Buffett: The Making of an American Capitalist Study Guide

Buffett: The Making of an American Capitalist by Roger Lowenstein

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Plot Summary

America is full of multi-millionaires and some billionaires. In every generation throughout history, in fact, there have been the super-rich in this country. Most of these individuals made their money through products and/or services which became valuable (e.g., automobiles, fast-food, computers). Unlike these individuals, Warren Buffett has made his money on the value of products and services offered by others, by investing in their companies. He did not do this alone but, rather, convinced other people to invest with him, first as partners, and then as shareholders in the now famous Berkshire-Hathaway Investment Corporation.

Obsessed with numbers and accumulating savings from childhood, Warren Buffett began investing at a young age. His investment strategies as an adult, however, were primarily based upon the philosophy of a university professor at Columbia Business School, Benjamin Graham. The key principle was to find companies whose stock was under-valued, purchase the stock, and hold the stock until its value was commensurate with the company's worth. Buffett added themes of his own, to include holding stocks for a lifetime and retaining management that was ethical, frugal, and effective. By 1995, Buffett was personally worth ten billion dollars, and any investor who began with him in 1956, putting in ten thousand dollars, was worth eighty million.

Buffett's personal life has been unlike that of any other billionaire. Still living in his hometown of Omaha, he resides in the modest home he and his wife first bought, drives his own car, and eats at his favorite local steak house. His extravagances include a personal jet and a vacation home in Laguna Beach, California, as well as a once-a-year extravaganza for his annual shareholders' meeting. His wife, Susie, lives in California, and his mistress, Astrid Menks shares his home. All three are close friends.

One of the greatest legacies Buffett has left for the lay person is the unraveling of the mystery of Wall Street, his common sense approach to investing, his opposition to the majority of fund managers and large traders who buy and sell stock daily, and his personal and professional values of commitment and loyalty. One cannot read this biography without developing a strong sense that this man, though eccentric and unusual, has the unique genius to "smell" a bargain, to attract the right people to manage companies in which he has huge interest, and to have the patience and integrity to ride through the rough investment times without panic. Indeed, anyone in the stock market or considering investing in the stock market would be wise to read Warren's Buffett's story, before jumping into funds whose managers take the traditional Wall Street approach.

Omaha

Omaha Summary and Analysis

From the time he was a little child, Warren Buffett was fascinated with numbers. He memorized that the populations of cities, baseball scores from multiple seasons, and horse-racing odds. His desire for money caused him to play monopoly incessantly and to wear a coin changer as he sold chicklets and lemonade. He collected bottle caps from the soda machine at the local gas station, comparing how many of each kind was sold and which was the best business. His father was a stockbroker, and he loved to get rolls of ticker tape and decipher the symbols from Standard and Poor's.

The Buffett family originally settled in Long Island as farmers. Sidney, one of the brothers, struck out for Omaha and opened up Buffett Grocery Store, just as the railroad was reaching the town. Sydney's business grew and he decided to include his two sons. Ernest opened up another store on the other side of town. Howard, however, had no desire to become a part of the family business. He was the editor of his college newspaper and dreamed of a career in journalism. He ended up in the insurance business with a friend of his father's and then as a securities broker, not a particularly hot job during the Depression. He eventually married Leila Stahl and had two children, a daughter and son named Warren. When Howard's bank closed, he lost both his job and savings, but continued with investment sales by opening up his own firm, surviving several lean years. As the Depression waned, business picked up, Howard began to make more money, and the family moved into a larger home.

Warren was a mild-mannered child who was often teased by his "rough and tumble" classmates. His early poverty affected him greatly, and he vowed from the age of 5 to be rich above all else. From the age of 6 on, his obsession was to make money in any way possible, including buying soda at the grocery store and selling it at a profit door-to-door. At the age of 10, he accompanied his father to New York and, among other things, visited the New York Stock Exchange. He was hooked. Back in Omaha, he visited his father's office often and began to chart the prices of stocks to determine patterns. With his savings from soda, chicklet, and lemonade sales, he bought three shares of Cities Service at $38 and sold them at $40. The stock eventually climbed to $200, Warren's first lesson in patience.

Warren spend little time at home. Leila had a rather apparent mental illness, perhaps genetic. One sister committed suicide; another sister and her mother were both institutionalized. She would fly into furious rages, and home was not a pleasant place. He spent a lot of time at friends' homes, often arriving in time for breakfast and staying through the dinner hour. With these friends, he developed numerous schemes to make money, to include collecting golf balls from the local golf course and selling them, and scrounging for winning tickets that had been thrown away at the race track.

In 1942, the local Republican Party successfully ran his father for the Congressional seat from the district; he won and the family was off to Washington D.C. Warren hated leaving Omaha and his friends during his 8th grade year, and being a creative child, he faked an allergy so that his parents would send him back to Omaha to live with his paternal grandfather and aunt. He was thrilled to both return to his old school and work in his grandfather's grocery store. Even as an 8th grader, he continued to tell everyone he would be a millionaire. When asked why, he said, "It's not that I want money. It's the fun of making money and watching it grow."

Runaway

Runaway Summary and Analysis

Warren had to return to Washington after his 8th grade year, as his parents had moved into a new home in Washington proper, one they felt would not trigger his "allergies." Other than accumulating money as a Washington Post paper boy, he was miserable. After a failed runaway attempt with two other boys, Warren settled into Washington by expanding his paper route to include the rival morning paper, adding four more routes, handling them all before and after school and netting $175.00 a month, saving every bit of it. In 1945, at age 14, he took $1,200 and bought forty acres of Nebraska farmland, leasing it out to a tenant farmer. He was faring better in school as well, making a few friends and improving his grades. In his spare time, he avidly read any business books he could find.

During his senior year, a friend, Donald Danly, bought a used pinball machine, which he was able to repair. Warren suggested that they put it in a barbershop on a rental basis. The first barber agreed to a fifty-fifty split, and they netted $7.00 the first day. Warren bought more machines and placed them in seven shops. They stuck to barbershops, because it was a retail area into which the "mob" had not moved. Danly kept them repaired, and Warren put up money for purchases and parts. Howard Buffett was a staunch enemy of Roosevelt and then Truman, voting against the United Nations, against helping to re-build Europe and Japan, and was, essentially,. an isolationist. Warren held some of his father's beliefs but did not desire any part of a political life. Instead, he was studying the stock pages of the newspaper and trading on the exchange on his own. He was earning money from newspapers and pinball machines and from a tenant farmer on his land.

Upon graduation in 1947, Howard talked his son into attending Wharton School of Finance, where Warren insisted he knew more than his professors and that they lived in a world of theory not in the practical world of making money. He made several good friends, however, to include Charles Peterman, Henry Beja and Jerry Orans, all of whom would become future investors with Buffett. When Howard was not re-elected to Congress, he moved his family back to Omaha and Warren left Wharton in favor of moving home and attending University of Nebraska at Lincoln. He was a student in name only, even though he carried a full load, and focused instead on launching his career. He took a newspaper delivery supervisory position for the Lincoln Journal and went back to the golf ball business as well. By the summer of 1948, he had accumulated $9,800 in savings. He graduated at 19 and attended Columbia Business School, having been turned down by Harvard. His friend, Jerry Orans, was attending Columbia Law School.

Graham

Graham Summary and Analysis

Buffett met his "guru" of investing, Benjamin Graham, at Columbia. a man who laid out to his students a methodological basis for picking stocks. Graham was born Benjamin Grossbaum in London and immigrated to New York as a child. His parents lost all of their savings in the panic of 1907, but he eventually attended college and moved onto Wall Street, starting as a floor man who put stock prices on the chalkboard. He was bright and quick, began to invest and analyze and, by the 1920's, he was considered a bit of a expert. His basic formula for investing was to look for a company whose stock was such a bargain as to render it essentially risk-free. Graham lost a great deal during the crash of 1929, but his partner coughed up $75,000 to allow the partnership to survive. Graham's addition to his basic formula was not to buy common stocks, as they were not really investments at all. The popular thought of the time was that value was totally tied to public sentiment, not to earnings of a company, and common stock rode with public sentiment only, not to earnings. Graham's advice was not to try to figure out public sentiment but, instead, to pay attention to the business beneath the stock. Focussing on earnings, assets, and future prospects would give any investor the value of a company and should determine investment decisions. The trick was to invest when the stock was low and then wait until the market corrected and the stock went up. If the company is solid, according to Graham, this would happen eventually. Stock was a share in a business and its value would be directly related to how well that business did over time. All of this investment philosophy and advice was included in Graham's books, Security Analysis and The Intelligent Investor. The Golden Rule of investing is to buy stock when one truly believes it is undervalued. Hold it, even if the stock continues to drop. Do not panic as long as nothing changes with the company. Eventually, it will correct and the stock will reflect the correction.

Buffett grasped Graham's philosophy as gospel—it made total sense to him. In class, Graham had students of all ages. Many were already working on Wall Street and took his tips, making money. Graham himself made money too, but did not seem to care a great deal about that. He enjoyed more being a father figure to his students. His personal life was not stable, with a string of wives and mistresses and poor relationships with his children. However, with his students, he was warm and congenial. Buffett joined a small group of stalwart Graham disciples, a group that remained friends and confidants throughout their lives.

Buffett graduated in 1951 and was advised not to go into the stock market but to wait for the next crash which was sure to come. Buffett, of course, was determined to get on with his career. He went home to Omaha, to his father's brokerage house. He was not particularly interested in selling stocks and bonds to potential buyers, but rather, in researching companies and selecting those that exemplified Graham's "good" buys. He first sold GEICO, a company partially owned by Graham and one in which he himself invested $8,000. It doubled in two years. He then found some small gems and bought

them as well. In 1952, he married Susan Thompson, whose father preferred Buffett to the blue-collar boyfriend she had at the time, and took a course in public speaking so that he could teach investing at the University of Omaha. He was so enthusiastic about the subject, he virtually mesmerized his students. When Graham offered Buffett a job in New York, he was off, researching potential purchases for the Graham Newman Fund. The goal was to find companies whose stocks were trading at least one-third less than net capital of the company. Buffett invested in the fund himself and made good profits. However, he was a bit frustrated. He wanted to visit companies himself, talk to their management, and get a "feel" for the people in charge, believing that management was a critical aspect of a company's future. Graham did not agree. Graham finally retired in 1956, and Buffett took his accumulated profits of $140,000 and went back to Omaha. He wanted to develop a partnership a la Graham and convinced family and friends to "pony up" investment funds totaling $105,000. A form Graham investor kicked in an additional $120,000 and Buffett was on his way.

