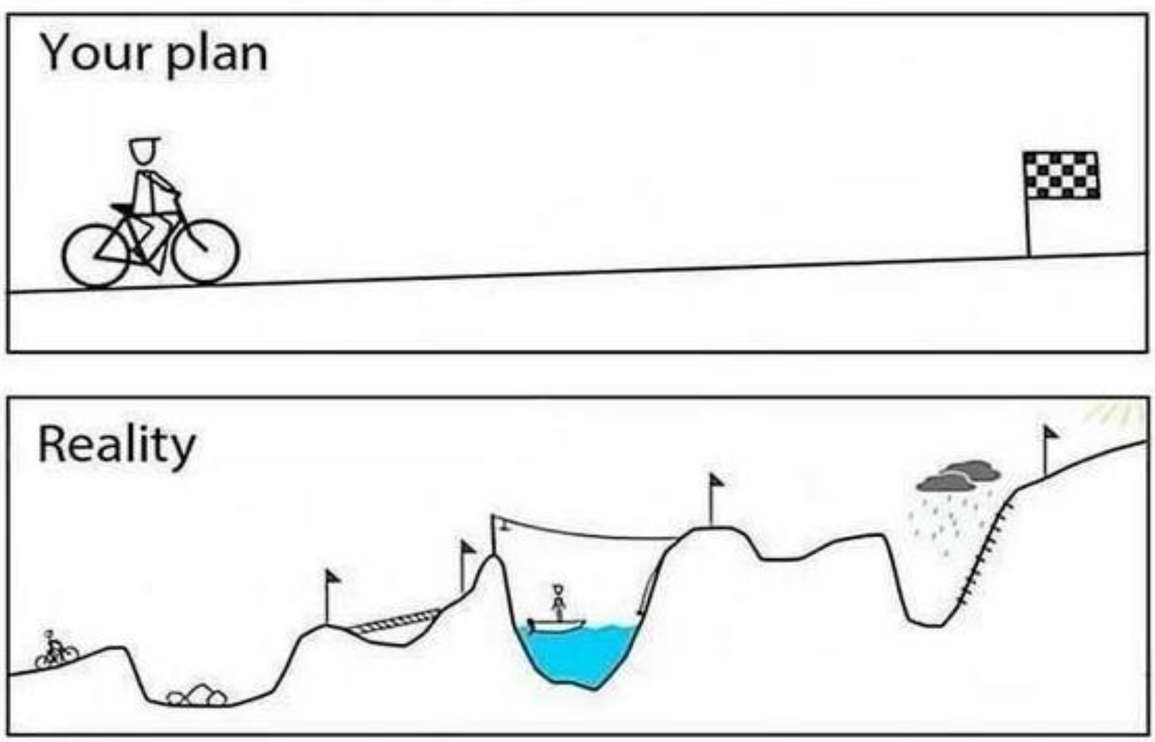
So, what is an expectation?

“a strong belief that something will happen or be the case.” - Google dictionary

And what is reality?

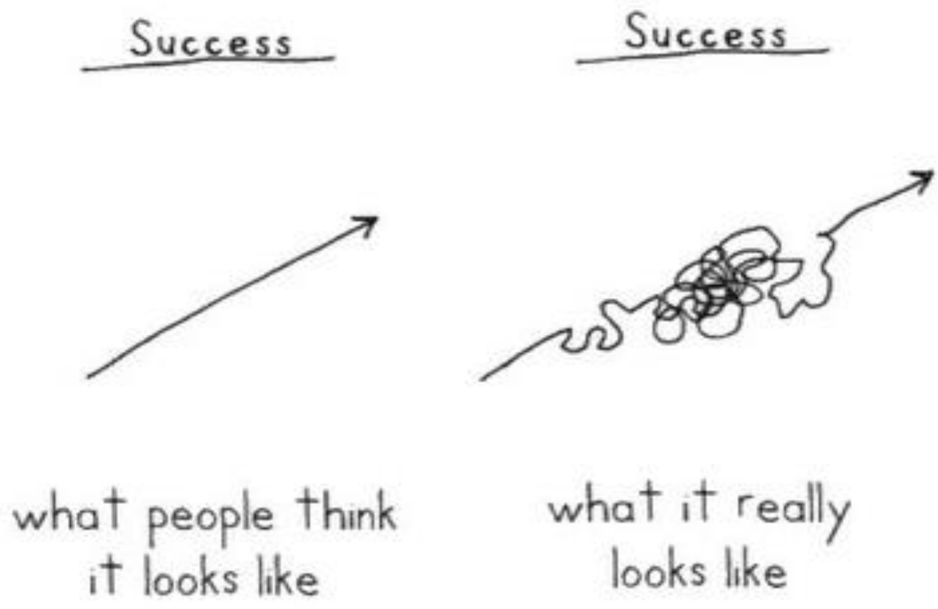
“the state of things as they actually exist.” - Google dictionary

An expectation is formed from our belief regarding future events and future is uncertain. Future events might occur or might not occur as well. And may occur but not as same as we have made an expectation. That means the real journey from our expectations to the reality can differ.



