Mohnish Pabrai's Q&A Session at Nairobi with EO Kenya on October 8, 2022

The contents of this transcript are for educational and entertainment purposes only, and do not purport to be, and are not intended to be, financial, legal, accounting, tax, or investment advice. Investments or strategies that are discussed may not be suitable for you, do not take into account your particular investment objectives, financial situation or needs and are not intended to provide investment advice or recommendations appropriate for you. Before making any investment or trade, consider whether it is suitable for you and consider seeking advice from your own financial or investment adviser.

Mohnish: I think the format is, a little bit of a monologue by me, then Kavan and I are going to have a little bit of chat, then we can open up for questions. I think the second and third parts are more interesting for me. Buffett has a saying, "I'm a better businessman because I'm an investor and I'm a better investor because I'm a businessman". Basically, there's a lot of cross-pollination between running a business and making investments. If you're really good at making investments, it's going to give you some leg up in terms of the operations of a business. If you are very good at operating a business, it's going to give your leg up on investing. It's good to understand the other side. I heard about Warren Buffett accidentally for the first time about 28 years ago in 94. There were two or a few things that really stood out for me when I heard about him at that time. One was, I was lucky, because that time, the first couple of biographies had come out on him. When I read up on him and the books, and letters, I concluded that if there was such a thing as the laws of investing, Buffett, Graham and Munger had put them down. They were not really flexible. They were almost like the laws of physics; the kind of gravity works one way and at that time I didn't know there was a fund industry. I wasn't in the Russian business at all, but I was aware of the mutual fund industry. I noticed that the mutual fund industry in the US did not follow, what I would call, Buffett's laws of investing. They were doing something completely different, and their results reflected the fact that they were not following the laws. Most of them underperformed the index and for example, in one of Buffett's kind of core indexes you make very few bets, their big bets and the infrequent bets, the typical mutual fund would have hundreds of positions. The turnover rates are like 80 to a hundred percent a year. They're cycling through these investments almost every year. They don't really think of them as fractional ownership of business. I had a notion at that time. I didn't know much about investing but who followed Buffett's approach that he should be doing better than the professionals. Because, here, the professionals are not following this kind of the laws. I started to apply his approach to investing in 94 with my own money. Then about five years later, I had a few investors who wanted me to manage money for them and then Pabrai Investment Funds got started and I got going from there. The thing that most interested me is, I was running an IT firm before starting for Pabrai Investment Funds. When you're running a business, you would spend maybe two or 3% of your time figuring out the strategy and direction of the business. Then maybe something like 97% of the time is all the blocking and

tackling to make it happen, all the execution. I always enjoyed the 3% more than the 97%. The 97% was fine, but the 3% was really where I enjoyed it. One of the things that struck me when I heard about Buffett for the first time was that he had converted the 3% to 80%. Basically, what happens is that the part of your brain that you use as an entrepreneur for that 3% of the time is the same part of your brain review the investor almost all of the time. I said, okay, this is great. You can make strategy and direction the whole thing which was very appealing to me. Let somebody else do the heavy lifting. But I'll switch gears a bit. The topic today is “compounding, the eighth wonder of the world” and it's actually a quote by Einstein. I'll just give you a story that Buffett used to tell his investors in the 1950s. In 1626, a Dutch guy, Peter, was authorized by the Dutch settlers who are coming into what we now know as New York and Manhattan to buy the island of Manhattan, the Native Indians in that area. A deal was struck on the island and at that time it was undeveloped land, a great harbor and great geography to sell it to the Dutch for $24. When people hear that the Indians got paid $24 for Manhattan which is so valuable, but let's say the American Indians had a chief investment officer and they told their chief investment officer that for the benefit of the price, we don't need the $24 invested for the price, because we don't need it for centuries. Let's assume that the trust officer made a 7% return. There is something known as the rule of 72. Some of you may be familiar with this. Just show me your hands, how many of you are familiar with the rule of 72? We have a few hands, good. The rule of 72 is a thought to understand how long it would take something to double. It's not precise, but it gives you a very quick shorthand of. If I am compounding at 7% a year if I use the rule of 72. I would just say those 72 divides by 7 which is approximately 10 years for anything compounding at 7% to double. If in 1626, they had $24 compounding at 7%, in 1636, they would've $48 and 1646 they would've $96 and so on. You just keep doubling. Now if you take a hundred-year period which is 10-year periods, right? You're doubling every 10 years, that's 2 to the power of 10, right? 2 to the power 10 is 1024. 2 to the power of 4 is 16 and 5 is 32, 64 and it keeps going to about 1000 to the maximum. In hundred years, at 7%, you would have a thousand X. 1626 is $24, 1726 is $24,000, 1826 is $24 million and 1926 is $24 billion and 2026 is $24 trillion. Now we are not in 2026, we are only in 2022. It is four years off, it might be 10X, it might be like 5 or 6X. The $24 trillion, if you go back 10 years is $12 trillion. Then instead of multiplying the 10, you can say it's like $18 trillion or something, 18 to $20 trillion. If the Indians had compounded at 7% for these four centuries, they would have $24 trillion. What's the island of Manhattan worth today? That's the comparison introducing whether they were taken or not. If we look at the entire wealth of the planet, all the money with every man, woman, and child of the planet, it is about $500 trillion. The US portion of that is about $130 trillion or so. It is very unlikely that undeveloped land in Manhattan is 20% of that because there's so much of the US. In fact, look at what land prices are in Manhattan now and look at the square footage, it comes to about, well under a trillion, $200 billion you could buy all the land in Manhattan. Clearly, the Indians got a great deal, right? The problem they had was, they had a stupid investment officer who couldn't even