Beginnings

Beginnings Summary and Analysis

By 1957, Buffett had investment partnerships with several relatives and friends, managing about $300,000 and knew virtually every stock and bond in existence, studying them voraciously. He realized that, in order to grow, new investors were needed, and he got a break when a doctor's family decided to join. Buffett's rules were quite strict. New partners were to give him their money and not ask any questions. They could add to or cashout at the end of each year. Buffett would give them all profits up to 4% and then 75% of any profits above that. By the end of 1957, Buffett's portfolios gained 10% while the Dow Jones dropped 8%. By the end of 1958, the portfolios rose 41%, the Dow 39%; by the end of the third year, the partnership money had doubled. The minimum investment was raised to $50,000. Another strict rule that often turned away potential investors was that the investments remained Buffett's secret; he would not reveal them to any partner. This slowed the growth of new partnerships, but Buffett remained steadfast, following the rules of Graham by picking up small cheap stock after analyzing the long-term value of the company. After the first five years, he had netted a gain of 251%, while the Dow had netted only 74.3%. Buffett became rather famous in Omaha.

Buffett's personal life was organized and quiet. He depended upon Susie to run the household and organize their lives. She also shielded him from his mother, taking her calls and running interference for him. They complemented one another—he was self-absorbed, and she dealt with the world. At parties, Susie socialized; Buffett found a chair and sat, holding "school" as others gathered around him to learn investment strategies. Though he refused to give stock tips, Buffett was happy to expound on the "biblical" investment philosophy of Ben Graham. Warren and Susie had friends in New York and visited often, Warren constantly looking for new investors. By 1962, he had 90 investors, merged all of his partnerships into Buffett Partnerships, Ltd., and moved into an office in Omaha. The minimum investment was raised to $100,000.00.

At about the same time, Buffett renewed a friendship with Charlie Munger in Los Angeles. Munger had grown up in Omaha, worked at the Buffett Grocery and finished three years of college. Without a degree, he still managed to get into Harvard Law School, based upon the admissions test, and set up shop in California. While he and Buffett shared the same views about investments, they were personally quite different. Buffett was quiet and reserved, Munger outgoing and gregarious. Buffett persuaded Munger to give up the law and to set up investment partnerships in California, and thus began a friendship and mutual investing that lasted for years. Buffett had made one bad move—the purchase of Dempster Mill—and Munger recommended a friend as manager for the company. Buffett hired the guy, who trimmed the company out and used profits to purchase other securities. Dempster finally sold for $2.3 million, and Buffett had tripled his initial investment.

Partners

Partners Summary and Analysis

Buffett began to stray from the strict teachings of Graham and looked at businesses beyond just those having under-valued stock. He decided that the quality of a company's business and its management bore analysis as well. Accordingly, he bought stock in a suit lining manufacturer that was doing poorly but which had assets and took a big risk on another company that was actually in trouble—American Express. American Express had been on the financial scene for some time already, and was transforming purchasing and traveling activities with its credit cards, traveler's checks and money orders. However, in 1963, the company had major problems. A small subsidiary, actually a warehouse, had been defrauded by Anthony DeAngelis, who sold it salad oil that was really mostly seawater. DeAngelis used the receipts for the salad oil to obtain loans and then declared bankruptcy. The warehouse was left with worthless product and was out millions of dollars. Howard Clark, CEO of American Express, felt obligated to "make good" on the fraud and declared that American Express would pay the claim against the warehouse subsidiary, which had also declared bankruptcy. Stockholders were angry and saw the issue as the potential end to the company. Buffett, however, went to see Howard Clark and investigated the health of its major money-maker—credit cards and traveler's checks. Realizing that the company was thoroughly sound, he waited until the stock had dropped from 60 to 35, and then began to buy.

Buffett's portfolios were truly different from the norm. Most fund managers counted on wide diversification, that is, accumulating hundreds of stocks from a variety of sectors. The philosophy was that, if one sector did poorly, the loss would be balanced by other sectors which did well. Buffett did not care about sectors. He bought based upon the company only, and his entire portfolio consisted of American Express, Berkshire Hathaway (a suit lining company that was not too healthy), and two or three others. He was out to beat the Dow averages while other fund managers only wanted to replicate them. By 1964, Buffett was managing $22 million from investors and had about $4 million for himself.

He continued to live simply, not interested in what his money might buy, but, rather, the accumulation of money itself. As a family man, Buffett was not the all-American dad and husband. He rarely showed emotion and was not demonstrative with his children, as his father had not been with him. He was more interested in being a moral role model to his children above all else, and this he certainly was. While he saw his own father as his best friend, he did not share much of his politics. As a conservative Republican, Howard was a member of the John Birch Society and believed in complete separation of the races. During the sixties, Warren read and adopted many of the beliefs of Bertrand Russell, believing that any society must protect its environment and do whatever necessary to avoid war. He became a Democrat but never told his father, who was suffering and eventually died from cancer.

In the summer of 1965, the Buffetts visited Disneyland with the Mungers. While the women and children enjoyed the park, Warren and Charlie dissected the place financially. Warren met with Walt Disney. The stock was priced above earnings, but Buffett saw the asset of the film library as well worth the price. He bought 5% of Disney for $4 million. Again, he had broadened his analysis of a company from the earlier Graham model. The value of Disney was not so much in its earnings but in the film library which could re-release and re-make all of the original Disney films. He probably was encouraged by the recent success of American Express, as its stock had just reached 73.5. In 1965, Buffett beat the Dow by 36%. In fact, over a ten-year period, from 1962-1972, Buffett's portfolio gave a 1,156% return while the Dow gave 122.9%. Buffett was thrilled, of course, as were his investors; however, he warned them that this would not go on forever.

Go-Go

Go-Go Summary and Analysis

In the 60s, the stock market was exploding with lots of new companies and growth—the "go-go" years for money men. Buffett was a bit trapped, because he had lots of money but could not find enough bargains to buy. He eventually closed the partnership to new accounts and continued to scour for bargains. Usually, he bought bargains slowly so as not to alert the competition, but, more and more, he was outsmarted by others who snatched them up.

The additional phenomena of the 60s were mergers and "letter stock," that is, stock in companies that were essentially "fads" and whose stocks were overvalued. Performance funds were managed by high rollers who bought and sold stock to beat the Dow on a daily basis. Buffett could not get on board with these new methods of profit-making and taking. He retained his conservative, old-fashioned approach. Instead of buying what he felt were over-priced stocks, he bought two retail businesses, thinking that he could make them profitable. One retailer, Associated Cotton Shops, was an inner city dress shop chain, and Buffett asked the former owner to stay on. The business survived and remained profitable.

Hochschild, Kohn and Co., the other retailer, was in downtown Boston and was deteriorating. It was clearly a mistake. At the same time, Berkshire-Hathaway, the suit liner company he still owned, was also doing badly. He wrote to his investors that he still believed in his approach because, while the newer approaches could bring substantial profits, they could also result in huge overnight losses. He further declared that his new goal was to earn 9% a year or beat the Dow by 5%. Thanks to American Express and Disney, 1967 brought a 36% gain. In 1968, as the bull market began to turn bearish, and some of the most popular performance funds began to retreat badly, Buffett posted a 59% gain, beating the Dow by 50 points. the problem with the Dow, as Buffett saw it, was that stocks were ridiculously overpriced in comparison with their companies' assets and the belief that stocks were worth whatever people were will to pay was wrong and dangerous.

In the midst of the spasms of the market, Buffett simply quit. He liquidated the assets and distributed them to his partners, saying he did not understand the market environment anymore and did not want to continue the "game." He had accumulated a personal fortune of twenty-five million by this time and thought he might spend some time on societal issues. Buffett's two big causes were first to open up the Omaha Club to Jews, a feat he accomplished by first getting a membership in the all-Jewish Highland Club, and, second, along with Charlie Munger, to fund the case of a California doctor on trial for referring a woman to an abortionist. Both causes were successful.

In June of 1969, the Dow began to dip. Performance funds crashed one by one. By 1970, the Dow had dropped from its previous high of 1,000 to 800. The comparison to

Buffett's partnership was amazing. If a person had invest $10,000 in the Dow in 1957, he would have had $15,260 by 1970; the same $10,000 in Buffett's former partnership netted $150,270. In a final letter to his former investors, Buffett recommended the Sequoia Fund, managed by a Graham student, or municipal bonds of medium-sized cities. He held on to Berkshire and Diversified Retailing, the two textile and clothing businesses he owned. He told his investors that they could either stay in these two businesses or sell their stock back to him. Many stayed in.

Berkshire Hathaway

Berkshire Hathaway Summary and Analysis

New Bedford, Massachusetts was originally a whaling community which ran out of steam as that industry declined. Wealthy whalers then built cotton mills and used their ships to bring cotton up from the South. This business thrived through World War I, largely through providing military uniforms, but was hit hard by the Depression. Most of the mills then moved to the South where labor was cheaper. The single exception was Hathaway Manufacturing. Seabury and Otis Stanton, two brothers, ran the mill and eventually prospered by the production of rayon for parachutes and eventually men's suit linings and curtains. Competition in the early 1950's hurt Hathaway, but, rather than fold, it merged with Berkshire Fine Spinning Association, another New England textile manufacturer based in Rhode Island, in 1954. Berkshire was run by the Chace family and produced fabrics for sheets, handkerchiefs, slips and shirts. Seabury Stanton was out of touch with his employees and ruled the roost like a dictator. Otis, on the other hand, was outgoing and largely responsible for sales. The business was losing money by the 1960's, and the two brothers continued to feud over management style. By this time, Buffett's partnership had become the biggest shareholder, and he continued to purchase shares off the street, finally engineering the takeover that resulted in Seabury's resignation. Buffett placed Ken Chace from Berkshire at the helm and began to plan for the company's turnaround.

Part of the turnaround of the Berkshire-Hathaway merged company involved acquiring other companies, the first being National Indemnity, an Omaha insurance company that took high-risk clients. This acquisition was followed by Sun Newspapers of Omaha and Illinois National Bank and Trust. In all cases, Buffett succeeded in getting the current CEO's to stay on the job. Slowly, he closed cotton plants until only rayon and other synthetics were manufactured. By 1970, profits from textiles were a meager $45,000, while those from insurance and banking were more than two million. Still, Buffett kept one Berkshire mill open, out of loyalty to Ken Chace.

Return of the Native

Return of the Native Summary and Analysis

Buffett had an abiding interest in publishing, having purchased an Omaha newspaper. He subsequently invested in the Washington Monthly, a new publication, begun by Charles Peters, a former Peace Corps volunteer. Peters blew the money and Buffett invested an additional $50,000, hoping to turn it around. He then had a hot news tip upon which the editor refused to act. So, he called the Omaha Sun, which he owned. The tip involved Boys' Town, a revered organization, that had an investment portfolio of 162 million, while sending out pleas for gifts, purporting to be in poverty. The Omaha sun grabbed onto the story and won a Pulitzer Prize.

