Buffett Partnership Letters

Property	Value
Category	Investing
Mental Model	
Optimized?	☑
People/Website	Warren Buffett
Status	Read
Type	Letters

Before you start reading I want you to know that Warren Buffett no longer follows this style of investing. He has evolved as an investor from Cigar Butt approach to Moat investing.

Just look at the below image. Warren has moved from left to right as he evolved.

Source

The Letters

▼ 1957

- Warren Buffett(WB) emphasizes on the importance of luck for short term gains for his partnership in 1957.
- During the acquisition period WB desires the stock to do nothing or, even better, decline in price

▼ 1958

- What WB looks for
    - Very strong defensive characteristics
        - does not expand on that
    - Good solid value building up at a satisfactory pace and,
    - Evidence of value unlocking
        - I think I was missing out this third part while I used to follow this cigar butt approach

▼ 1960

- Gives example of a company 'Sanborn' which had a business of making maps and was doing poorly but they had huge amounts of cash in the marketable securities made it an attractive bargain.

▼ 1961

- His method of operation
  - Three categories:
    - "Generals"
      - Undervalued stocks, not sure when, but will soon unlock the value
      - Here corporate events does not matter
    - "Workouts"
      - Unlocking of value due to some corporate event
    - "Controls"
      - finding undervalued company, taking over control and unlocking the value
      - He would try to buy most of the shares available in the market hence the price does not change much

- Also, talks about taking leverage but only for 'workouts' categories as they are safer bets
  - I believe that he might be definitely having some information edge here
  - He had a rule of not increasing leverage above 25% of the partnership net worth
- Talks about that there is always a high probability of a market crash once in a decade

▼ 1962

- Growth stocks went down significantly compares to Dow.
  - This is the problem with them, they run at a very high rate and when there is sudden drop[in the rate] the stock also corrects significantly.

▼ 1963

- Warren considers 5 years of period as a test to compare performance and even if you still want to compare then 3 years is the absolute minimum.
    - I haven't been investing for 3 years 😂 (Just completed my second year)
- Two things that matter to WB
    - Value over popularity
    - no risk of permanent loss of capital by the use of margin of safety

      Margin Of Safety While Driving

> Just because something is cheap, it doesn't mean it is not going down

> By buying bargains we don't need to pull rabbits out of a hat to get extremely good percentage gains.

> Never count on making a good sale, have a purchase price so attractive that even a mediocre sale gives good results. The better sales will be frosting on the cake.

▼ 1964

- Things WB looks for:
    - While Quantitative comes first, the qualitative part is also important
    - Decent Industry
    - Certain amount of 'ferment' in the people running it.
        - Excitement or energy I believe
    - Value

▼ 1965

- How to beat fund managers?

        - Don't over diversify
        - Handling your own investment decisions
        - Avoiding use of inferior investing techniques
            - He does not expand on this

> If a 20-30% drop in market value of equity holdings is going to produce emotional or financial distress, you should simply avoid stocks.

> If you can't stand the heat, stay out of kitchen. It is preferable, of course, to consider the problem before you enter the 'kitchen' - Harry Truman

- Four categories in his portfolio
    - General: Quantitative + Little Qualitative
    - Relative Undervaluation: Substantial Bargain
    - Workouts: They have a timetable, i.e. when they are going to perform
        - Need to understudy the difference between timing the market and these 'workouts'.
    - Controls: taking control of the company and making it perform as per your needs
- Buffett on Taxes:
    - He says that although taxes may be a factor to be considered in achieveing the end.
    - Means and end should not be confused.
    - End is to come away with largest after-tax rate of compound.
    - There are only three ways to avoid paying taxes
        - Die with the asset
        - Give the asset away
        - Lose back the gain if your mouth waters for tax savers

- One's policy should be to maximize gains and not minimize taxes

▼ 1966

- Huge Capital Disadvantages
  - Size: Huge money can't buy small caps
  - Price: price could suddenly increase when you pour in huge capital
  - Cost: Huge transactional cost, therefore you can't take a quick exit
- Why Fund Mangers don't outperform
  - Group Decisions: so many people involved in taking the decision
  - Desire to conform to the policies of other large organizations
  - An framework where average is 'safe' and no personal rewards for outperformance with the risk attached to it
  - Too much diversification
  - Inertia
- It is very difficult to find many attractive investment ideas to invest in.
- If you diversify there is less volatility so people find it comforting but at the cost of exponential returns in the long run.
- WB has felt that he should have done more of concentration on some bets.

▼ 1967

- WB again talks about three factors which lead to poor performance of fund managers
  - Too many restrictions in their investment decisions
  - "Diworsification"
  - Less incentive for abnormal performance
- From this year Buffett seems to be shifting to Moat investing as this year he claims that there are less opportunity available in the market which he could understand and take a decent position in it.
  - He gives three reason for this:
    - Change in the market environment

                - At one extreme we have people who concentrate only on qualitative aspects like Philip Fisher or Saurabh Mukherjea.

                    > Buy the right company and the price will take care itself

                    - No insight is required on quantitative side, "the figures should hit you over the head with a baseball bat".
                    - The big money is in getting right at the qualitative aspects but sure money is in getting right the quantitative aspects.
                - On the other extreme we have people of only quantitative aspects like Benjamin Graham.

                    > Buy at the right price and the company will take care of itself

                - Now even after a person combines both the aspects his performance will be determined on which aspect he assigns more weight to.
            - Increased size of the capital
            - More competition
    - Even though Buffett now seems to get only 2-3 ideas to invest in a year he is still determined in staying within his circle of competence.

▼ 1968

- After twelves years of performance the actively managed fund could out perform the index with over 1%.

> Price is what you pay. Value is what you get.

> We don’t believe in miracles – we rely upon them.

> It is possible for an old, overweight ball player, whose legs and batting eye are gone, to tag a fast ball on the

> nose for a pinch-hit home run, but you don't change your line-up because of it.

▼ 1969

- WB takes decision to close the partnership and discusses the same three reasons which he gave in year 1967.
- Buffett highlights a very important advantage of working alone.
    - When one starts to manage other people's money you tend to start getting involved in activities which do not contribute to a superior investment performance.
        - Ex: Taxes, company structure, etc.
- Reason for not liquidating Berkshire Hathaway: 1100 hard working people it employees.
- Buffett on succession: One could only know whether the people second in command are capable of running the company only after they have taken over and not before that.