compound at 7%. The interesting thing about compounding is and it's really important I think when you're running a business or you're making investments to be able to do this in your head, and the rule of 72 makes it easy to do in your head. Let's say the deal was done a hundred years before, 1526 and we have the same 7% compounding. We would end up with the same result. It's 2400 cents. If the deal was done in 1526 at 2.40 cents, we would still end up with the same end number, right? If you go back to 1516, 10 years back or like 1510 would get down to 1 cent. The 1 cent would become $12 trillion. The reason why Einstein called it the 8th wonder of world is that you could start with an extremely small sum and you could also have a compounding rate that is not high. 7% is not that high, not in Kenya. In Kenya, your bank is paying you more than that, right? You still end up with an extraordinary sum. If you think about it, there are three variables, right? There is the length of the runway that would be the starting amount and there is the annualized component rate. If your starting amount is small, but your length of the runway is large or if your compounding rate is high, the combination of those three, especially over long periods, can do some magical things. If you ask Warren Buffett, some genie comes to you and you can have any one wish you want, he says, “look, I only want one wish, and that is when they look at my corpse, they should say, man, he was old”. He doesn't want to live long because he likes all of us, okay? He doesn't have any particular love for humanity that I'm aware of. He wants to live as long as possible to extend that runway as fast as long as possible. Buffett bought his first stock when he was 11 years old, and he says in his own words that he was wasting his time before then. I think by the time he was 16 or 17, he had figured out compounding and all of this and he had told his wife that. I think he got married in the early twenties, probably in the early thirties there would be millionaires and there would be multi-millionaires many years after that, which she didn't particularly care about. I want to just give you another story about compounding just to, which is maybe a little bit more real than the Indians. My younger daughter went to NYU, and she used to come home late at night and take flights back to California, I'd pick her up sometimes one or two in the morning and we are driving, maybe an hour’s drive home or something from LAX and I would say, okay, this is a good time for some lessons in compounding. Just before she started NYU, she had done an internship and she had made about $5,000 and really had no expenses and stuff. She had saved $5,000. I asked her, I said, okay, there's $5,000 and you're 18 years old. If you were able to get a 15% return on this money and the rule of 72, what would happen to it in five years? If you took 72 divided by 15, it's approximately 5. 15% of the money would double every five years. I said, when you're 23, she said, yeah, it will be $10,000. Then I said at 28 it'll be $20,000. What would it be at the age of 68? You will realize it. Pick all these numbers to make the math easy for me. From 18 to 68, it is 50 and it is 10 doubles, right? We got ten five-year periods. As you'll understand by the end of this talk, or maybe much sooner than that, life is all about doubles and how many doubles we can pound into the runway. This is 10 doubles, right? 10 doubles we already know is magically 1000. The $5,000 would become $5 million right? But I said you haven't even started college yet.

At 19 you will do another internship and instead of $5,000, maybe you'll make $6,000. If you think about the compounding, like at 18 if it's $5,000 and you go a year forward, it's $5,750. It is the exact same number. If she saves $5750 at 19 up to 68, it would again be $5 million. If you take the $5,750 and add 15% to that, about $900 at 20, and again go to 68, that's another $5 million. If you were to keep doing this for 10 years, from 18 to 28 for example, saving this amount. that would basically become like $50 million, right? By now she's wide awake. she's no longer asleep, wide awake. I said, obviously you're not going to stop saving at 28. You're like just hitting your stride in your career and now you're making like $400,000 a year or something hopefully. Then saving rate might be like $30,000 or hopefully maybe $50,000 a year or more. You can keep going. Now, if you look at that math, its 15% is relatively high in terms of a rate of compounding, but the runway is within our lifetime, right? 50 years is within our lifetime. That's why I'm more excited to speak to EO than YPO. I cannot do anything for them. Over the hill *runway khatam ho gaya hai, Ramayan khatam ho gayi, ab puchh rahe ho Ram kaun hai!* That's a lost cause. That's just for entertainment, but you guys, there's a chance. You are not 18, I actually feel that rule of 72 should be in the high school curriculum, the thing is that I was taught probabilities, compounding, and all these things in school, but not in the context of money, which is stupid. What's the point of learning compounding without learning money like you do link those two together? I always hope that the high schools change so that we can get the engine going earlier because in the early years it becomes really hard to make up the lost year. I think the reason Buffett became the wealthiest guy was because he was doing a lot of different jobs and many different things whatever he had, by the time he was 18, he had saved more than $10,000, which in today's money, would be probably close to $120,000. He was at 18-year-old and about $10,000. Then he kept compounding that from there and of course, he even started a fund and now he is getting more, and it's a lot of people's money and he just kept pouring there, the compounding lesson is important. The lesson correlates them to being running a business. All of you actually have a significant head start on any MBA or any fund analyst or something because they have no amount to pay, they have never run a business. Buffett says that "talking to somebody about business or investment who never run a business before is like talking to a fish and trying to explain to the fish what it is like to walk on land". You can spend 1000 years talking to a fish about what it is to walk on land, and it would not be equal to even five minutes of actually walking on that, right? It's a huge advantage if you have run a business before. One of the things about investing is that you simply need a spreadsheet, you should have a spreadsheet for investing because when you run your businesses, you don't run it through a spreadsheet. If we look at this business, Spring Valley Coffee, which I just want to have a 5% stake, speaking to 5% staking, yeah. Anyway, that's all I want. Spring Valley Coffee, he doesn't run it through spreadsheets, okay? There are three or four variables in his head about what would make the business grow and thrive. For an investor to do well, and invest in a business like Spring Valley, they would need to hone in on those safe variables. They would need to