Little by little, Buffett began to get back into the "game." After the crash of performance funds, the new funds were comprised of big name growth stocks, such as Xerox and Polaroid, called the "nifty-fifty." Again, the price of these stocks was hugely more than earnings, and Buffett would not consider them. Instead, he found some bargains and bought them for Berkshire Insurance. Then, in 1973, the "nifty-fifty" began to fail, the Dow declined, and stocks fell across the board. Buffett, like a kid in a candy store, began to scoop up bargains. He borrowed money to buy more, particularly the Washington Post, which also owned four television stations and Newsweek Magazine. From there, Berkshire went on to buy other media stock, all of it at bargain prices.

Moving on to ad agencies, Buffett and long-time friend, Bill Ruane, were buying their stocks again at bargain prices. Meanwhile, stock in Berkshire-Hathaway was available publicly, but there was little interest. As well, the stock slumped with the general market trend, as did the portfolio of stocks that Berkshire held. Buffett, however, remained optimistic, because he knew the stocks were under-valued and would come back. As stocks continued to decline in 1974, he continued to buy. These Watergate years saw a period that economists called "stagnation," a recession accompanied by inflation. At one point, the Dow dropped to 580, and the big fund managers were stumped. There were certainly bargains, but in the current economic situation, investing might not be wise. Buffett, however, described himself as "an oversexed guy in a whorehouse," and he kept on buying. Clearly, he was back.

Alter Ego

Alter Ego Summary and Analysis

Charlie Munger was the one friend in whom Buffett totally confided. He was typed as Buffett's alter-ego because, while Buffett was optimistic and cheerful, Munger was pessimistic and "dour." Munger was a lawyer by profession but managed an investment partnership in California. Buffett and Munger renewed their acquaintance because they were both buying stock in a company called Blue Chip Stamps, and the acquaintance quickly developed into a lifelong friendship, as they both sought bargains among stocks. Together, they bought See's Candy, Buffett's investment to that point.

Now, Buffett was faced with a bit of a juggling act. He used Blue Chip, Berkshire and Diversified money to invest in other companies. Further, each of these three companies had stockholders, so he had to try to balance purchasing and earnings among the three. As well, his ties amongst all of the holdings were getting complicated. When he and Munger proposed a merger of Diversified and Berkshire, the SEC (Security and Exchange Commission) stepped in and launched an investigation. Specifically, the SEC was concerned about Buffett's and Munger's purchase of Wesco, a savings and loan, and then managing to stave off a buyout, subsequently purchasing additional Wesco stock. The SEC investigation focused on the possibility of price manipulation on the part of Buffett and Munger both. After two years, Buffett and Munger were cleared, and Buffett was named to an SEC panel to study corporate disclosure practices. In response to the public scrutiny, Buffett simplified his holdings, merging Diversified and Berkshire, and Munger became vice-chairman. Berkshire was a company that Buffett had personally built and totally transformed. At this point, it consisted of an insurance unit (Diversified), a bank, a stock portfolio, and majority interest in Blue Chip(a grocery trading stamp company), See's Candy, and Wesco Savings and Loan.

Washington Redux

Washington Redux Summary and Analysis

Katherine Graham had inherited the chief executive position of the Washington Post when her husband killed himself in 1963. She did not see herself as totally competent and thus hired Benjamin Bradlee to run it. In 1971, the Post was propelled into international fame when Katherine overrode the opinions of her advisers and published the Pentagon Papers, despite Nixon's threat to indict her. As an encore, she backed the Watergate investigation of two of her reporters. The Washington Post catapulted to greater fame, but its financial picture was not commensurate. The Post had gone public, and Buffett began to buy what he perceived a bargain. Graham did not know what to think but, after meeting Buffett, asked him to be on her board of directors.

The relationship between Graham and Buffett was complex. Buffett schooled her in finance, so that she began to make clear decisive moves, including buying back Post stock, which was still cheap, and declining offers to buy other ailing media enterprises. They visited one another often, Buffett staying in her townhouse or Graham meeting him in his Laguna Beach California home. Buffett obviously enjoyed socializing with Washington elite, and Graham began to see him as her "escort."

Meanwhile, Susie Buffett was feeling the pangs of an empty nest. Buffett traveled a great deal and only one child remained at home. She decided to become a singer, put together a small band, and booked herself into a couple of nightclubs in Omaha, drawing large crowds. She was actually quite good. Their lives were clearly taking separate paths with more separations, but they continued to be much in love. The relationship between Buffett and Graham continued, and she followed his advice to the letter. Buffett was conservative and if he could not "see" a business, or did not understand a business, he was opposed to investing in it. Such was the case with cable television networks and cellular technology. As a result, the Post lost some good opportunities for investment. However, on the other hand, Post stock growth continued and, by the time Buffett left the board in 1985, his original investment of $10 million, through Berkshire, was worth $205 million.

During the time that Buffett joined the board of the Post, he rekindled an old interest in GEICO Insurance. He had long ago sold some previously purchased shares, but GEICO was in trouble. It had relaxed its guidelines and had begun to insure higher-risk drivers. Claims increased to a level that resulted in the posting of a $126 million loss in 1976. GEICO stock was now cheap, and Buffett's early guru, Ben Graham, still had lots of his savings in it. Clearly, Buffett saw an investment opportunity, as well as a chance to rescue Graham's money. He met with the CEO, John Byrne, and promised that if Byrne could find bail-out capital, he would take a large stake of stock. It was accomplished, and Buffett's Berkshire bought $23 million in stock. Within six months, GEICO stock quadrupled.

Press Lord

Press Lord Summary and Analysis

Buffett became enamored with the idea of actually owning a newspaper outright. He learned that the Buffalo Evening News was for sale. Buffalo had two papers, the Courier Express being the morning and Sunday paper, the Evening News publishing six evening papers a week. Because Buffalo had a largely blue-collar population which rose and went to work early, the Evening News was the predominant weekly paper, and a long-time agreement between the owners had resulted in the Courier Express being the only Sunday paper. Thus, both papers had specific customers and profits. Buffett and friend Munger purchased the paper with the intent of running it, and their first goal was to add a Sunday edition.

Immediately, the Courier Express took Buffett and Munger to court under anti-trust laws, claiming that it was Buffett's goal to run the competition out of business. The judge allowed the Sunday edition but severely restricted its marketing and promotion to subscribers and advertisers. The paper lost money on its Sunday edition, but the new owners persevered.

Two years later, an appeals court overturned the lower judge's decision and removed all restrictions on the Evening News. The war was on between the two papers, especially for the Sunday edition sales. The Evening News was losing money and Buffett and Munger were seeing their capital decline by frightening amounts. At the same time, the Express Courier got an infusion of cash when it was purchased by a Minneapolis publisher, and it continued to be the favored Sunday paper. Then came the labor troubles. A total of thirteen unions were involved in the Evening News production and delivery. They had enjoyed some of the best wages in the country under the previous owners and Munger and Buffett knew they had to cap this expense above all else. The Teamsters, who delivered the papers, were the first to engage in contract negotiations. Buffett would not budge and threatened to close down the paper if concessions were not made. On one day, to prove he meant business, he sent all employees home, stating that if the paper did not go out, payroll could not be met. The other unions pressured the Teamsters, and concessions were accepted.

Eventually, another stroke of luck pushed Buffett and Munger into the black. The Minneapolis owner of the Courier-Express closed the paper, and Buffalo became a one-paper city. Immediately, the Evening News became the Buffalo News and began a morning edition, ushering in years of of huge profits. By the late 1980s, it was earning more than $40 million a year. Buffett had used earnings from Blue Chip Trading Stamps to buy See's Candy; he then used earnings from See's Candy to purchase the Buffalo News; profits from the Buffalo News could now finance his next venture.

With the paper on track and prosperous, Buffett became much more an absent owner, leaving the operation in the hands of the managing editor, Stan Lipsey. He maintained

the journalistic integrity of the publication, though many employees were saddened by Buffett's loss of interest in their work. Residents of Buffalo did miss having two papers in town.

Partners, Redux

Partners, Redux Summary and Analysis

As the years progressed, Buffett and his wife saw one another less and less frequently. The last child was in college and Susie continued to pursue her singing career. Eventually, in September, 1977, she left and moved to San Francisco. Buffett was devastated, and the home was now empty. They spoke by telephone daily and vacationed together, but continued to live apart. Susie, worried about Warren being lonely, encouraged a relationship between him and a waitress at the Omaha French Cafe, Astrid Menks. Eventually Astrid moved into Buffett's home and assumed wifely duties and providing the companionship that he missed. The relationship between all three was amicable, and children and friends alike were rather astounded.

What probably salvaged Buffett's disposition most was the recession and stock market decline of the late 1970s, a situation that motivated him to scoop up lots of bargains for Berkshire and himself personally. At the same time, he began to put into a portfolio all of his annual reports for Berkshire. These reports were not the standard fare, but, rather, homey, informal treatises filled with investment history, progress throughout the years, witty comments and quotes, and a unique ability to simplify the often complicated and overwhelming maze of investments, the market, and strategies.

During the 1980s, Buffett's writings seemed to espouse very definite themes. One was his fear of inflation which would de-value the dollar and, once set in motion, be impossible to reverse. As well, inflation devalued bonds, the overwhelming investment of insurance companies. His strategy was to invest in companies that could be inflation-proof, that is, those that could raise their prices without loss in sales—cereal and tobacco, for example. Another theme was the arrogance and vanity of corporate CEOs, whose puffed up opinions of themselves caused serious error in deal-making, buyouts, and mergers, often paying hugely inflated prices for companies on the auction block. Still a third theme was the criticism of CEOs amassing personal fortunes at the expense of their shareholders. To Buffett, CEOs were to be the good stewards of shareholders' dollars, because, after all, the shareholders truly owned the company.

By 1982, Berkshire-Hathaway stock was $750 a share because, Buffett stated, he invested shareholders' money as if it were his own. As the recession of the late 70s gave way to the "bulls" in the 80s, Berkshire stock continued to climb. By the end of 1983, the Dow was at 1245; Berkshire was at $1310 a share, and Buffett was named one of the richest men in America. There was some pressure from shareholders to split the stock, so that more investors might come on board. Buffett refused to do this, however, because he wanted permanent, long-term owners, not those who would purchase stock for short-term profits. In his annual letter of 1983, he told his shareholders that he would not succumb to the new Wall Street of "flipping stocks and companies like trading cards." Berkshire-Hathaway was an investment company that

held stock and owned businesses for the "long haul," and that would never change. Who could argue with his success?

