

Mohnish Pabrai's Lecture at Peking University (Guanghua School of Management) on October 14, 2016

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Mohnish: It is a true pleasure and honor to be invited to speak to the students. Obviously, Peking University is amongst the best of the best. I saw a few of the resumes and they look exceptional. We've got lots of horsepower in the room, which is great. Behind me, is a bust of Charlie Munger. Charlie will be overseeing the proceedings for the next couple of hours. In case we go off track, he'll get us right back on track. Anyway, the topic for today is "the quest for ten to hundred baggers".

The term 100 baggers comes from feed or lynch. It means making a hundred times on your investment or making 10 times on your investments. If you say 10 baggers, it's 10 times, a 100 bagger is a hundred times. I haven't given this talk before which is always a lot of fun for me because it's very boring if I must repeat some talk that I've already given before. In some ways you guys are Guinea pigs, but in other ways I think it'll be exciting. Because I have not given the talk before, I'm not exactly sure of the timing but I'm going to try to move this along because there's a lot of material relatively fast. It'll feel like it's going quickly, but that's why we have the recording. Later you can watch it kind of more at your leisure if you want to, or certain parts but also certainly during the Q & A, we can go through things that you have an interest in.

Anyway, I started my journey as a value investor 22 years ago. I quite by accident heard about Warren Buffett for the first time. Unlike you, when I heard about him, I was 30 years old, I was much older. When I read about him, I was stunned. I haven't been to business school. I'm an engineer by training. All of you probably know a lot more about finance than I do. But, I was stunned with Warren Buffett's approach and the way he had been so successful.

The crux of his success, at least what I took away from what I read in 1994 was a quote by Albert Einstein, which is "compounding is the eighth wonder of the world". Even though Einstein was a physicist, he figured out a few things about compounding. Obviously, in 94 when I had read about Buffett, he had been compounding at the rate of about 25, 26% a year. 26% is a magical number. I thought of a magical number then, because if you compound money at 26%, it doubles in exactly three years. If you have a thousand dollars, you compound at 26%, you're going to have \$2,000 in three years and so on. If you go for 30 years that's two to the power of 10. This group doesn't need me to tell you that

2 to the power of 10 is 1024. We throw away the 24, it's a thousand times your money.

If you had a thousand dollars and you compounded at 26%, 30 years later you would have a million dollars. If you had a million dollars and you compounded at 26%, 30 years later, you'd have a billion dollars. That's basically the key to Buffett's success. I thought it was worth trying to do what Buffett did. Of course, no, we are never going to have another Warren Buffett, but I thought it was worth trying to compound at high rates. I gradually, (over five years), switched from being a CEO of an engineering company to eventually being a hedge fund manager.

The key nuance, or you could say mental model I used was very simple, which is, I looked for companies that were selling for half or less than what they were worth in two or three years. If I could find a dollar bill for 50 cents, then what that meant is that if it got valued as a dollar in two years or three years, I would be compounding at 26%. If it happened in two years, it would be even higher. It'd be like 35, 36%, and it happened in two years, it'd be 26%. I said, it's worth trying to see if we can find these 50 cent dollars, because 26% sounds high, but finding things that are half off in an auction driven market. I didn't think it was that hard, and I thought it was worth trying, because the rewards are so high.

That's what I embarked on doing, I said, Okay, let's try to find these dollar bill for 50 cents, and then you just sit back and wait for two years or three years. Markets are weighing machine in the long term, and they'll get reweighted accordingly. For the most part, if I look at my performance from 95 until let's say 2014 it's done about the 26%, approximately. Last two years. I'm down about one third, so it would've taken it down a little bit. But we think in the next few years we'll make it up. We'll see how it goes. I'll report to you next year when I'm with you in person. But this journey, it's been 21 years since I started doing this.

I had a million dollars in 90, 95, and I wanted to try to see if that million in 30 years could convert to a billion. I said, Okay, basically we have the million. I don't need it for anything. I'm going to try to put it in this Buffett engine of compounding, and I want to see what happens to it. The good news is that even if I missed by 90%, it's still a big number. Even if I missed by 95%, it's still a big number. They're all acceptable numbers. It sounded like a good game to play. When I first set up the first set of stocks I bought in 1995, I had one year of experience reading about Buffett. I didn't have a lot of experience. I hadn't gone to business school, et cetera.