understand what are the three, or four variables that he's focused on. They would first need to hone in on those save variables and then they'd have to assess, well what are the probabilities that these things will come to pass in the manner that he is thinking they might come to pass. None of that had anything to do with the spreadsheet, right? He was just talking about what he bought, that very high-end coffee, 120 kilos or whatever else and such. It's a very different game. That's what you have to get to. But with that, I think what we'll do is we'll go to Kavan and see where he wants to take this.

Kavan: Sir thank you very much for compounding and the introduction to compounding. From here what we like to do today is get into the mind of Mohnish to ask things as I call it, beyond YouTube, right? The big question is for us to know how to invest outside of our business and it may be easy to buy a stock today. But it's not simple. Maybe you can talk a bit about why buying a stock is complicated. What is complicated about buying a stock?

Mohnish: Let me take a step back on that. Investing is a little bit of a strange business where the small retail investor has a huge advantage over a large institutional investor. The large institutional investor has a lot of resources, a lot of capital and lots of options where to invest. But the small investor has a big advantage. The first advantage is that the more money you need to put to work, the smaller the universe of possible options. If I am the Abu Dhabi investment authority and I've got several hundred billion to invest, I can't do $2 million at a time, I have to do billions at a time. Spring Valley is close to them, they can't invest in Spring Valley, they are fit. The smaller the size, the greater the advantage for investors because your universe is larger. The second is that most institutions and most professional investors lag the index. The simple math is that if you invest in the index, the frictional cost is very low. If you are a professional investor or mutual fund or whatever else, and you're charging fees, you have to overcome those fees, and the reality is, when you look at the empirical data, most professional investors after fees are below the index. My suggestion would be either starting point is you look at something like the S&P 500, it's 9% return over more than a hundred years. The odds that it gives you something like 8 or 9% or 10% over the next 20, 30, 40, 50 years is quite high. It requires no knowledge, it requires no research, set it and forget it. I would say that the starting point should be an index more important than indexing so target them the runway is really important, right and we saw that. You need to give as much runway as possible. The savings rate is important. How much are you saving to spend less than you earn and then consistently put away. Now when I give people this answer, they find me very boring, this guys' a very boring guy. *Index lekar kya karenge?* There's no excitement in buying Index. But we are looking to compound, not looking for excitement. The second piece is if you want to buy a particular stock or a particular business, I think then it is like significantly more complicated. The first question that would come up is, is the business within your circle of competence? It's the very first question to ask, when you look at a company. Sometimes I would go to my health club in California. This