The Carpet Woman

The Carpet Woman Summary and Analysis

The Nebraska Furniture Mart was a large warehouse-type structure in downtown Omaha. Buffett had "eyed" it in past years, and an offer to purchase it had been rejected by owner Rose Blumpkin, a Jewish-Russian immigrant who had escaped during World War I by lying to and bribing a border guard, crossing into Asia and finally meeting up with her husband in Seattle. She and her husband finally settled in Omaha. There, she ran a pawn shop and used clothing store until, in 1937, she managed to rent a small space on Farnham Street just a block away from the Buffett grocery store. She sold furniture at heavily discounted prices by buying overstock from other retailers. She discounted carpet as well. Her sales policy was simple—10% markup on everything—and, over the years, she built her business on repeat customers and by running any competition out of town. Buffett continued to watch the business grow.

In 1983, Mr. "B" agreed to sell the business to Buffett for $60 million, and she and her sons continued to run it. To Buffett, Mrs. "B" typified all that he had tried to teach others, specifically, that one must reduce money-making to simplicity and remain singularly focused. Mrs. "B's" focus was a high-volume/low price policy, also practiced by her sister and brother-in-law in their jewelry store, named Borsheims, another business Buffett eventually purchased.

The original Berkshire was a textile mill that made men's suit linings. It was a highly competitive business, constantly needing machinery upgrades, and it became a money-loser for Buffett. When the original manager, Ken Chace, retired in 1984, Buffett made plans to shut it down, giving employees severance pay and re-training. The equipment was auctioned off, but Buffett kept the property, leasing it out to a variety of businesses for years to come. Ken Chace and Buffett remained friends and confidants, however, and pooled their talents and strategies in future investing.

The Eighties

The Eighties Summary and Analysis

Buffett got wind of a potential takeover of Time Magazine and offered to become a major stockholder, never to sell. J. Richard Munro, the CEO, was unable to get approval of his board of directors, and, as an alternative, Time merged with Warner Communications, destroying its financial health. This 1985 merger was only one example of an entire new trend on Wall Street, to include mergers, acquisitions, and junk bonds being used to finance leveraged buyouts. Spurring all of this were pension and mutual fund managers who bought and sold stock daily, taking the high bid and running. Stockholders were no longer long-term investors but, rather, short-term daily traders and raiders who paid inflated prices for companies, paying for them through the sale of junk bonds.

Buffett decried the activity of Wall Street but still hoped for additional investment opportunities. An old friend, Tom Murphy, gave him the chance. Murphy was a privileged child who attended Harvard Business School and became involved in broadcasting, both radio and television, forming a company called Capital Cities. Buffett and Murphy had met in the 70's, and Murphy often consulted Buffett on major business decisions. In 1985, Murphy purchased ABC but called Buffett to say that he needed help with paying for it. Buffett knew that, if Cap Cities bought ABC, it would be a prime candidate for a hostile takeover, so Murphy needed someone who would buy enough shares and promise not to sell in order to ward off any takeover. Buffett knew he wanted to buy the shares, but there were problems with the FCC. Buffett already owned the Buffalo News, and one of Cap Cities television stations was in Buffalo. Murphy agreed to sell the station. The other FCC issue was sitting on the board of the merged Capital Cities/ABC and also that of the Washington Post. Buffett decided he could give up his board seat on the Washington Post and still remain active in the company, and he purchased three million shares of Capital Cities, giving Murphy the equity he needed to finance his purchase of ABC. The one snag was that ABC wanted warrants, that is, the guarantee that shareholders of the former ABC could buy stock in the newly merged company. This went against all of Buffett's beliefs, but, in the end, he agreed and lived to regret it.

During this time, Wall Street was going wild. Companies were being raided by hostile takeovers, and CEO's were running scared. Buffett saw Berkshire as a "save house" for solid businesses, a place to park the business and avoid the raiders. His first purchase in this vein was Scott and Fetzer, a conglomerate that owned a diversified set of businesses, to include World Book Encyclopedia and Kirby Vacuum Cleaners. For $315 million, Buffett purchased controlling interest and saved the company from a hostile takeover. He used cash from an unusual source—a hostile takeover. Philip Morris had recently taken over General Foods. Berkshire owned large block of General Foods and made $332 million profit when Philip Morris bought its stock. By the end of 1985, Warren Buffett was a billionaire.

ABC was a financial mess when Murphy took over, losing $70 million the first year Buffett owned it, despite tremendous cost-cutting on the part of management. However, Buffett had promised to hold it forever, and he was a man of his word. To Buffett, the themes of his investment practices were inviolate. To him, continuity was a philosophy of life—"to work with the same people, to own the same stocks; to be in the same businesses" (p. 272). A second recurrent theme was to avoid debt, as it was a "financial temptress" which could lead to loss of home or business. The third brick of his philosophy was that business and investment should create value, defined as some addition to "useful or desirable products and services" (p. 273). Leveraged buyouts merely moved money around and created tax breaks for the movers; no new value was created. This is how he approached Cap Cities/ABC. He retained the management he could trust, he committed for the long haul, and he vowed to create value without debt. Over time, ABC became financially stable and remained a big player in television programming.

Public and Private

Public and Private Summary and Analysis

By 1986, Berkshire shares were selling for $3000 each, having multiplied 176 times, while the Dow had merely doubled. Buffett had a large following, including all of the millionaires he had made of those early investors. Privately, however, Buffett lived no differently than he had years earlier, in a simple home and office, without computers, only a small office staff and no domestic help. He drank Pepsi laced with cherry syrup, until Coca-Cola launched its Cherry Coke, at which time he switched, purchasing cases at a time. As reserved and uncomplicated as he lived, however, he had become a hugely public figure. While most annual stockholders' meetings saw a tiny attendance, investors with as little as one share attended the Berkshire-Hathaway annual meetings, primarily to listen to Buffet and Munger answer questions of the audience. Every other year, he got together with his original friends from the Ben Graham years, most of whom were also investors. His office staff was and has remained minimal, each of the eleven employees completing their assigned tasks quietly. Buffett remained a private person, often lunching alone on McDonald's and Cherry Cokes. He relied on management of each company in his huge conglomerate to run their operation effectively and efficiently, refusing to engage in any form of micromanagement. He demanded a monthly financial report and little more. His managers have made their mistakes, to be sure, but Buffett refrains from firing them, trusting instead that they will learn from mistakes and motivate themselves to get back on track. That motivation is also in the form of extrinsic monetary rewards for profit.

One investing behavior that those in the business found particularly confounding was Buffett's quick decision-making about investment opportunities. Company executives would often visit him with proposals for investment from Berkshire-Hathaway. Prior to their arrival, Buffett had researched the company thoroughly, asked tough questions and either made an offer or declined their proposal. There was never a need for a second visit or negotiation, as he never changed his mind. His office staff has been minimal—eleven people at its largest—and each one completes his or her tasks with dependability and silence.

Berkshire was an odd investment conglomerate with only two levels of management. Buffett was the CEO of Berkshire, and the managers of each company comprised the second level. He has not required income projections from his managers nor does he communicate with them regularly. Each is required to submit a monthly financial report, which Buffett memorizes. Rarely will managers receive advice from him, nor will he veto any plans for re-organization or innovations. Twice a year, each manager is to transfer profits to Berkshire, but are largely left alone otherwise.

Crash

Crash Summary and Analysis

Insurance was a huge part of Berkshire by the mid-1980's, in the form of a group of casualty and property companies under the umbrella of National Indemnity. To Buffett, insurance rates were simply mathematics. Using the odds of disasters and car crashes, one simply priced policies accordingly. Buffett's insurance business was really re-insurance, that is, selling big policies to smaller insurance companies, thereby assuming some of the risk the smaller companies had in insuring individuals, especially high-risk policy holders. There had been setbacks in the insurance industry in the 1970's and always there was competition that might discount their premiums. Premium "wars" were not uncommon, but Buffett's policy was always to "ride them out." However, realizing that he had not managed the business well, he hired Michael Goldberg, originally a New Yorker and one who worked and lived much like Buffett, to manage National Indemnity. Refusing to lower prices when all others were doing so, the business shrank in the early 1980's. However, Buffett and Goldberg were patient, knowing that discounted prices could not be sustained by their competitors. By 1986, the Berkshire reinsurance business was back and profitable, bringing in a billion dollars in that year alone. After expenses, $800 million float was leftover, that is, money that was available to reinvest. Berkshire had a huge amount of cash by 1987, but no bargains to buy. The Dow was too high, dangerously so, according to Buffett. So, he poured his cash into municipal bonds and waited.

Buffett received a panicked call from Harry Gutfreund, CEO of Salomon Brothers, who was facing a hostile takeover by Ronald Perelman of Revlon. Salamon's biggest shareholder was a company called Minorco, and Perelman expressed his interest in buying Minorco's shares. With some hesitation but also with a favorable deal, Buffett plunked down 700 million dollars of Berkshire money to thwart the Perelman takeover. He faced significant criticism, because he had just done what he always cautioned against—buying in with a firm of traders.

The Dow continued to climb far more than the value of its stocks, and investors were trading wildly. Finally, in October, 1987, amidst inflation, trade deficits and a declining dollar, the Dow began to dump. Yields on bonds went up. Buffett began to clear out his stock portfolio, taking what profit he could. On October 19, the Dow dropped 508 points and Buffett's net worth dropped by $342 million. However, no depression followed, and the Dow began to climb again in 1988. Berkshire shares had dropped from $4320 to $3170.

A Brief Introduction to Darts

A Brief Introduction to Darts Summary and Analysis

There are two basic schools of thought about investing in the stock market. The Efficient Market Theory says that a stock is worth whatever it will sell for, and the key to doing well is to diversify. The other school states that a stock's value should be based solely on the factual data available about a company, and the way to do well is to purchase only bargains and invest only in companies whose business you fully understand, for the long-term. Buffett has held to this latter school for most of his investing life, and it has "worn well with time." To the first school, picking stocks by throwing darts is just as valid as any other method; Buffett, they insist, has not been right, but merely lucky. Both schools have differed on the definition of "risk" as well. To Buffett, risk is paying more than the business is worth, and that worth is dependent upon net profit, number of customers and quality of management. To the Effective Market Theory school, risk is based upon historical volatility of the stock itself. Less volatile stocks have lower risk return while more volatile stocks have higher risk and higher potential returns. Stocks were subsequently assigned a "beta" number. If they rose and fell much as the market as a whole did, they were given a "beta" of 1.0. Above 1.0, a stock was more volatile than the market, and "betas" cold be as high as 2.5.

The Efficient Market Theory followers took hold of Wall Street in the 1980s, and they expanded into the purchase of index funds, that is, large groups of diversified stocks. Speculation was rampant, and no one thought long-term investing was wise. The idea was to have fund managers, who bought and sold on a daily basis in order to gain profit at the end of the day. Buffett condemned this behavior as irresponsible and irrational, because it was not based upon solid analysis of a company's value. He proclaimed that this type of investing was dangerous and would ultimately result in overall market instability. No one listened. In October, 1987, the crash hit, and no one really knew why. Fund managers, afraid of other fund managers, began hyperactive trading. The end result was a major sell-off and market decline. Buffett felt somewhat vindicated, but no one on Wall Street acknowledged his correctness.