When we make a plan for achieving our goal then we might get biased many times; and start thinking that we can easily achieve our goal as we have to make a plan; without getting any disturbances. But is it really happening?

As above image indicates, we face many ups and downs on the way towards reaching our goal. Many unexpected events can take place when we put efforts to fulfil our expectations.



Success never comes in a straight way but many times, we expect to get a success in an easier way. Reality might differ many of the time and we don't get success very easily. Many confusions, obstacles, nervousness, anxiety effects when expectations transform to action for achieving goals.

Let me take a simple example,

When we have to make a plan to build body, start to work out and to start a diet. We have built an expectation that we can easily control on our diet and stay away from the food which contributes extra fats. Also, we have to make a plan that we do regular workouts and within a short span of time, we can able to build our body like Amir Khan. ;-)

But is it really happening? Are we able to control on our diet easily?

When we actually start executing our diet plan and at the same time, the friend brings pizza in front of us. First, we refuse to eat, he requests to eat. Again, we refuse, he again requests for eating and only 1 piece. We again refuse, he again offers with dialogue - "Ek piece se koi fark nahi padega" (One piece will not make a huge difference). We also start thinking in the same way. Let me eat one piece and will do an additional workout for burning fat.

And that is the time, expectations and reality start showing differences.

This is only one incidence but such many of the incidents happen with us in our regular life where we can find a difference.

Obviously, we can able to achieve what we have expected but many times not in a way what we have actually expected.

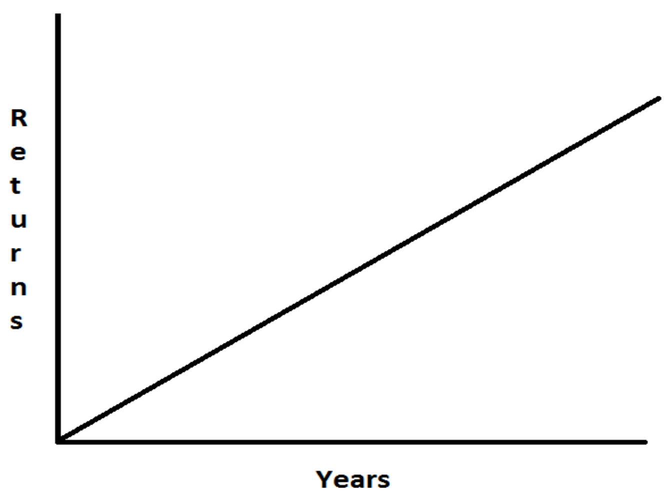
The same things happen in an investment world.

When we make an equity investment, we have already built certain expectation for our investments. Equity investment is as similar as our regular life. Here, also expectations and reality can differ. In equity investment person comes with an expectation of getting a good return (*actually an abnormal return ;-)*) and also, additionally have built an expectation of linear return year on year (*actually within a year ;-)*).

But,

Is it really, we get a good return in a linear manner while we are making equity investments?

No, never *(According to my experience)*.



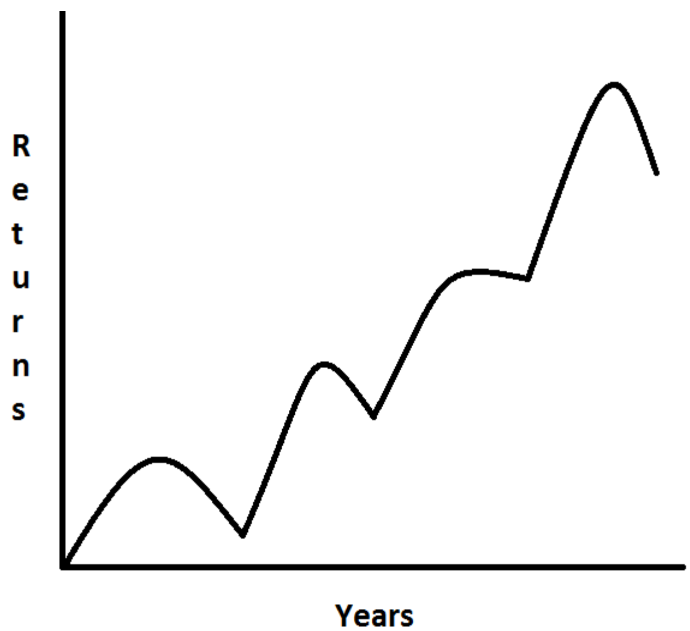
Year	Return
0	100
1	115
2	132
3	152
4	175
5	201

We have an expectation of getting a good return (*abnormal return ;-)*) in a linear manner year-on-year (*within a year ;-)*). And our investments should grow regularly.

That means, if we have built an expectation of getting a return of 15% CAGR (*not at all we expect such low returns ;-)*) then we expect that our equity investment will deliver it regularly.

But such linear returns, we get only from fixed income instruments (such as Bank FD, corporate FD, debentures, Liquid fund, etc.).