guy, the next-door locker is saying to me, what do you think about Apple? Should I buy Apple? I say to the guy, what is the market capital of Apple? He has no idea; he said the stock price is like 150. I said, “I didn’t ask you to stock price, I asked you the market cap”. “Why is that relevant?” I said, “Market capital is what you can buy the whole company for, right? That's the value of the entire business. If you're going to buy a business, you should at least know what you buy the whole business for. Knowing the price of a share does not tell you anything”. Apple has a market cap, I don't know if it might have changed recently, but $2.4 trillion. Let's say its $2.4 trillion and then you are saying, should I buy Apple? The second question would be that if your family had a fortune of let's say 10 trillion questions what you should ask yourself is, “would I be willing to put one-fourth of that fortune into Apple?” Then the question that would come up after that would be, “is that okay?” I'm paying $2.4 trillion for Apple. I don’t know what the numbers are, let's say it’s maybe $120 billion. The multiple is 20 times. If there was a business available for a million dollar and gas station, petrol pump or something available to $s1 million and every year it is going to earn $50,000, maybe the earnings are going up 5% a year. The question you will ask yourself is, “if my family has $5 million, would I want to put a million dollars into a business that makes $50,000?” and the sort of question you need to ask yourself is, okay, I know Apple is maybe on the gas stations making 50,000 a year. What would it be making five years from now? What would it be doing 10 years from now? At what point might the business go into a decline? At some point, you might have declined, what happens then? What's real estate work? So on and so forth. If you can answer these questions well, it gets to a no brainer. Now the thing is, for 20 times earnings, I can't get out of bed. It's too expensive, things too expensive with a low growth rate. But let's say there was a gas station which is available for a million dollars and it's making $400,000 a year. Okay, *kuch zyada sochne ki zarurat nahi hai.* Would you do the deal? Center of town, $200,000? I think in investing, what happens is that especially in the stock market, because these are auction driven markets and pricing is set by few buyers and sellers, you can get very wide variations in price. If I were to look at all the stocks in the New York stock exchange and there like on a dark board and I push through a dark at any stock in the New York stock exchange and I looked at the 52 weeks range on that stock, it might be like $60 to a $100 or $55 to $110. The range is pretty wide, right? It's like almost in one year it's fluctuating almost 50% or doubling in a year or whatever. But if I look at, for example, the price of a particular home in Nairobi and I have a real estate agent who is a friend of mine and I call the person every day and say, Hey, what's this home worth today? He says, oh, it's worth $300,000. Is that okay? Then you call him the next day. What's it worth today? He said $300,000 and you call him the third day he says, it’s still 300,000. But he's a friend of yours. He entertains your calls every day. Then one day he'll tell you it's $301,000. You say hey that’s great, okay, you write down 300, plot out every day with the prices you’ll get a one year rate, $300 to $310,000, something like that. $300 to $320,000. You're not going to get $300 to $500,000, right? That's not going to happen unless something weird is going on. But in the stock

market, a normal year, if nothing weird going on, it's 60 to 100, right? If the same thing was a private business, if I look at a private business and a private investor was coming to buy it, the price will not change. The negotiated transaction between an intelligent buyer and an intelligent seller will tend to lead, under normal circumstances, to a rational price unless there's some distress or something else going on. The seller is desperate or the buyer has too much cash or whatever else. But normally, you get a rational price discovery. But in the stock market, because we have this auction driven mechanism, much wider ranges, and when you get much wider ranges, it lends itself to the possibilities of all the investment returns, if you can get it right. With that, you might go with your next question.

Kavan: Absolutely. Is it more complicated if you buy a stock?

Mohnish: Buying a stock is not complicated; it is the selling that counts, and I think a great investor said if the job is done right. Basically, what you really ought to be looking for is businesses that have characteristics that you could own it for decades and that's all you are looking for, you will be able to look for great businesses hopefully there are times when they're temporarily off and then you can take it from there.

Kavan: Excellent. Circle of competence; I think the question is how you enhance your circle of competence in your case as you are studying, researching every year for anyone, how could you enhance the circle of competence?

Mohnish: One of the key issues of competence is, you can do really well as an investor with an extremely small circle of competence. The most important thing is staying inside the circle and understanding the whole, the size of the circle is not important. I would say, even an effort to expand the circle is misdirected. The circle will actually expand by itself over time because you could see the gain and learn different things. By more people, with time, it'll expand, but that should be the case. In investing, it's better to be an inch wide and a mile deep, than a mile wide than an inch deep. You really want to have the knowledge and there's a friend of Charlie Munger who just passed away last year, Rick Guerin, he is a multi-millionaire, and all he had invested in Stanford university he lived two miles radius within the campus. Mostly, he bought some apartments and so on, but he never ventured outside of a two miles radius of Stanford. He was extremely narrowed, it's not even California University, it’s not even real estate, it’s not even Southern California, it's only the narrowed area. But the thing is that because he understood like he just walked off into the building, he could tell you everything about the buildings. He would rent that, and he built and what the economics are, what you buy for everything. What he was really good at until it got distressed because he was always under leveled, he was able to buy up a lot of stuff and when things went very euphoric, he was able to sell off things at premium prices and over decades and ends up being really wealthy. Don't worry too much about expanding the circle, expand by size.

Kavan: All right. With that circle of competence you have, you get a bunch of ideas being turned into all the time. How do you evaluate any idea coming your way, you heard of something good or not? What methodology do you sort of apply?

Mohnish: Yeah. What I do is, I have an absolute number in my head, usually I'm not interested in something where I can't get my money back in two or three years. Usually, I'm looking for something where it can be a double in 2, 3, 4 years, but not more than that probably 4 years. Then most things that show up on my radar, there are just two questions that run through my head very quickly. The first question is it in the circle of competence, which blows up probably 90%, 95% of stuff. The second is the needs on the board. Can we actually get what exactly would make me get a great return on this investment? It should be relatively quick and obvious, right? If I look at a $120 billion, 5, 10% a year or something, and one of the concerns I would have, I don't know what will happen in 10 years, but I would've concern over Apple of 20 or 30 years? For 10 years I can't see anything happening, but in that 20, 30 years I don't know. When you look at something withal, it's not often. The 40,000 of assets look more exciting.