Secrets of the Temple

Secrets of the Temple Summary and Analysis

In the fall of 1988, Buffett began to quietly purchase Coca-Cola stock. The CEO caught on but agreed to remain quiet until Buffett had purchased all he wanted—7% of the company for $1.2 billion. In making the decision to purchase Coke, Buffett used his refined principles of investment, based upon minor revisions of his original guru, Graham:

1. Do not consider the trends or forecasts given by the Wall Street analyzers—focus only on the long-term value of the company;

2. Invest in companies whose business you understand—if you do not understand the business, you cannot determine its value;

3. Research management of the company—managers who see themselves as true caretakers of stockholders' money are good ones;

4. Study the company yourself—do not rely on so-called "expert opinions" of others;

5. If you develop a conviction about a company, buy the stock.

These five principles guided Buffett in not purchasing common stocks between the years 1985-1988. His purchase of Coca-Cola was based upon its simplicity and its long-term value. Coca-Cola was reaching into an international market, had suffered some bad years, and its stock was a bargain. The CEO, Roberto Goizueta and Donald Keogh, the president, had divested the company of its non-cola holdings and began to concentrate on international markets and distribution. By 1987, profits from foreign sales had gone from a low of $607 million to $1.11 billion, and the overseas market was far from tapped. It was the value that Buffett saw. Further, he saw management that operated exactly as he wished. Wall Street analysts liked Coca-Cola too, but were not so bullish as to recommend a strong buy. When Berkshire's investment in Coca-Cola was disclosed, its (Berkshire's) stock rose from $4800 a share to $8000 a share in six months. Buffett himself was worth $3.8 billion, and he continued to maintain a close eye on Coca-Cola's expansion and profits.

Above all else, Buffett continued to insist that investing was a simple endeavor which people mistakenly made complicated. Many of his followers argued this a bit, because Buffett had the unique ability to remember all facts and figures about hundreds of companies at a time and was able to spout them as if his brain held drawers for each one. The common investor was unable to absorb and retain so much information at one time; however, certainly, as Buffett said, he was able to research companies one at a time and come to a conclusion about them by following the five principles he laid out. The problem was, he said, people confused "simplicity" with "ease." There was nothing

easy about research and thought—it just came easier to him than to others. Once one had the factual data, the investment decision was simple.

Howie Buffett's Corn

Howie Buffett's Corn Summary and Analysis

Buffett's relationship with his children was unusual and certainly different from the relationship between other super-rich and their children. Indeed, Buffett spoke and wrote terribly scathing words about the practice of the rich simply passing out their wealth to family members, particularly children, rather than contributing to societal good. For his part, Buffett contributed an annual gift of $10,000 to each child and no more. If he loaned them any money, a payment agreement was drawn up.

Susie, the daughter, seemed to accept her father's approach to his children. Each child had been left a small amount from their grandfather, and Buffett had invested it in Berkshire. Had they left the investment in, they would have been millionaires. Susie cashed hers in to buy a Porsche. Her marriage failed, and she moved to Washington, eventually marrying Allen Greenburg, an attorney.

Howie sold his stock to finance an earthmoving business which failed. After a short time in California, working for See's Candy, he returned to Omaha and sent into real estate. He also rented some land and grew crops, which he sold. Buffett knew that Howie really wanted a farm, and, in a moment of generosity, offered to buy a farm and rent it to Howie, who would turn over a percentage of the profits and pay the taxes. Howie loved the farm and wanted to share the experience with his father, who, in turn was only interested in timely rent payments. Eventually, Howie went into local politics and became involved in promoting ethanol. He subsequently secured an executive position with Archer-Daniels Midland and won his father's approval, having "made it" on his own.

Peter sold his Berkshire to purchase equipment for sound studio in San Francisco, a business that did not do well. He moved to Milwaukee and began to produce jingles until he wrote the score for a major musical number in the movie, "Dances with Wolves." He also enjoyed some success recording "New Age" music, and his relationship with his father blossomed as well.

It appeared that, as he aged, Buffett mellowed toward his children. He offered Susie's husband a position managing the Buffett Foundation, and they moved back to Omaha to do so. He and Peter became quite close. Howie made him proud. He spent time with Susie's children, and Susie became a director with the Foundation. His wife and Astrid continued to be amazingly close.

Perhaps satisfied with the way his children turned out, Buffett did decide that he would leave them something—perhaps three million each. However, he still felt strongly that society as a whole deserved the bulk. In the area of philanthropic pursuits, however, Buffett seemed stalled. If he gave money to charitable causes, that was less he had to grow more money. Berkshire contributed every year, but it was done by allowing each shareholder to donate six dollars per share to his or her favorite charity. None of this

came from Buffett's personal wallet, and his basic "stinginess" remained. His foundation accumulated much more each year than it gave away, and Buffett could not easily select causes because he could not chart their successes the way he could a company's.

Two passions of Buffett were nuclear disarmament and population control. Accordingly, he funded a professor who proposed "risk reduction centers" in Moscow and Washington, so that leaders could communicate quickly and completely in crisis situations. In 1990, he contributed $1.7 million to sex education, family planning, birth control and abortion rights. Thus he focused on future problem-solving, seeing his gifts as investments in the future. He disliked the idea of contributing to alleviation of current ills, because he felt it could corrupt the donee who would rely on charity rather than on his or her own need to be self-reliant. One annual giving program Buffett enjoyed was a ten thousand dollar gift to fifteen teachers in Omaha Public Schools, the recipients being selected on merit. As for his personal wealth, Buffett vowed never to sell any of his own Berkshire shares. He would leave them to his wife if he died first. Whoever died last would leave them to the Buffett Foundation for charitable purposes.

As stingy as Buffett was relative to charity, his politics were quite leftist. He has always believed that the entire tax system should be re-structured so that consumption and inheritance were taxed most heavily. In his view, heavy consumers use up societal resources and heirs do not earn any of their wealth.

Rhinophobia

Rhinophobia Summary and Analysis

After the October, 1987 crash, Wall Street rallied with a new wave of leveraged buyouts. Cast to fund these came largely from the sale of junk bonds and "zero coupon bonds," by which sellers could hold off paying any interest for years. Buffett took short-term advantage of a proposed buyout of RJR Nabisco by purchasing the stock before the buyout and selling it after the stock jumped. He refused to participate further in such activity but found himself with an overload of cash and no place to put it. In investment circles, this is known as "rhinophobia," the fear of having too much cash on hand and the temptation to do something with it, even if that something is not particularly wise. Buffett succumbed, and Berkshire purchased convertible preferred stock in Gillette, USAir, and Champion Paper, all of which were being threatened by hostile takeovers. The stock gave fixed dividends but could be converted to regular preferred or common stock at any time. For the perk, Buffett agreed to stay in for ten years.

Champion Paper was clearly badly managed. Its profits were the lowest in the industry, and the CEO, Andrew Sigler, was continually raising his salary and options. USAir was in the midst of expansion, and management looked good to Buffett. Gillette was a great money-maker. Shortly after these purchases, he reversed course again by buying up RJR Nabisco junk bonds to the tune of $440 million, because they were at a "bargain basement" price. When corporate bankruptcies and junk bond default hit new highs in 1990, Buffett invested in the ailing Wells Fargo Bank, an institution that began to take in water shortly after his purchase. With still more cash on hand than he wanted, Buffett helped to bail out American Express by investing an additional $300 million dollars. James Robinson, the CEO, had frittered away all profits on poor diversification investments, and Buffett was willing to take the long-term risk, because the basic business of American Express—credit cards and travelers' checks—remained sound, if the company could just sell off its clunkers and focus on what it did well. By the end of 1991, Wells Fargo, American Express, USAir and Champion Paper were all in trouble, and Buffett blamed himself in his annual report to Berkshire shareholders. Fortunately, Coca Cola, Gillette and RJR Nabisco more than compensated, and Berkshire stock continued to rise, to $8800 a share.

Buffett seemed to change personally during this time. He upgraded to a better jet and spent far more time out of Omaha, rubbing elbows with jet-setters and politicians. He maintained his "Will Rogers" image as best he could but was certainly becoming a national celebrity himself, so much so that his wife and daughter began to dress him more for the part. Another major event was the loss of "Mrs. B" from the Furniture Mart. She and her grandsons had a falling out, and they removed her as the carpet manager. She subsequently opened up a competing store next door, and sold her Berkshire stock.

The King

The King Summary and Analysis

Salomon Brothers was born from a family quarrel. Originally from France, Ferdinand Salomon came to America and continued his career as a money lender to securities firms. He had four sons, three of whom went into business with him. As Ferdinand was an orthodox Jew, he refused to work on Saturdays, but the sons balked at this. Eventually, the sons scraped up five thousand dollars and split from their father, forming Salomon Brothers. Originally, the Salomon brothers brokered money but moved into corporate bond trading and Treasury securities as well. The firm remained small and was not considered equal to the larger firms which dealt in underwriting and investment banking.

The decision by brother William to require that investors in Salomon Brothers leave their money in the firm, drawing only 5% each year, weeded out the short-termers and allowed the capital to grow. In 1979, IBM asked J.P. Morgan to share its underwritings with Salomon Brothers. J.P. Morgan, in a moment of arrogance, refused, and IBM chose Salomon exclusively. By the late 1970's, private Wall Street firms that existed largely as partnerships (a small number of investors) saw a need to raise capital. This could be done by "going public," that is, offering shares of stock to anyone who wanted to buy, or by selling to another publicly held corporation at a profitable price. At Salomon, this was a matter of heated debate, but, in the end, it was sold to Phibro Corporation, and the partners each made $7 million. Salomon continued to be managed by the Salomons and John Gutfreund, a New York native who had become a partner and spearheaded its growth.

Under Gutfreund's continued management, the company soared. Buffett bought in and got a seat on the board of directors. Troubles began when some deals went sour (leveraged buyouts and junk bond loans) and infighting began as Gutfreund had to cut staff and tighten the belt. He began to seek the counsel of Buffett instead of his colleagues. Buffett liked Gutfreund's integrity. What he did not like was the bleeding of money and the concurrent huge bonuses being paid to executives, even at a time when Salomon was losing money. Buffett believed, as always, that this practice was cheating the shareholders.

