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Challenging Conventional Wisdom

NEWSLETTER

Woodstock for Capitalists by Theo Vorster

"Woodstock for Capitalists" is what Warren Buffett calls the annual chat that he and Charlie Munger have with the Berkshire Hathaway shareholders. And it's astounding to think that 35 000 people went to Omaha in the US recently to listen to 82-year-old Buffett and 89-year-old Munger – more so when you consider that these two guys have been partners for 54 years in the fifth biggest company in the world – Berkshire Hathaway, a pure investment company. The pair answered questions for six hours, ranging from the state of the world economy, to investment strategies, to advice for business success.

It's impossible to sum up a six-hour session in a few pages. Instead I'll try to highlight a few of their main points in order to demonstrate the logic of these two investment icons. To present this summary in a sensible way, I've divided the discussion into themes and looked at selected points under each. Note that this is in no way a complete summary, and I have put it together by combining several sources.

State of the US economy

The US economy has been in a worse position than it is today, for example, following WWII, after which it recovered well and grew for decades. "We've encountered far worse problems than we face now." say the pair. "This is not our toughest hour."

If the US economy manages to increase its rate of growth, most of the current problems will solve themselves. Buffett says the problem will then fade into "insignificance".

Greece and the EU

Buffett is very critical of the decision to include Greece in the European Union. "It's like putting rat poison into whipped cream," he says. "Greece is not a responsible country."

But he says that while it will take a bit longer, Europe will eventually solve its economic problems. happens when you least expect it.

Decisions on the basis of macro-economic considerations

In the 50-plus years they've worked together, Buffett and Munger say they have never yet taken a decision on the basis of what is going on in the economy, or what the economic forecasts are. If you say you know what's going to happen, then you haven't done your homework, you're simply uninformed and haven't done enough research. "If you're not confused, you don't understand things very well."

Investment decisions

If you're not in control of your emotions, you shouldn't be managing your own investments. Investment decisions must be made on rational grounds, and not from a behavioural or emotional departure point.

"We've always tried to stay sane when other people – a lot of them – go crazy. That's a competitive advantage. When people get scared it is very hard to deal with them. People get fearful en masse. When we see falling prices we see opportunity."

They also emphasise that: "You can't afford to go with the crowd on investing."

When it comes to forecasts, their opinion is clear: "You can't make a lot of money trying to think what is going to happen tomorrow."

If you're not a professional investor

Ensure that you are in a diversified portfolio. The best thing to do is to use low cost index funds. The investment industry is good at shifting capital from the investor to the fund manager and the best way to overcome that is in an index fund.

The basis for this is that the costs are lower, and very few fund managers manage to beat the index.

Interest-bearing investments versus shares

He refers specifically to the US here, but many of the principles can be applied to South Africa. He feels sorry for people who invest in interest-bearing investments. "For 90% of my life, it has been better owning equities," he says, meaning that exposure to growth assets is critical for long-term growth.

Advice for successful business management

Here he focuses on three points: manage costs and keep them low, build your brand, and make sure your clients are happy.

When asked a critical question about their investment in the motorcycle group, Harley-Davidson, he comes back to focus on branding, saying: "Any company that gets customers to tattoo ads on their chests can't be all that bad."

The long-term nature of investing

Munger supports Buffett when they explain that long-term investment isn't three or five years – it's longer than that. It's noteworthy that a person aged 89 isn't worried about what's going to happen in the next three to five years.

On children, wills and inheritances

They recommend that you share your will with your children when they are in their 30s. Buffett emphasises that the behaviour of parents determines their children's future, and it's about them knowing about their inheritance, not the amount of the inheritance. The way parents work with money determines how their children will work with money.

Making an investment

Whether you only buy 100 shares in a business, or the whole business, you must regard any investment as if you are buying the whole company. He adds that you must be prepared to pay a premium price for a quality business. "Paying up for an extraordinary company is not a mistake," he says.

They also believe in allowing businesses to manage themselves. "We're decentralised almost to the point of abdication."

Life advice

To young people they say: “Start developing your track record as early as you can, one that is a product of sound thinking.”

On career choice: “You have got to work where you’re tuned in. I have never been successful at something I did not like.”

Munger says that: “The game of life is the game of everlasting learning.”

When it comes to expertise, they advise: “Knowing the edge of your competency is very important. If you think you know more than you do, that’s looking for trouble.”

Practicalities – what does this mean for investors?

1. Ensure you are not emotional when it comes to investment decisions. Therefore it’s better to consult a good financial advisor who isn’t emotionally attached to your specific circumstances, and who will give you rational advice.

2. Use cheap index fund solutions if you are not a professional investment manager.

3. Don’t pay too much attention to macro-economic factors and don’t rely on your ability to predict the future. The first step towards financial fitness is an executable, realistic strategy/plan that you can stick to. A plan like that helps you to focus through uncertain times and reminds you why you made certain decisions in the first place, should you begin to doubt yourself. That’s why it’s preferable to enlist the help of an expert so you can focus on what you understand and make a success of it.