Kavan: Okay. With those few ideas that come across the desk that hit the circle and you're like, I can get my money back, the undervalued asset, talk about concentration. A lot of us here need to diversify. From food companies into other things or from real estate that could be to other things. Concentration versus diversification, what is your view on that? Should we buy three or four things and be happy with them if they're compounders, or do you think a lot of variety?

Mohnish: I think the too much we do is, in US you call it a personal financial statement. The bank will want that when you apply for a loan or something. Most of you, I would say that the most significant asset might be the value of the business and the second most important thing might be if you hone something, then you have more savings than everything else going on but probably more than both of those is the future earnings that you'll have between now and when you stop working. Look at the earning potential over the next 30 years. That's a significant number, right? Then you have the value for business today and that might go up over time. You stated that you understood, and that you can do well good investment ideas are still there. I would say that if you had a business, let's say a million or 3 million you early next, if you have a portfolio of a $100,000 or $200,000 or something like that, it has four, five first when you look at the whole equation of everything you have, most of the money stock in your future earnings, I would say add 30 stocks there, and maybe two. Something seven or something might be good.

Kavan: Similar to what you said, maybe theoretically spend a quarter of your wealth for. That sort of in is your portfolio widely, you try and concentrate on a few.

Mohnish: If I look at my personal holdings four or five stocks would be most of it. I would say if I looked at the funds, the funds typically make 10% bets. By the time we get to 4th or 5th position, 60, and 70% of an asset. Pretty concentrated.

Kavan: Okay. Concentrated. You introduce the word bets. A lot of investing sounds like it is making bets, but not from a gambling perspective. But common ones are high risk high reward and low risk low reward. Is there medium that is low risk, high return you can think about?

Mohnish: How many here are from Gujarat? We want low risk and higher returns like all the Gujaratis which is also known as Dhandho. Basically, we want that cake and eat it too.

Kavan: Yeah. Does that work? Is that a question of being patient enough so that you find exactly that sweet spot.

Mohnish: Yeah. I think the thing is that the good news with option-driven market is that they vacillate between fear and greed all the time. I told you, you throw darts, and you see this wide range. At any given time, most of the market undervalue them, hardly any stock would be fairly valued. They would be on one end or the other end for one reason or the other. Our focus is on the end, which is undervalued, which we can understand, where we see great prospects in the future. You may have a particular insight into a particular business or an industry that the market doesn't particularly care about. That can lead to some exciting return. Three years ago, I made an investment in a company in Turkey, which is the largest warehouse operator in Turkey. They have about 12 million square feet, about 20% of that is refrigerated. These are 99% inflation index leases, tenure leases and Blue chip clients here, Amazon, carpool, they don't have any default or anything going on. The liquidation value of that portfolio was a billion and there was about 200 million of debt, about 90 million. It was worth about 800 million or so. The market cap of the company was 20 million. It was trading at two and a half percent of liquidation value. Did I mention to you that God loves me. In case you don't know, God loves me. I have this friend of mine, a good of mine in Turkey, he is a very good value investor and maybe sometimes he hasn't come and speak to you. I started visiting Turkey two years ago because the inflation was so high that everyone in their brother left the stock market. Turkey is a little unusual in the sense that 80% of the stock market is owned by either insiders or foreigners or institutional investors. That 80% doesn't trade. It's pretty dominant. The other 20%, which is mostly with retail, local investors, cycles every nine days. The entire 20% trades every nine days. We talk to the average, the holding three, four hours. I wonder it sells at 10'o clock and shuts up at 2'o clock. I was talking one time to the head of IR, large Turkish company. The same kind of calls I get from the retail investors is, some guy will call her and say, stocks at 20 liras.

I give you 20 liras today, how much you give tomorrow? She said, "I don't even know how to answer the question. You make a deal like he's buying carpet. You

know how much I can sell back to you tomorrow. I buy it today. I buy a lot of it today". Buffett has a saying that the stock market is a mechanism to transfer wealth from the active to the inactive and this could not be more than true in Turkey. Something that I was going to see my friend who is looking into the companies, and he's giving all these briefing, that I would invest in the company he's already invested, that gives me one filter already done. Someone already actually put their own money in. He was telling me this is a 20 million market. I said is it a fraud? He said, "no I've invested. They seem like honest people and there's no issue". I've never seen any. I met them, I couldn't really sense that I'm dealing with some cooks here. They seem like pretty smart business people. Then I spent the afternoon going and visiting all their warehouses and they're in absolutely prime areas and look great and everything. Then I thought I couldn't get any stock there. Such a small market there. We end up with one third of the company for $7 million. I mentioned that God loves. The founders of the business, they own 40% and my fund owns 33%. Buffett says, "you really understand the business only after you own it". Last two, three years, I actually met with them a few times. Because they have many other businesses, they're the largest freight trade operator, largest truck fleet, largest forklift rental, they're like four businesses.