Paul Mozer was head of the department that dealt with government bonds and treasury notes. Salomon bought these for themselves and often for client companies as well. The basic idea was to bid for them at an auction and then, often, to resell them to others. There were thirty-nine primary dealers, those that the Federal Reserve Bank of New York allowed to bid for themselves and for others. Anyone else could bid for themselves, but the bid awards were limited, so that no one could ever purchase more than 35% of the Treasury notes available. Mozer found a way, albeit illegal, to get around this. He would bid for Salomon and then submit bids for other client companies, even though those companies had not authorized him to do so. Then, he would write up

a fictitious sale of the notes from the client company back to Salomon. This was discovered within Salomon itself and reported to Gutfreund, who knew he should report it but procrastinated. Undaunted, Mozer then put in a huge bid for Salomon and two of its customers, taking 85% of the notes available. Other traders who needed the notes for their customers had to then buy them at an inflated price from Salomon. They complained. The SEC (Securities and Exchange Commission) began a quiet investigation of Mozer's practices not even knowing about Mozer's earlier false bid, because Gutfreund was now even more afraid to disclose it.

Eventually, the news broke and Gutfreund and Strauss, the one Salomon attorney who knew about the false bid, had to call the Federal Reserve Bank President and the SEC and confess. They issued a press release as well and placed Mozer on suspension. When the news broke on Wall Street, Salomon stock began to fall. Clients pulled out, refusing to do business with the company any longer. Gutfreund and Strauss were blamed, and the investigation heated up. Gutfreund called Buffett, urging him to come and take over. Buffett and Charlie Munger both flew in to see what could be done. Gutfreund and Strauss resigned, leaving Buffett temporarily at the helm, a position he really did not want. Trading of Salomon was halted while the firm re-organized, but clearly, it would be a tough battle. Buffett's first step was to announce to all managers that, from that moment on, even the slightest hint of inappropriate activity would not be tolerated, a statement repeated in the New York Times the next day. Mozer was fired.

Salomon's Court

Salomon's Court Summary and Analysis

Buffett convened a meeting of Salomon managers and, one by one, asked them privately who should run the company. Overwhelmingly, they selected Deryck Maughan from their ranks. While Buffett was holding this meeting, he learned that the Treasury Department had just banned Salomon from its auctions. Buffett spent the remainder of the day in conference calls with Treasury officials and Federal Reserve Board Chairman, Alan Greenspan. He plead for grace and time. In the meantime, he also had Salomon's lawyers prepare bankruptcy papers.

On the next day, Secretary of the Treasury, Brady, called Buffett, who updated him on the changes in management and gave promises to fundamentally change Salomon's business practices from the ground up. While Brady was not particularly concerned about the potential demise of Salomon, he did know Buffett. By a strange coincidence, Brady, an MBA from Harvard, wrote his Master's thesis on his family's business—Berkshire Fine Spinning. He knew full well what Buffett could accomplish. Buffett warned Brady, however, that he would not assume the chairmanship of Salomon if the banning of Salomon from Treasury auctions stood. Brady stated that he would get back to Buffett later. By late afternoon, Buffett held a press conference, introducing Maughan and announcing two things—he would be interim chairman at no pay, and the Treasury Department had decided that Salomon could bid at auctions but only for itself. The press conference lasted for three hours, but Buffett came out on top and assured reporters that Salomon would move forward with impeccable integrity.

Now for the real work—developing a strategy to satisfy the government, the press, customers, creditors and Salomon employees. Buffett fired the in-house attorney, Fuerstein, and managed to talk a "squeaky-clean" attorney friend, Robert Denham, to leave his practice and join the Salomon team. He then began to liquidate assets at the same time that several customers were leaving. He met with the SEC Chairman and promised full cooperation with their investigation of Salomon. He gave his home phone number to all executives, with instruction to call him if they felt anything inappropriate was occurring. His ultimate goal was to avoid a Justice Department indictment, and he had to do so by opting to cooperate in every way possible.

Congressional hearings on Salomon began with Buffett as the primary witness. He began by apologizing for the behavior of the few Salomon executives who had performed without integrity. Again, he promised a new corporation which would act only in full compliance with laws and regulations. Hearing his apology changed a lot of minds. In times past, investment bankers on the "hot seat" had been defiant or non-compliant. Buffett's final point of his opening statement was this: "I want employees to ask themselves whether they are willing to have any contemplated act appear on the front page of their local paper the next day, to be read by their spouses, children and friends...If they follow this test, they need not fear my other message to them: Lose

money for the firm and I will be understanding; lose a shred of reputation for the firm, and I will be ruthless," (p. 395)

Buffett was not used to a battle to save a company nor to the demands of creditors, investors, Salomon staff and the press. Fortunately, he had self-confidence, the ability to keep his eye on the goal, and a remarkable talent for communicating with everyone. He released all documents to the SEC, showing all of Salomon's "sins," he fired all political consultants and the legal team that had been associated with Gutfreund; he banned all political gift-giving. The press was brutal, and the Salomon scandal remained front-page news; more clients and investors bailed; the stock dropped to 20 3/4. Buffett's biggest challenge with the corporation itself was bolstering the morale of managers. To ease the financial crisis, he sold off $50 billion of Salomon's assets, and most analysts felt that Salomon would survive but as a smaller, far less powerful firm. Gradually, Buffett began to spend less time in house, retreating to Omaha as much as possible. As was his traditional practice, he left the daily operations to Maughan.

The biggest long-term issue Buffett had with Salomon was its relatively small return to shareholders. He believed this to be the result of a single practice—the ridiculously high bonus program for which Gutfreund was famous. In October, 1991, he paid for two page ads in the four largest newspapers and published Salomon's third quarter report. Within the report was the news that $110 million was being cut from the end-of-the-year bonus money pool. As well, some two hundred eighty staff were laid off. Outside the company, the move was applauded. Inside, traders and managers began to defect, and some good talent was lost. Buffett managed to hold onto some younger analysts by giving them moderate bonuses, and designed a system that would tie future bonuses to actual performance. Over the first year, however, many traders and bankers left for positions with competitors.

Critics of Buffett surfaced to take their shots at his performance. Despite the fact that he had saved Salomon, they pointed out that he was an "old-fashioned" mid-westerner who was publicly concerned with ethics and morals but was probably personally not "Mr. Clean." They pointed out his mistress. His wealth was attributed to lucky coin tosses. Buffett, who was used to operating independently and insulated from Wall Street, was profoundly affected by what he perceived to be disloyal employees and a vicious press.

Eventually, the Justice Department and the SEC determined that Salomon should plead to a felony and pay a $400 million fine. The case was weak, however, and no criminal activity beyond Mozer's false bids could be found. Buffett defended the company personally to Federal Prosecutor Otto Obermaier in a lengthy meeting. In the end, charges were dropped, and Salomon paid a fine. Salomon stock began to rise, and was 25% higher by the time Buffett stepped down as board chairman in June, 1991. Bob Denham, Buffett's lawyer throughout the case, took his place and Deryck Maughan continued to manage the firm. Over time, Salomon recouped, filled its management and trader openings, and Buffett purchased more of its stock. While stating that the experience was "interesting and worthwhile but far from fun," he was thrilled to be back in Omaha, focusing on Berkshire, his first love.

Buffett's Trolley

Buffett's Trolley Summary and Analysis

During the early 1990's, Buffett continued to expand his investments and profits, purchasing General Dynamics, more Wells Fargo (purchased at 62, rising to 145), Guinness, and Gannett Publishing. He also bought three shoe manufacturers and welcomed "Mrs. B" back by purchasing her store. His previously purchased holdings all continued to rise, except for USAir. Berkshire stock itself soared to $16,325 by the summer of 1993, then to $20,400, at which point Buffett was worth $9.7 billion, surpassed only by Bill Gates. Buffett's average annual growth over thirty years was 26.77%, the Dow Jones, just 9.51%. An investment of $10,000 in Berkshire in 1965 would have grown to $11.3 million by 1994.

The future may provide challenges for Buffett. He has relied heavily on consumer products, television and newspapers. Public movement to high tech and discount retailers may pose problems for his investment strategies. One area Buffett considers is re-insurance, banking on only one-two catastrophes a year. This brings in large sums of cash which can be used until the next catastrophe occurs. For himself, Buffett remains an agnostic and the lover of a simple life in Omaha. He deplores the thought of running businesses; he simply wants to own them. His love is the accumulation of money and assets, not in spending. He continues to hold his annual stockholders' meeting in Omaha at Borsheim's Jewelry Store. Most of his shareholders are known to him personally.

Buffett's investment strategy has changed very little. A company's value is based upon current assets and growth potential. Investing should occur only when the share price is below the value. Value, one must remember, includes the quality of management. The big concern, of both Buffett and his investors, is the fate of Berkshire once the leader is gone. Munger, if still alive, will assume the helm; if not, Buffett has a successor, but refuses to reveal the person's identity. As well, Berkshire has a board of directors, currently comprised of his wife, son Howie, himself, Ken Chace, Munger, and a local friend, Walter Scott.

Buffett continues his unique relationship with Susie and Astrid. He and Susie meet somewhere at least once a month, and he and Astrid operate as any married couple in Omaha. Each fulfills separate and distinct needs. As well, in his waning years, he has eased up on the finances, supporting the local minor league baseball team, a Rose Blumkin Performing Arts Center and Children's Theater. The overall picture of Buffett, however, is that of a modest man who remains in the same home, drives his own cars, and likes bargains in groceries as well as stocks. He retains his investment philosophy and espouses it still to informal groups and college audiences.

Perhaps the greatest legacy to be left by Warren Buffett is the unraveling of the mystery of Wall Street, the common sense approach that flew in the face of the investors who

insisted and continue to insist that the value of a company's stock is whatever someone will pay for it. Further, unlike Wall Street, Buffett invests in a solid company, in his own words, "forever," and has become the second wealthiest American by doing so. However, perhaps the larger part of his legacy lies in the values of commitment and loyalty, not just with respect to investing but in the operation of both our personal and professional lives.

Characters

Warren Buffett

Multi-billionaire from Omaha, Nebraska, Warren Buffett has made himself and others rich by very specific investment principles, which he has followed almost exclusively throughout his adult lifetime. As a young boy, Buffett was fascinated with numbers and money and, at a very young age, vowed to become rich, not for what riches could buy but, rather, just for the fun of accumulating money. He developed several plans for making money, to include gathering up used golf balls at the local courses in Omaha and re-selling them. When his family moved to Washington D.C., he built up five paper routes and, with a friend, placed pinball machines in barbershops. By the time he was a senior in high school, he owned stock and land in Omaha. He went on to college and graduate school, becoming a faithful disciple of Benjamin Graham, who taught that the value of a company determined the worth of its stock and that the only time to purchase a stock was when its price was lower than the company's value. Buffett added other principles to his guru's and spent his life primarily investing in companies based upon low stock price, long-term prognosis, effective management, and solid understanding of the business. Most investments are "forever," though the concentration seems to be on consumer products, re-insurance, and publishing. Buffett is considered rather odd for his status as the second richest man in America. He still lives in the home he and his wife Susie purchased early on in their married lives, drives his own cars, and drinks Cherry Coke by the case. His personal life is not particularly traditional either. His wife lives in San Francisco, and Buffett continues to reside in Omaha with his mistress, Astrid Menks. The three are wonderful friends. Buffett has three children, of whom he is quite proud, but he does not intend to leave his fortune to them. Believing that inheritance breeds irresponsibility, most of the fortune will go to the Warren Buffett Foundation, run by his daughter and son-in-law. Warren Buffett's legacy goes beyond investment advice and strategy. His values of commitment and loyalty, his belief that money should be used for societal good, and his modeling of a moderate lifestyle free of excesses, provide a blueprint which many other corporate leaders and politicians might consider.