I basically used to just, if I found a company, I would make a 10% bet. My portfolio for a million dollars, got divided into ten stocks, okay? I bought these 10 stocks, but then I had an interest at that time in making investments in the Indian market because there were some companies I had noticed in the Indian

stock market that looked very compelling. It was very complicated at that time in 94, 95 to invest in India, especially as a US resident. For example, they didn't have Demat. If you bought shares, this is like 21 years ago, they gave you physical stock certificates. Also the Indian government said that if I brought in dollars and I bought Indian stocks, I'd be able to take the money back without taxes back in dollars.

The country had a lot of exchange controls, so I didn't believe them. I was a little skeptical that a country that had all these exchange controls would kind of honor these things that they were saying, if you will. I was skeptical. What I did is, out of the million dollars, I only allocated \$30,000 to India, and the \$30,000 I allocated to four stocks. I had to physically go to Mumbai. I opened a brokerage account, opened a bank account, and then I bought these stocks. Then a few weeks later, I got these physical stock certificates in California, and they were almost falling apart. Like, they looked like they almost were worthless. They looked so beat up. One stock I bought, which was half of the 30,000; 15,000 was an IT services company.

That was the business I was in, and Satyam computers, and then three others. One was a broker to whom I bought the stocks, and two were courier companies, kind of like FedEx or DHL because India had a very bad postal system. I thought that as the economy grew, these companies were basically doing what the postal system should be doing, but were doing it in private ways like FedEx and DHL and UPS. I thought these were all very long-term plays. When I got these certificates, I said, Okay, I'm going to stick them in my drawer and not look at them for 10 years, just let them be. But what I noticed is after about five years one of the stocks, the IT company, Satyam computers, I had bought it for 45 rupees, and it was trading at 7,000 rupees.

It was up 130 or 140 times what I paid for it. At that point, actually, I'd been tracking a little bit, but in about 1999 which was about four years after I bought, I said, let me just study this business again because I know the business, but this is ridiculous. I noticed that the multiple it was trading at, it was trading at more than a hundred times earnings. It was just a ridiculously low price. One of the reasons it was priced that way is because they had spun off A dotcom Company, which they still owned a piece of, and the market at that time was in a major bubble for all these dotcom. This company, which was just a system integration IT company had spun out a subsidiary that was doing some nifty things on the web.

The market gave that spun-out company a huge valuation. Because of that, this company got a big valuation. Anyway, I thought this was complete bubble territory, and I was also concerned the 15,000, the exchange rate had moved against me. The 15,000 was worth over 1.5 million. I started with a million dollars. I'm going to tell you whether the remaining 985,000 in a second, but 15,000 of the portfolio was sitting at one and a half million. I was concerned whether the Indian government would allow me to take the money back,

whether I could even sell the stocks, whether the shares were fake or real, I had a lot of questions. I said, we're going to test this out. I contacted the broker, I said, I'm ready to sell these shares. I sent them the shares, they sold the shares.

I sold within 5% of the all-time high of that company. They put the money in my Indian bank account. Then the next day, I asked them to wire it to the US and they wired it. Everything went flawless exactly as the government had promised, no issues, okay? I was blown away. I said, Wow, no taxes. I gave them 15,000, five years later, they gave me 1.5 million no questions asked, what a country. Then these other stocks that I had, they were all kind of, you can say old economy stocks. They hadn't done much. The remaining 15,000 maybe was worth 20,000 or 25,000. It had not moved much. In fact, everything else was going down in price at that time, except the frenzy for the dotcom. Even Shire Hathaway hit a multi-year low at that time.

In 2001, I decided to completely exit my Indian positions, and I sold all the remaining three. One of them was down 50%, but the other two, we made a little bit of money, were basically part of the remaining 15,000. I got like 20,000 back or something. The overall result in India obviously was more than acceptable. 30,000 in one and a half million out is perfectly fine. Then the other 970,000 I had, there was one company I had in there, which went up 100 X and I had a hundred thousand dollars. This US Company, CMGI went up a hundred times. That one company became 10 million. Now I had 10 million in that one company. I had one and a half million in this one Indian company. The rest of the portfolio had done okay, because at that time, from 1995 to 2000, the US markets had gone up like 25% a year, so that it had moved up, but nothing like these other companies.