I didn't even value those businesses. Those are more difficult to value. The warehouses are extremely, more valued, and I will give the liquidation value if I get to intrinsic value that's even higher. Even real estate is depressed. It actually might be worth it in more normal times. Then I discovered that these guys don't just have great assets. They're good capitals. They're just like me. They don't want to invest in the 'get the money back in 2-3 years' I said, good I like my brothers. Basically, that was an unusual market, with a bunch of participants who are not intelligent investors if they have all these things. In investing, when you look at particular stocks, the threshold has to hit you in the head like a 2/4. 2/4 is an American term but like a block of wood or something. Be obvious that this is an incredible deal like the $4,000 gas station. If you don't see something where it's obvious when you need a spreadsheet or something, because there are 50,000 stocks in the world, you can keep looking. I'm ok if I make two investments in a year, it's a good year, and even one is good, but that one a year is good, like Reysas in Turkey and will come along once in a lifetime. I know I'm never going to get that again, no matter how much God loves me.

But I would just say, this's probably for all investors, if you really keep your eyes open, you'll all get that option. I was just reading yesterday on Twitter. Most of you are familiar with Charlie Munger, the Buffett partner. People have asked him many times about his greatest investment mistake. He says the greatest investment mistake was not buying enough of Belridge Oil. Belridge oil was a company in California with, huge oil field producing about 5 million barrels of oil a year. The stockbroker called him and offered him 300 shares of Belridge Oil for under $35,000 at that time. The shares were bought for about 4% of liquidation value. Like Reysas shares in 2019 offered at 2.5% of liquidation value.

Then the next day, the broker called again and said “I have another 1500 shares available at $115”. Now Charlie didn't have cash, he had thirty-five thousand. If he wanted to buy it, he had to sell. He was thinking about it, he told the broker I will call you in 10 minutes and he thought about it, it was uncomfortable. He said, “I'll pass”.

That company in 1974, that was at 115 in 1979, 5 years later it got bought for 30 times that price. I think Chevron or Shell came and bought them. It already had a 15% dividend yield when he bought. It was like 30-35 times with money, and he says, the 1500 share would've been about $175,000. He had the money in other stocks he owned. He said, if I take that back, it cost him about $500, because it would've been about $5 million, the $175,000 will come over $5 million by 1980, 6 years later. At that time, Berkshire Hathaway was $400 and now it's $400,000, you would've had 1000X. He would have put it into Berkshire, so basically that $5 million would have become $5 billion and his total net worth today is less than that. It’s like all of you running businesses you are busy or whatever else, you keep doing that and occasionally something shows up which you think oh, this looks incredible. You then focus on that and go back to any of them.

Kavan: Sir I think the lesson there was to start with unreasonable standards and making your money back in two, two or three years at high returns in your circle of competence. Then have extreme patience as you're waiting for all the salmon to pass by but only the salmon you want. Then extreme decisiveness, which was go for it when it does come. I'll take you to a second part which we're going to talk about the idea of growth engines and tailwinds a little bit. You are evaluating this business; it can make you your money back in two or three years. Talk about the idea of what you call a growth engine. What's a growth engine?

Mohnish: Yeah, the best businesses to invest in businesses that have a very long runway. There's a guy named Chuck Akre. How many of you have heard of Chuck Akre? Oh, we have a Chuck Akre fan in the back. Yeah, I'm actually going to meet Chuck next month in Virginia and has to be fun. He lives in a town in Virginia with one traffic light. I know I won't miss the traffic light. Anyway, Chuck Akre says that his investment philosophy is a three-legged stool over here. He says that first leg of the stool, he wants management with very high integrity, the second leg is the management. The third leg of the stool is he wants a long runway. The gentleman I met at Spring Valley, like I told you that God loves me, brought me to Ritesh to speak. It seems to me Ritesh is very honest, and it seems to me Ritesh is high energy and high integrity. *Abhi mere paas spreadsheet wagerah nahi hai.* It also seems to me that this is a business that has high earnings, Ritesh is not interested in anything without an earning. Everything was there. I was standing in the back and I'm saying is *Chuck Akre kya keh raha hai.* Then I went to Ritesh. Bill Gates has a saying, “even if you're a monopoly, you have to ask for the order”. I went to Ritesh and said, “Ritesh any time in the future, you need money, please call me”. He was actually receptive.

He said, oh I'll get your contact, whatever, and I'll get his contact to make sure he doesn't forget. If you look at Spring Valley now, I don't know what the price is, right? But the thing is that if the runway is long enough and the return on equity is high enough, even an expensive looking price can be okay. Now the thing is that when you look at a business like this, it's not a listed company.

It doesn't have that much history. You have more variance, right? But on the other hand, I would not make a large investment either. He can't even take a large investment, right? It would anyway be size small. If and when Ritesh answers my phone call, *hum dekh lenge*, the thing is that, if the deal is 30 times earnings, or 40 time earning 50 time earning, it may be a good deal. We don't need to always get things at two and a half percent of liquidation value and liquidation, Spring Valley will not be done at that price. I think that's a beautiful thing.

Kavan: Correct. The runway in terms of tailwinds, when you see a tailwind like listing, it is going to pick up naturally over time. Like things that are in its favor.