Benjamin Graham

Born in London as Benjamin Grossbaum, Ben Graham came to America (New York, specifically) as an infant. Despite the poverty imposed by his father's early death and his mother's loss of all of her savings in the stock market crash of 1907, he excelled in school and went to Columbia University. Taking a job on Wall Street, he took to the world of finance and investing extremely well. He became a frequent lecturer and authored several books on investing. Graham's investment partnership was almost wiped out during the Depression, but a partner put up money to allow the the company to survive. He continued to teach at Columbia, where Warren Buffet was enrolled. Buffett became a disciple of Graham and followed his book, Security Analysis, as he

began his own investment career. The main theme of the book was that investors should pay attention to the intrinsic value of a company, not to the market price of its stock. Stock should be purchased only when it is below the intrinsic value of the company and held until the stock price adjusts to an appropriate level. Graham's personal life was interesting. He had a number of wives and mistresses during his lifetime and was distant with his children. He eventually formed Graham-Newman, a mutual fund, and followed his own investment strategies, hunting stocks that were at least one-third less than their net capital. For a while, Buffett worked for Graham but was really interested in striking out on his own. In 1956, Graham retired to California, taught at the University of California, and led a life of leisure with his wife and mistress.

Susie Buffett

Susie Buffett grew up in Omaha, daughter of a minister and psychology professor. Her parents were friends of Warren's parents, and she roomed with his sister at Northwestern. She was an outgoing young lady who, having spent a sickly childhood, was so enamored with her healthy life that she loved life to its fullest, and reached out to others. Having no fear of death, she often spent time with those who were dying, the complete antithesis of Warren Buffett who feared death and would not approach the subject. They dated once or twice, but Susie was in love with another man, to whom her parents objected because he was Jewish. Her parents approved of and liked Buffett who spent many evenings in their home, and so, eventually, she gave in and allowed Warren to "court" her. They were married in 1952. Buffett was not the rich man he told Susie he would be, and they rented a dilapidated apartment, putting their first child, Susie, in a dresser drawer for a bed. As time went on, Susie became the organizer of Warren's life and dutifully managed all of his personal needs. They had three children in all, but, as Buffett became more prominent and was absent from home more often, and as the children grew and left, Susie began to desire a life of her own. She had always wanted to become a singer and put together a band, performing at local nightclubs. She was actually quite good, and Warren could not have been happier with her new "project." Eventually, Susie moved to San Francisco, feeling stifled by Warren and Omaha. He was devastated, but she stood her ground. Eventually, Susie cultivated a relationship between Warren and Astrid Menks, an Omaha waitress she had befriended during singing engagements, and Astrid moved into the Buffett house, taking the place of Susie. Still, Susie and Warren have continued their relationship, meeting at least once a month, and she is a member of the board of directors of Warren's investment firm.

Howard Buffett

Father of Warren, Howard grew up in a family that ran grocery stores in Omaha. Howard had no desire to go into the family business. He attended college at the University of Nebraska in Lincoln and was editor of the college newspaper. He met and married Leila Stahl, daughter of the West Point, Nebraska weekly paper editor. She met Howard at college, and they married and returned to Omaha, where Howard began

work for an insurance agency. He later took a job as a securities salesman with the Union Street Bank, but the Depression brought bank failure and loss of job. Howard paired up with a partner, George Sklenicka and, together, they peddled securities, not an easy task during the Depression. Income was so low that there was often not enough to eat. They survived, however, and Howard became a bit more prominent in Omaha. Howard was highly principled and taught his children that they must serve the community as well as themselves. In 1942, the local Republican Party convinced Howard to run for their Congressional seat against the favored Democrat. Howard was a New Deal hater and an isolationist but was well-liked locally and won. He lost in 1948 and returned the family to Omaha.

Leila Stahl Buffett

Growing up in West Point, Nebraska, Leila Stahl had an invalid mother and educated newspaper editor. She graduated from high school at the age of 16 but was unable to attend college immediately, and assisted her father at the newspaper, setting type and interviewing travelers when the train would stop at their station. Eventually she went to the University of Nebraska at Lincoln where she met Howard Buffett. They married as soon as he graduated and settled in Omaha. Life was not easy during the Depression, and Leila had to work outside the home to make ends meet. Eventually, the family prospered and they moved into a more substantial home. There was a history of mental illness in Leila's family, and it is believed that she suffered from it as well. For no apparent reason, she would fly into rages that often lasted for hours, and the children, one of whom was Warren, took to staying away from home as much as possible. When the family moved to Washington, however, Leila was a staunch supporter of Warren's efforts to make money, often helping him with his paper route.

Charlie Munger

Charlie Munger was a lawyer by profession but since the 1960's he had managed Wheeler, Munger and Company, an investment partnership in California. He and Buffett met quite by accident. Both had been purchasing stock in Blue Chip Stamps, a grocery store trading stamp company popular in those times. Buffett eventually became the largest stockholder, Munger the second largest. Buffett and Munger eventually met and formed a friendship and alliance which has stood the test of time. They have invested together and are of the same philosophical approach to the stock market and the value of companies. Most people see them as "clones" of one another.

Rose Blumkin

Affectionately known as "Mrs. B," Rose Blumkin was born Rose Gorelick in Russia. She married Isadore Blumkin who immigrated to the United States just before World War I. She was to follow, but the war broke out and she could not get out of Russia. She managed to travel to the Chinese border and talk her way across and, eventually, joined

her husband. They settled in Omaha and she was able to subsequently purchase the Omaha Furniture Mart which she ran with a passion, driving out all competition. Buffett bought the store, but Rose and her children and grandchildren continued to manage it. She left the store following a dispute with her grandsons and set up competition next door. Eventually, all was resolved and Mrs. B. returned to the fold. Even though uneducated, Buffett thought her to be one of the most astute business people he had ever known.

Kay Graham

Kay Graham inherited the Washington Post when her husband died, but had no idea how to run it. She hired Benjamin Bradlee to run the paper, and it became famous for publishing the Pentagon Papers and then breaking the Watergate scandal. Buffett began to buy stock until he owned 10%. He was invited onto the board of directors in 1974. Buffett and Graham became fast friends, and many suspected the relationship might be more than just platonic. No one ever knew for sure, but Buffett "schooled" Kay in the financial management of her business, an action for which she was certainly grateful.

Astrid Menks

Astrid was a waitress at the French Cafe where Susie Buffett had singing engagements. She was raised primarily in an orphanage and lived in the bohemian section of Omaha, leading a very different life from the Buffetts. When Susie left Warren, she encouraged Astrid to drop in on Warren and fix him a few meals. Within a year, Astrid had moved into the Buffett home with Susie's blessing. Together they have remained, and move about Omaha as any typically married couple. Warren, however, is still married to Susie whom he sees at least once a month.

John Gutfreund

John Gutfreund was the CEO of Salomon Brothers and an effective manager, in Warren Buffett's eyes. Buffett particularly appreciated Gutfreund's integrity. Gutfreund's big mistake was not reporting an illegal bid of one of his managers to the SEC and the Treasury Department. It eventually cost him his job, severance and benefits, and Buffett had to step in and run the company for a period of time. Buffett was saddened that Gutfreund had gotten himself into such a position but, if the company was to survive, his ouster was the only solution.

Objects/Places

Omaha, Nebraska

Home of Warren Buffett , where he has lived most of his life, and from where he manages Berkshire-Hathaway Investment Company.

Kiewit Plaza

Small group of office buildings in downtown Omaha where Buffett has his modest office.

Indefensible

Name of Buffett's private jet.

Gorets

Steak house in Omaha and Buffett's favorite place to dine.

Laguana Beach, California

Site of Buffett's vacation home.

Nebrasks Furniture Mart

Large warehouse-type furniture and carpet store in downtown Omaha owned by Buffett and managed by the Blumkin family.

Borsheim's Jewelry Store

Owned by Buffett, managed by relatives of the Blumkins, and site of the annual meeting of shareholders of Berkshire-Hathaway.

Farnam Street

Major street running through Omaha. Buffett purchased a modest home on this street years ago and still lives there today.

Steam Shed and French Cafe

Two nightclubs in Omaha at which Susie Buffett had singing engagements.

Hathaway Manufacturing Company

A cotton mill in New Bedford Massachusetts which became the largest manufacturer of men's suit linings. An early acquisition of Buffett's, its name became part of the name of his investment firm.

Berkshire

A cotton mill in Rhode Island originally owned by the Chace family and which Buffett merged with Hathaway in 1955.

Columbia School of Business

Graduate school at which Buffett took classes taught by Benjamin Graham

Themes

Investment Need Not be Chance or Luck

Despite Buffett's rather consistent and pervasive success, Wall Street "big boys" have continued to attribute these accomplishments to luck or chance. They posit that Buffett has simply been one of those "blessed" investors who, by randomness, has managed to pick winners. Buffett, however, insists that his financial fortune is the result of very specific axioms which he has practiced throughout his investment career. These axioms include the approach of Benjamin Graham, his graduate school professor, and his own strategical additions. Successful investing involves four basic activities: 1) A company being considered for investment must be thoroughly researched in order to gain an understanding of its intrinsic value and its long-term potential for sustained growth; 2) A stock should only be purchased when it is a bargain, that is, the price is less than the net profit and/or assets of the company; 3) Management of a company should be focused on good stewardship of shareholders' money and must be lean and efficient; and 4) Investments should be for the long-term, requiring patience and discipline. It would appear the Buffett's strategies are well worth following, for he has consistently beaten Wall Street over a fifty-year career in investment, making his investors wealthy as well. In Buffett's own words to Wall Street fund managers and investment bankers, "If you're so smart, how come I'm so rich?"