I had 13, 14 million out of the million dollars in five years. I said, Mohnish, forget about 26%. We've just kind of blown it out of the park. Very well done. Good job. I was very happy, it was a fantastic job, especially for never having even attended a single class with the professor at Peking University. Just winging it on my own, if you will. Now recently I went back. What happened is, these other stocks, when I went to sell the other three Indian stocks, they told me one particular stock certificate was fake. It was a very small amount of shares, but they said it was a fake certificate. The broker said, we're not responsible for fake certificate. I didn't care. It was a small amount, and I just kept that one certificate in my desk.

Recently I looked at it again, I said, No, it doesn't look fake to me. I sent it again to a broker in India to sell, and I asked them, Can you sell these hundred shares of this company? Now what had happened is, I had held this one company, Blue Dart, which was like the FedEx of India for 21 years, and I held it for 21 million years by accident, because that one little piece can get sold because of this kind of fake thing. I trace back, because I kept getting these dividend checks all this time and all that, that Blue Dart was ultimately a 60 X. If I had kept those

shares, I'd invested in Blue Dart, I had invested \$7,700, and I would've had about half a million if I'd kept those shares.

Then I went back and said, let me check all the four stocks in India. What happened to the other three if I'd not touched them? Because they were designed to not be touched. I was stupid. I sold it after six years. What ended up happening is that Blue Dart was 60X. There was another one, Kotak Mahindra, which was my broker that was up 50X. The third one which was SkyPack, which was competitive Blue Dart that basically went down to half that didn't do anything. But what ended up happening in that portfolio of 14 stocks in 1995 is, I had four out of the 14 that all eventually went up more than 50 times. In one of them, I had a serious position. I had a 10% position, which completely altered my net worth. I started thinking that this is not good, that I ended up with these companies in my portfolio, and I never recognize how great they were.

I recognize it in two cases. In both cases, I cashed out a hundred X both because of the bubble, not because of valuations went up. They probably should have been worth 10 X or 15 X, but not a hundred x. But we over kind of collected more than we should have, which was fine. But these other ones, these were real businesses like the FedEx of India the, the Goldman Sachs of India, and these were businesses I should not have sold, and I sold them. I started thinking, how often has this happened in my portfolio? How often has it happened where we had these companies where I was smart enough to buy them but not smart enough to hold them?

Why is that happening? Which is the subject of the talk today, is kind of a framework. The best way to learn is to teach. I have to admit that one of the reasons I wanted to do this talk and this lecture is because I'm trying to learn. Whether or not any of you guys learn anything from me, I am definitely going to learn from this talk. Because what I want to do is I'm 52 years old, hopefully I have another 30 or 40 years left, and the next 30 or 40 years, when these hundred baggers show up in my portfolio, and they're guaranteed to show up I am at least smart enough to figure out that some of them are 50 bagger or a hundred bagger, and I hold onto them and I do not sell them.

What I did is, I said, Okay, how do we identify these hundred baggers? What I discovered is that if I just looked at the examples in my own portfolio and obvious examples around me, there are basically about five different categories that these 10, 200 baggers fall into. Now, it could be more than five, but five is the one I was able to come up with before it was time for this lecture. If I come up with more, I'll update you next year, but we at least have five very distinct kinds of companies, which should give us clues that these are businesses that we want to hold onto. The first category of companies that has the potential for these 10 to 100 by a hundred baggers is these are businesses that have huge tailwinds.

Tailwinds mean they just have all the factors moving in their favor. They have very deep moats, they have very long runways, and they have a very high return on equity. They typically don't need any debt. The most important condition an idiot can run these companies. Like Warren Buffett says, "Invest in businesses that idiot can run because one day an idiot will run them". Which are the companies that a complete moron, stupid idiot can run? The businesses like 'See's Candies, Coca-Cola, Moodys, Visa, MasterCard, American Express are the types of businesses that are deep in the moats. In fact, if you look at a company like Coca-Cola, they have more than a hundred-year history. In the hundred-plus year history, for several decades, the company was poorly managed.