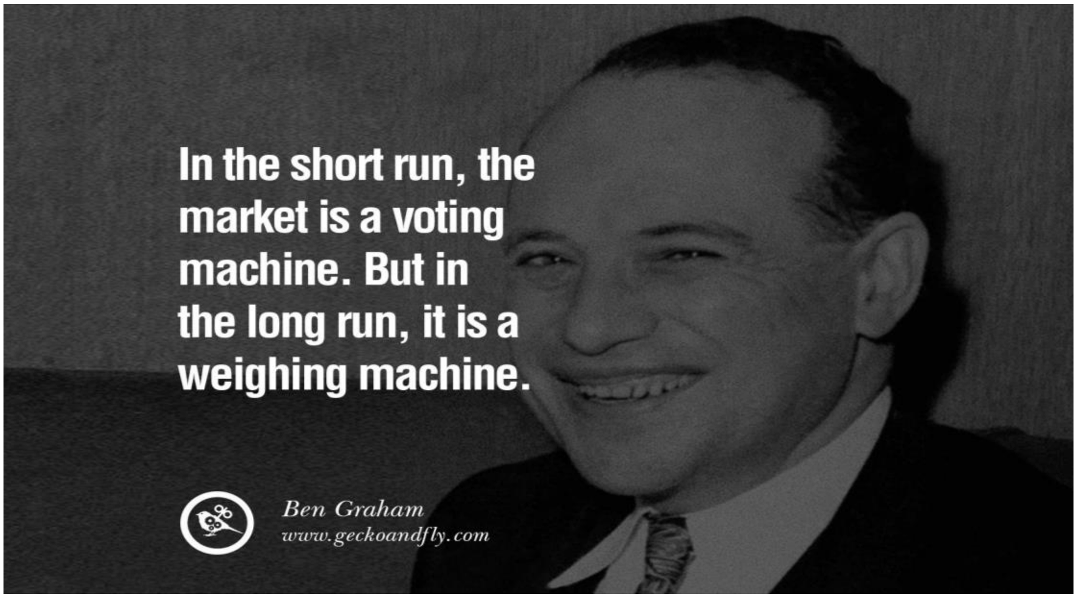
What really happens when it comes to an equity investment?



Year	Return	Return (%)
0	100	
1	90	-10%
2	122	35%
3	154	27%
4	139	-10%
5	201	45%

When it comes to reality in equity investments then we get 15% CAGR returns but not in a linear manner which we have expected. Equity by nature itself always fluctuating. So, we have to know it in advance while we are making equity investments.

We ultimately get a 15% CAGR return over 5 years of the horizon but not in a linear manner. We can see it in an above image that our returns every year keep on fluctuating but at last, we reach to our expected return targets. But actually, when our returns start fluctuating, we are start leaving stock markets and starts deploying our money into fixed income instruments where we probably cannot able to even beat an inflation well. We again come into equity when equity starts show its glory. But in real we have to be a part of every fluctuation of equity market for getting a reasonable return which helps us to beat inflation and also help us to build our wealth.



We should ignore short-term fluctuations of the equity investments and need to focus on our longer-term goal. And also, need to keep our expectations reasonable (*should not be expecting more than double of our capital within a year*).

If we keep our expectation low/ reasonable then we can able to achieve more in reality and that help us to stay happy. We should keep in mind that we can able to achieve what we have expected but many a times results will not be in a way what we have actually expected.

Love to read again and again

- 25 Questions with Indian Investor Neeraj Marathe
- FAIR & FINE ???

My Popular articles

- WHAT IS ROE (RETURN ON EQUITY)? AND WHY ALWAYS CONSIDER DEBT WHEN CALCULATING ROE?
- WHY CONSIDERING ROCE (RETURN ON CAPITAL EMPLOYED) WITH ROE (RETURN ON EQUITY) IS BETTER????

Simple is Better Series

Issue - 1	Issue - 2

Disclaimer

Above article is just my perception, and perception can be wrong. For me, my perception can be right but for others, it might be wrong.

I am Grateful to

I am really grateful to - Mr. Neeraj Marathe Sir, Prof. Sanjay Bakshi Sir, Mr. Vishal Khandelwal Sir, Dr. Vijay Malik Sir, Mr. Rajeev Thakkar Sir, Mr. Raunak Onkar Sir, Mr. Vijay Kedia Sir, Mr. Howard Marks, Mr. Warren Buffett, Mr. Charlie Munger, Mr. Benjamin Graham, Mr.Porinju Veliyath

I am especially grateful to Mr. Vishal Khandelwal Sir for getting inspiration to start series of articles.

I am grateful to Mr. Tejasbhai Jariwala for providing an idea to me for the issue - 3.

I am really grateful to my parents and almighty for providing me always support whenever I needed.

Please forgive me, if I forget to mention any person who has contributing value to my journey.

Author: Jimit Zaveri (Founder of Lucky Idiot)

Blog address: https://jimitzaveri.wordpress.com/

As a founder of Lucky Idiot; My mission through "Lucky Idiot" is to educate novice investors and to distribute learning to more and more people in a simple manner.

Follow me: @ Twitter Jimit Zaveri