Mohnish: I would just say that one of the problems with investing is even the best investor will be wrong at least 40 of the time. If I look at Buffett's record, he bought about 90 businesses in the last 50 years out of 90 businesses probably at least 30, 40 of them. Now he doesn't want to talk about that because it will demotivate the managers and all of that. He doesn't want a name. But you can look at those businesses and say these are useless. I've talked to Charlie about it. They made an investment in jewelry and only the first one worked; all the others didn't work. When Buffett invested in banks, he's never missed, it's 100% successful. When he invested in grants, he had a very high error rate. When I look at Buffett's record in grants, he has done really bad. Banks, financial companies and all of these things done really well. Apple has stood as the brand. One of the things you always remember on investing is look at a business and think back and fast forward 10 years, there are factors many that come in. Some are within control and somebody outside the control, and some may end up with businesses having tailwinds that others could take it out. We must have the ability to understand. In Spring Valley, if I must make the bet, I will not put more than 1% of my assets, and I can lose the 1%, it's okay and 1% could grow quite a bit. If our man does his job, then it works okay. Yeah, we must keep in mind the error rate.

Kavan: Okay sir, I think you brought up a good analysis. We all are running the business, somewhat own the business, if our businesses overcame across your desk, and some of them you like great, and some of them you feel like this doesn't fit. How would you convert bad-looking investments into good ones? How would you advise someone to do that?

Mohnish: I think the best lesson on that is a lesson from Berkshire Hathaway. Buffett starting the seed was a terrible business. He took a controlling stake from a textile, couple of textile mills, which were doing from day one. They had very

high energy costs, they had very high labor costs and they were producing a commodity, men's suit liners. Literally before the ride, he realized that he made a mistake. But now he owns a business. What he did was that the manager of the business would come and tell him, we buy this loom, it'll make us more efficient, and will reduce our cost a bit impossible. Buffett will look at it and say everybody else will buy the same loom, everyone else will also reduce their cost. In the end, if you're watching a parade, one guy goes on tippy toes and everyone will on tippy toes, we still can't see to the same place. What he did was he started the business of Capex. He just said basically it was cash flowing. He took that tiny stream of cash that was coming out of the business, and it went into a completely different set of businesses and the businesses it went into. I think it's really easy for you to tell whether you have a high ROE or low ROE business. You can just look at your income statement and balance sheet, what your book value is and what your earnings are and what the bank can pay you for your money. It's relatively easy to tell whether the business is a high return equity business or not. Obviously, with the history you have in the business, you can also tell whether there's a growth engine, and what kind of growth engine there is, right? If the business does not have a high return on capital, that should be a red flag to avoid putting more capital into the business. I would say that if I were in a situation like that, I would want to sustain and run the business, but I would not want to keep putting the earnings back in because you're going to keep getting low returns. I would look to see what my alternatives are. Everything is about opportunity cost. Basically, one of the things I found very funny is that in 94, I heard about Buffett for the first time. I had sold a portion of my IT firm and after taxes everything, I had a million dollars. First time ever, I had money, and my business started with credit cards and so on. The business did not need the million. It was the first time I had money in the bank. I heard about Buffett, I said, okay, I can invest, and I want to see what happens. I want to see if I can do better than from 94 to 2000. The million became 13 million, it compounded by more than 70% a year.

I know that at that time that the market was slowing down with IT. I was just looking at my firm. My IT firm had 170 people. It was a high business because we didn't have much in terms of capital assets. But the annual earnings I had from me doing part-time work on my portfolio exceeded what the company was earning with 170 people. I just said, okay. I spent my whole day at this firm and there are 170 other people who spend their whole day at the firm. At the end of the day, this other hobby on the side is doing better. I was actually losing interest, probably moving interest for a good reason in the IT business. Eventually, my YPO forum helped me, and I broadened my CEO and then eventually patrol and so on. Then I accidentally ended up in the fund management business, the fund managers, and the thing is in Pabrai Investment Funds, I don't think it took even a thousand dollars of capital to get going. There have been millions business. I think that nature capitalism is that we don't get paid for the degree of difficulty. We are very hard to run, very hard to manage and have a very low return on equity and very low growth. There are

other businesses that are extremely easy to run and manage and have very high returns in equity and are like a license to print money. That's the nature of capitalism. I think what we want to try to do when you are an entrepreneur is yeah, you can easily run this lens through your own business and when you look at other opportunities that show up on your radar, you can evaluate those opportunities relative to what the alternatives are. I think it's a really good exercise to go through, like I said, a better business plan. I'm a better business plan because I'm investor a better investor, I'm a business plan. It can really be helpful to do that.

Kavan: I think we're away that we're sort of a universal model in your business in other companies and that's a good way to just measured.

Mohnish: One of the things that Chuck Akre mentions is, high returns on equity without leverage in a lot of businesses do well and what you really want is a business that delivers those high returns with almost no leverage. That's the trademark of a great business.