You have a company in China, Maotai, maybe some of you even consume the product, and with due respect, I think Maotai probably has great management, but with due respect to Maotai, an Idiot can run that company, Okay? You do not need anything between your ears. You can put me in charge of Maotai and I can run it. Even a person like me can run that company. That is an unbelievable, fantastic business. There's a good friend of mine, you might have heard of him. His name is Guy Spier, and he lives in Zurich, I think he's going to try to also speak to you next year. Maybe we'll both come together we'll see if we can do. (back to lectures). Guy has a mental model he uses, and his mental model, which is used for more than 15 years is that, if he identifies a company like Moody's or S&P as a great business, or let's say if he identifies Coca-Cola as a great business, or let's say the Coca-Cola Bottlers as a great business, then he looks around the world for Coca-Cola Bottlers in other countries.

If he finds that being a Coca-Cola Bottler is great in Tennessee in the US, then I want to find the same business in Brazil. I want to find the Bottler in China. I want to find the Bottler in India, and I want to go around the world looking for the Coke Bottler, and I want to find which one is being undervalued, and then I want to invest in it. Because the economics of these Coke Bottlers, no matter where in the world they are, is about the same. They all are great businesses. One of the businesses, which is the ultimate deep business is Moody's. They do the debt ratings. Even in the financial crisis, when they gave all bad and flawed and garbage debt ratings, it still did not destroy the company. This is a great business that an idiot can run.

Guy said to himself, what are the credit creating agencies all around the world, which have the same business model like Moody's? Because Moody's is a model where they'll hire an analyst, they pay him maybe a hundred thousand dollars for each analyst, they pay a hundred thousand, and they're probably collecting \$4 million in fees. It's just a great business. Just the economics are fantastic. He found a company in 2001 in India, which was very small, but was a number one credit rating agency in India, exactly like Moody's was in the US. He found that and S & P 500 owned 10% of that company. S & P had done a lot of due diligence, and they bought 10% stake in the company. That company was called Crystal. Guy's Pier at that time was managing about 30, 40 million.

He made a small investment in Crystal, and it went up, it doubled or tripled in two, three years, and then he bought a little bit more. Then another year or two later, he sold it all. He had made like four times his money. Sometimes I like to pour salt on the wounds of Guy Spier. Like sometimes I want to have fun with him. I spoke to him last night when I was preparing to talk. I said, hey, Guy, you know that crystal position that you owned, which you sold if you had not sold it, it went up 130 times after he sold, okay? He's the kind of guy who doesn't even trade that much. He just buys and holds. I said, hey, by the way, that Crystal you sold back then, why'd you sell it?

He said, Mohnish do not remind me. That's the dumbest thing I did. Because basically, if he had kept Crystal, he manages 160 million, the crystal position would've exceeded the entire portfolio he has today. 1 decision. What was so hard about that decision? Well, it wasn't hard. They were a replica of Moody's. I'd already told you, an idiot can run Moody's, just like an idiot can run Coca-Cola. Idiots have run it, and they've not been able to destroy these businesses. The first thing to do is when you run into businesses that idiots are running or can run, and they still continue to be in business, buy those companies if they have these characteristics, and then forget the PE ratio. Just buy and hold forever, because probably those are very few businesses on the planet. Like, I can almost bet that maybe 10 or 20 years from now, Maotai looks very different.

But it's hard to tell the path it takes. But it looks like a great business. That's the first one. The businesses that idiots can run. The second is exactly like the first, except these cannot be run by idiots. These are businesses which are exactly like the first kind, which is they have huge tailwinds, they have deep moats, they have ultra-long runways, they have high ROE, they don't need any debt, but they need great management, and they do have great management. These are businesses like Amazon, Costco, Geico, Ammo Pacific Kotak Mahindra Bank, the one I bought in India, which went up 60 times or something, Blue Dart, which is the FedEx I bought in India, Satyam, the IT company. Then Restaurant Brands, which is the one that owns Burger King, Tim Hortons, McDonald's, and Yum Brands, Domino's Pizza.

These are all great businesses, but they do need solid management on top of them to make sure that they keep those franchises. But these businesses have economics that are just phenomenal. Just great economics. That's the second type of business you want to keep and look for in your portfolio. You get these massive runs as we saw with Blue Dart and others in India. Then the third kind is the ones which have shown up the most in my portfolio. I have never had the good fortune of having the first kind of business, which is huge tailwinds and idiots for management. I've never had that. If I ever get that in my portfolio we are never going to sell those. We're going to keep that forever. Now the third one is when the market gets confused between risk and uncertainty. What I want to do over here is I want to go through some examples from my own portfolio. In the past, in some cases, I was able to capture the upside. In other

cases, I was too stupid and I missed the upside. I made some money, but I didn't make a lot of money.