Continuity is the Key to Success

In both his personal and professional lives, Warren Buffett has practiced continuity. From a personal standpoint, he has lived a thoroughly consistent moderate lifestyle, avoiding the excesses that many of the super-rich seem to practice. He continues to live in his modest home on a main street in Omaha, drives his own cars, eats in the same restaurants, and believes that his family members must be independently responsible for their own financial well-being. Accordingly, when his sister failed to exhibit continuity in her financial activity, he refused to bail her out. When his children cashed in their initial Berkshire shares for unsuccessful pursuits, he did not replace their losses. His relationships with both his wife and mistress have remained constant, each fulfilling specific needs. From a professional standpoint, Buffett has seldom veered from his basic beliefs about investing, following the same strategies over a fifty-year history. Thus, he invests for a lifetime, never abandoning a company or manager, but, rather, preferring to allow managers to learn from their own mistakes and depending upon his basic belief in the long-term potential of a company. As well, he consistently tailors investments to specific types of companies, those which offer products and services that will have value despite the ups and downs of the market and the economy in general (for example, popular consumer products and insurance).

Companies Must be Stewards of Shareholders' Money

One of Buffett's greatest complaints about American corporations is that the CEOs and upper-level managers have little or no relationship with the vast majority of their investors. In this climate, Buffett asserts, there is no commitment to use profits to benefit the shareholders first and themselves second. Thus, corporate bonuses and random unwise investments become the rule, often resulting in only small returns on investment for the stockholder and huge wealth for the executives. Indeed, if a company does poorly, it is not the executives who suffer—their salaries and bonuses remain extraordinarily high. Annual reports to stockholders are complex, difficult to understand and provide very few means for the average investor to understand a company's health. Buffett, on the other hand, knows the vast majority of his investors on a personal level, holds a huge annual meeting which is attended by almost every shareholder, and publishes an annual report which is simple, straightforward and honestly depicts the successes and failures of the firm over the year. Buffett himself takes a very modest salary for managing Berkshire-Hathaway, and provides himself no annual bonus, even when the profits have been extraordinary. In Buffett's eyes, ethical and personal treatment of investors guarantees long-term investment relationships, rather than consistent buying and selling of shares, and allows a firm to compound its success over time. This way, everybody wins.

Style

Perspective

As Roger Lowenstein states, his interest in the study of Warren Buffett came about as an investor in Berkshire Hathaway and as a financial reporter for the Wall Street Journal. In these capacities, he hoped to mesh a familiarity with Buffett's personal and professional life and the objectivity of a reporter. In much of the work, this was accomplished. While Buffett himself refused to become involved or to be interviewed, he did not discourage others from doing so. Lowenstein was thus able to gain the personal perspectives and opinions of those closest to Buffett—family members, friends, and colleagues, in order to give the reader a relatively comprehensive picture of both the public and the private "oracle of Omaha." The objectivity, however, is a bit opaque. Lowenstein is obviously a fan, and this is clearly apparent throughout the work. Nevertheless, the portrait of Warren Buffett and his truly remarkable accomplishments unfold with such clarity and detail that the reader cannot help but share the author's admiration for the man who "shunned the game" of Wall Street and practiced instead patience, discipline, and rationality. Warren Buffett is a unique phenomenon and a hero to his shareholders, and it is this perspective that Lowenstein successfully gives.

Tone

The reading of this book is not for the "faint of heart" in economics. It is filled with facts and analyses of investing and the stock market that can be difficult to grasp if one does not have a relatively sound basic understanding. In this respect, the tone is often academic and thus difficult, requiring re-reading of entire sections, in order to grasp exactly what specific financial and investment maneuvers actually involved (for example, LBOs). Fortunately, however, Lowenstein provides significant relief, as he switches to Buffett's own simplification and lay-friendly explanations of Wall Street activity and of investment in general. As well, the blend of Buffett's personal life and his mid-western personality provide the rather constant motivation to read on, if only to root for the Nebraskan who defies the "big boys" and becomes richer than them. The work is thus academic, objective, subjective, certainly partisan, and wonderfully insightful all at once. Buffett is obviously an American hero to the author, and this subjectivity is apparent throughout the work. Even as Buffett became the subject of investigations and law suits, the opposing sides were not presented as viable, and Buffett's essential integrity was clearly promoted. Though the average reader may see Buffett as somewhat a "tragic" figure in his personal life (his wife moved out and his children clearly characterize him as undemonstrative), it becomes clear that Buffett is satisfied with himself, has compartmentalized his life comfortably, and the tone remains upbeat and optimistic.

Structure

Lowenstein has divided the book into twenty-three chapters, each with an enticing title. The first few chapters are wholly chronological, in order to give the reader a thorough picture of Buffett as he moved from a childhood of fascination with numbers and money-making projects, to a college student who claimed to know more than his professors about the business of investment, to a graduate student who suddenly grasped the connection between his instinctive beliefs and his mentor Benjamin Graham. The remainder of the chapters, because of the focus on specific concepts, companies, and strategies, lose chronology in favor of a more thematic approach and long-term professional and personal journeys. The final three chapters return to chronology, however, as a detailed time line of the Salomon Brothers crisis unfolds and resolves and the author sums up the Warren Buffett of the first half of the 1990's. Lowenstein has done an excellent job of moving back and forth in time without confusing the reader, a difficult task indeed. The effect of his approach, indeed, allows the reader to track the complete process of each of the major investment decisions and to analyze each in terms of its relationship to Buffett's basic investment axioms, as well as to understand the complexities of his personality.

Quotes

Partly, Buffett was just tight, but he genuinely did not think people or organizations (or his kids) benefited from easy cash. He measured social projects through the same lens as business ventures: he wanted a return. Good works required that one proceed on the basis of trial and error, even on faith. Buffett was incapable of such a leap. Indeed, the very discipline that made him a good investor crippled what could have been a powerful inclination to work for societal changes. He needed a yardstick. "In investment you can measure results,'"he admitted to a reporter. "With some of this other stuff, you don't know in the end whether you've won or lost." (p. 144)

This ability of Buffett to cut through the clutter suggests a certain genius. Buffett focused so exquisitely on his object, and his simplicity was a counterpart to that genius. He recognized that layers of added executives—though each might be bright, earnest, well-intentioned, etc.—would blur his focus...He did not like protracted decision-making or drawn-out and contentious bargaining. His negotiating style was to seek or propose offers on a take-it-or-leave-it basis. And once he made a decision he did not reverse it. (p. 286)

Instinctively, he shrank from confronting his adversaries, but he was superb at winning them over without a fight. He did not so much convince; he disarmed, he co-opted. Though fearful of hostility, he knew what many are slow to learn—that a sustained demonstration of good faith is apt to be returned in kind, if it is not undermined by any conflicting behavior. (p. 392)

In the annals of investing, Warren Buffett stands alone. Starting from scratch, simply by picking stocks and companies for investment, Buffett amassed one of the epochal fortunes of the twentieth century. Over a period of four decades...Buffett outperformed the stock market, by a stunning margin and without taking undue risks or suffering a single losing year. This is a feat that market savants, Main Street brokers, and academic scholars had long proclaimed to be impossible. (p. xiii)

What was most unusual about the young salesman (Buffett) was his appetite for research. Searching for ideas, he read the heavy purple-bound Moody's manuals page for page with the zest of a small boy reading comics. And he found small gems—unwanted and very cheap cigar butts such as Kansas City Life, Genesee Valley Gas, and Western Insurance Securities, all trading at three time earnings or less. It seemed too good to be true; if the stocks were so cheap, Buffett figured, somebody out to be buying them. But slowly, it dawned on him. The somebody was him. Nobody was going to tell you that Western Insurance was a steal; you had to get there on your own. (p. 49)

Buffett avoided trying to forecast the stock market, and most assuredly avoided buying or selling stocks based on people's opinions of them. Rather, he tried to analyze the long-term business prospects of individual companies. This owed to his bias for logical reasoning. One could "predict" the market trend, a one could predict which way a bird would fly when it left the tree. But that was guesswork—not analysis. If he ever sold

stocks "just because some astrologer thinks the quotations may go lower," he warned, they would all be in trouble. (pp. 97-98)

His main contribution (to the Washington Post) had been earned. Buffett gave the Grahams a way of thinking about the business that was oriented to the shareholders, and at a time when media companies were devoted to acquiring empires. He insistently reminded them—as he had Ken Chace, so many years earlier, outside the textile mill—that size was not the goal; the return to shareholders was. Opportunities were missed, but he saved the Post from the business error that is truly a tragic error—throwing the profits from a good business into a bad one. (p. 193)

This suggests Buffett's most pervasive theme, which was the proper relationship between corporate managers and shareholders, i.e., between the stewards of capital and its owners. In his view, the managers of other people's money bore a heavy burden, which he demonstrated in 1980, when a change in federal law forced Berkshire to divest the Rockford Bank into a separate company. Buffett calculated that the bank was worth 4 per cent of Berkshire; then he allowed each shareholder to choose between keeping his or her proportional stake in Berkshire and the bank, or to take more of one and less of the other, depending on which slice (bank or Berkshire) a holder might prefer. The only one who did not get a choice was Buffett; he would take whatever shares were left. The principle was that he who cut the cake should be happy with the last slice. (pp. 239-40)

Buy-and-hold did have a financial logic, but at Buffett's extreme it can only be seen, as he put it, as a "quirk" of character, appealing for "a mixture of personal and financial considerations." He liked to keep things—stocks, "pals," anything that lent a sense of permanence...Any other investor would have deemed that Buffett was the crazy one. But Buffett had always craved, and had always felt enriched by continuity: to work with the same people, to own the same stocks, to be in the same businesses. Hanging on was a metaphor for his life. (p. 272)

Buffett's record also posed a challenge, for it was the inconvenient fact that failed to follow the form. Buffett would taunt the scholars with the evidence of his career, and implicit in his taunts was a simple question: "If you're so smart, how come I'm so rich?"...Nonetheless, at business schools and economics departments, the Efficient Market Theory acquired the power of sacrament. Its truths were regarded as absolute, whereas competing doctrines were virtually banned. The theory also permeated Wall Street, as well as the investing culture as received in financial talk shows and advice columns. It is, indeed, the intellectual basis for the eggs-in-a-thousand-baskets approach of extreme "diversification," which is the prevailing bias of most investors today. (p. 307)

Topics for Discussion

Warren Buffett committed himself to companies "forever." In today's economic picture, is this still a wise course of action? Why or why not?

Given the collapse of Enron and, more recently, Bears-Stearns, how might an investor have foreseen these crises, using Buffett's approach to investment?

Computerized "day trading" is a recent phenomenon. Discuss the probable comments Buffett might make about this activity and those involved in on-line investing.

If you were Warren Buffett, how would your personal last will and testament read?

Discuss the pros and cons of Buffett's parenting philosophy. Comment specifically on his approach to making his children "independent" and to his beliefs about leaving inheritance to them.

Buffett's pet causes in the 1980's were disarmament and population control. What might they be today and why?

Buffett always advised that one should never invest in a business whose activity he does not truly understand completely, and he followed this "rule" explicitly. Given the complexities and highly scientific/technological nature of some of America's largest corporations, do you believe that this principal still applies today? If not, support your position. If so, what must you do to "understand" the "incomprehensible?"