Kavan: Okay. Coming to Pabrai Investment Funds now, we take that you do the parts and blocks and all of that, what's your advice on a CEO or on the management team of that business? How do you interact with the CEOs of the various investments, ones that you are active in and what would you advise them to focus on? What should their role be? Is it capital allocation? Is it a strategy? Is it making sure the operations keep running? What would your advice be?

Mohnish: Yeah. Actually, we are not in any way activists, so whatever happens in the future, what I'm really more interested in is what has happened in the past that is, and the past gives me a good sense of the nature and competence and abilities of management. From that, I can make some extrapolations of what may happen in the future. Like what I found in the business in Turkey is that they have a very strong belief in high return projects. I think that's just part. They also are creative, they're willing to enter new businesses, but they'll start small and they kind experiment and once they feel confident, then they'll start increasing the capital, which is also really good. My take is, yeah, they'll make some mistakes, and they'll learn some mistakes if they're following that playbook that looks good. In some cases, management have been open put from us and we don't push it, but we, if I notice things that they could do differently or tweak and let them know, and in some cases, they made those changes. But I think, for the most part, I think when you're making an investment, the clay is set, you're not going, humans cannot change after the age of five, the genetics and profile they set. We are never able to change people, we just have to understand who they are, and basically, who they are, is whom they're going to be forever.

Kavan: Okay, capital allocation, is probably your number one goal. How much does it matter for a CEO and your own business on an annual basis? We all be thinking

the same way that we do have even what we think is, of course, that's good for business you really think about capital allocation more actively?

Mohnish: It is probably one of the most important jobs you have. I think there are a lot of jobs you have hiring great people, motivating them, building great team, but it doesn't work without strong capital allocation. I think you have to have a very hardnosed view. Amar and I were talking when we were driving over, so he has two businesses as far as I understand, he has probably more than two, but two that I can understand. On one hand, he is a dealer for steel in Kenya, on the other hand, he manufactures office furniture, and distribution. The two businesses are different, right? The capital intensity of the two businesses is different. If he was to look at these two businesses from a capital intensity point of view, they will come out differently in how they are. I don't understand the working capital cycles and all that are better, but that would tend to give you some indication about where to step on the accelerator and where to step on the brake, right? Because they may also have very different curves in terms of growth, but that's even in the same business you have, you may have multiple lines and products and stuff that they have very different economics and growth engines and so all of that. You have to look at it carefully and you have to understand which ones. I'll give you an example. When I was making these investments in the mid-nineties, I was in the IT business and software. I understood tech and software well. A lot of my investments at that time were in that industry. What I was finding is that I would find some software companies where the PE ratios high, like 60 times, 70 times earnings and they were growing fast. The market was recognizing that these were good businesses, and they were giving them very high valuation.

I liked the businesses a lot, but I said, I can't really invest at these multiples because I don't know what the terms are going to be. I remember there was a business called PeopleSoft, which was doing human resource software for large companies and PeopleSoft required a lot of custom programming and configuration. Each time they sold a license, they needed a bunch of consultants to go and make it work. The consulting revenue streams and people were significant. What I did was I said okay, I can't invest in PeopleSoft, it's too expensive to buy. But what I did in my own business, I said I'll set up a PeopleSoft practice, okay? Because I just said if a PE is 70 and the market mostly gets it correct, it's growing really fast, right? I didn't even know how to spell PeopleSoft, right? How do I, like as a person, layman suddenly profess to have expertise? I said, let's do this. We'll place an ad for a PeopleSoft practice director; some senior guy into a company can build this thing. For me to hire PeopleSoft director, it would've cost me, at that time, about $300,000 a year to bring in this senior person, right? I placed an ad, and I got a guy, Paul Gates, whom we hired, and I think we hired him for $270,000 or something and he was going to start in three weeks. My only expense so far had been a few hundred dollars in the ad and maybe $1 for the letterhead for his offer. Paul is supposed to start in three weeks and he's going to start burning you through

your firm running the same project. They don't want me to leave. I said, “Paul, what are they paying?” He said, “they're paying $550 an hour”. I said,” Paul, tell them yes”. My revenue was going to be $1.1 million on him. My cost is less than $300,000 or something. He's going to start there on the first day. Okay, I said, “Well done Mohnish, better than buying the stock. I didn't even put in money out. The total expense was less, you look at the stock market, you look at the highest speed software company, then you go, no need to buy the stock”. At that point, I was looking at the ROEs and all that is giving calculations. It was like so far; all the charts and it worked so well. It's great. I think that yeah if you have a good investment mind, I think it can be a lot of help on the business side. I wouldn't have understood that PeopleSoft is growing so fast and all of this stuff unless I'd actually looked at their financials and saw how they were, how the market was valuing them, and all of that.

The contents of this transcript are for educational and entertainment purposes only, and do not purport to be, and are not intended to be, financial, legal, accounting, tax, or investment advice. Investments or strategies that are discussed may not be suitable for you, do not take into account your particular investment objectives, financial situation or needs and are not intended to provide investment advice or recommendations appropriate for you. Before making any investment or trade, consider whether it is suitable for you and consider seeking advice from your own financial or investment adviser.