The first company I want to talk about, and sorry, these are not businesses you may have heard of, but that's the nature of this game. The ones that are going to be a hundred bagger they're not going to be the biggest names around that you've heard of. In 2005, I invested in a steel company which was based in Canada. They were traded in the US called IPSCO. IPSCO made two types of steel. They made plate steel, and they made tubular steels, kind of like pipelines drilling for drilling oil wells and all that. They made this kind of these specialized steel, which was either in pipe form or plate form. The company had the following characteristics.

When I invested in it, the market cap was two and a half billion. They had 900 million of extra cash on the balance sheet. The company had contracts on the book because there are these pipelines that were going to buy this steel for the next couple of years. They had a two year backlog where they knew that their earnings for the next two years were going to be 650 million each year. You had a two and half billion, two and half billion dollar market cap, and you had 2.2 billion between cash they already had, and then cash that was coming in the next two years. You would collect about 90% of the market cap in cash in two years. After two years, you still had all the plants and equipment and people and everything was still there. But after two years, there was no visibility into earnings, and we know the steel business can go up and down.

The way I looked at it, I said, what we are going to do is, I'm going to make a bet. I'm going to put 10% of my assets into this. I'm going to just sit there for two years, and if it doesn't work, we probably get back 90% of the company's completely gone, but I don't think it's completely gone. I think it's a real business. What happened is a year later, they made the 650 million, and the year later they had visibility for one more year. Now they said that they would make 650 million for the third year. Now they had three years of 650 million, which was almost 2 billion plus the 900 million. Now we were above my purchase price. The stock that I bought at 45 a year later was sitting at \$70. I said, well, we are above what we paid, but we still don't know what the business does after three years.

Why don't we just wait for another couple of years? See what happens? In 2007, I waited one more year, and by now the stock had gone to maybe \$105, and they got a buyout offer. Another company came and bought them for \$160 a share. When the deal was announced for \$157 something, I sold the stock. We ended up with almost a four X in about two and a half years. We captured the entire 4X, right? This was a situation where it's a highly cyclical business and markets hate uncertainty. It's a highly uncertain business. But the risk for this business was very low. It is what I call very low risk and very high uncertainty. When you find a combination of low risk and high uncertainty, usually that

combination is going to give you a high reward because markets are not very good at pricing in uncertainty.

They hate uncertainty. We get some benefit from that. In fact, there's a business in my portfolio currently, and I don't talk much about my portfolio, but I'll just make an exception because I love you guys so much. I own a company called Fiat Chrysler, which is based in partially Italy and partially in Detroit. Fiat Chrysler is very similar to IPSCO. The stock is at \$6 and change, and the management of the company says that in the year 2018, their earnings are going to be around \$5. If the management is correct about the future prospects of the business, then basically the business is being priced at 1.2 times earnings for one year. My answer to that is, okay, we'll hold this stock to 2018. If it's completely worthless as a business, I mean, they have 130 billion in sales of cars. They just started manufacturing Jeep in China. The Chinese love their Jeeps. Raise your hand if you think Chinese love Jeeps.

All right? At least a few Chinese love their Jeeps, That's great. Their Jeep sales are going up like five times in the next three years in China. But anyway, I happen to think that what they are saying makes sense. The market thinks it doesn't make sense. No problem. Just like IPSCO, we put the stock in the portfolio and forget about it. I'll wake up in January 2019 and see what happened. If you invite me back in 2019, I'll tell you what happened to Fiat and between us girls, we may end up with five times our money if it trades at five times earnings or seven times our money if it trades at seven times earnings and such. That's IPSCO. Then there's another company too; Tesoro Petroleum.

This is one which we did not capture, we should have, but we didn't. IPSCO is in the steel business. Tesoro is in the oil refining business. They have oil refineries in the United States. In the United States in the last 30 years, not even one new oil refinery has been built because of NIMBY. NIMBY is Not- In-My-Backyard. Nobody wants the oil refinery near them. In the entire US anyone who wants to build an oil refinery never get the permits. The oil refineries that we've had for 30 years ago are the same ones we have today. They keep trying to tweak the oil refineries in the US to get more and more capacity, but they're not able to build new ones.

Anyway, Tesoro had a bunch. The oil refining business in the US is a good business. The reason is good because all the different states have different requirements for how the gasoline or petroleum is to be produced and the amount of emissions and all that. You need different refineries for different states to meet the standards, which makes it difficult for other competitors to come in. Even though oil refining may be a commodity business, it's not a commodity business because it's got these kinds of local aspects to it. Anyway, what happened with Tesoro is that there was another merger taking place with two large oil refiners. In order to make that merger happen, they were forced to sell one of the oil refineries to make the merger happen.

Tesoro bought that refinery; they leveraged their balance sheet to buy that refinery. After they leveraged the balance sheet, the crack spread, which is the spread that refiners get to make crude oil into gasoline, the crack spread narrowed to almost nothing. Their profits went next to nothing at the same time when they had a huge amount of debt. Markets looked at the debt and they saw a lot of uncertainty because it is very hard to predict the crack spread. Just like the uncertainty of steel prices, the refining margins are always uncertain and markets project presence, and circumstances to infinity. Markets said, Hey, the crack spread is small, it'll always be small. They have all this debt; they may not be able to pay the debt. What happens if they don't pay the debt? Well, what happens if they don't pay the debt is they have many refineries.

They can just sell a refinery. They don't need to go bankrupt. They can just sell some assets and they can get out of the jam they're in. I looked at the company, the balance sheet, the debt and so on, and the stock was at seven and a half dollars. It had gone down a lot. It used to be at almost \$30. It had gone down to 25% of the price. I bought 10% of assets at seven and a half dollars, three months after I bought the stock, it was trading at \$1 and 33 cents. The 10% of assets I put in just this alone took my portfolio down by 8%, this one position. But one of the things that always happens to me, but it only happens to me, it doesn't happen to you, is every stock I buy goes down first and it always goes down.

I don't know why it doesn't go down before I buy, but they all go down after I buy somehow it knows. Bruce Berkowitz is a fund manager. He calls it premature accumulation. I always have premature accumulation and anyway, so 750, we're down to a dollar 33, we are used to that. We're not going to sell anything. We sit there and then a few months later, the crack spreads widens and they're paying down debt. The stocks is at \$15. I said, Hallelujah. From a dollar 33 to 15, 10 times from 750 to 15, double less than three years still on track for 26%, we are out of here. Or like Arnold Schwarzenegger would say, as to we release the baby sold the stock and moved on. Now, what I didn't realize is that Tesoro had a phenomenal manager, Bruce Smith, just a kickass manager.

He was just a master at extracting value from these refineries. He bought pipelines and refineries when the financial prices took place. If I had kept the Tesoro from the bottom tick of a dollar 33, it went up 200 times till today. Okay? From the time I bought it went up about 40 times. I only captured a double. But the rest of the ride I completely missed because what this guy was able to do was, he was a master at buying these assets, extracting more value, getting more ghetto, getting more assets. They spun off a pipeline company. A lot of things they did, he de leveled the balance sheet and all of that. Even now, I think it's done well.

That was an example of a low risk, high uncertainty business where I already knew in the period I owned the stock that I was dealing with an exceptional manager. Because in the conference calls, I was in love with Bruce Smith. He

was just a great guy. He was doing all the right things, but we missed that 40 X and there was a chance to get a 200 X. Then we are going to go to another one, which is a shipping company. All these wonderful businesses, steel business, refining business, shipping. You thought you can only make the money on Alibaba and Baidu. No, you can make the money without Alibaba and Baidu. You can make it at other places too. For example, Frontline was a shipping company. This company basically focused on transporting crude oil.

They had something known as VLCCs (very large crude carriers) that they owned. Global Fleet at the time I invested, I haven't looked at the shipping business lately, but this was an investment I made. I think in around 2000, 2002, there were about 400 VLCC in the world. Frontline was the largest among all of them. They had about 70 of them in their fleet. 70 out of 400 were owned by Frontline. This is the ultimate high uncertainty business. The VLCCs have chartered two different ways. Either they are time charters or they're daily charters. The entire frontline fleet of 70 ships was on daily charters. The daily charter rate for these ships can vary from \$5,000 a day to \$300,000 a day. It is a huge variance. That time, I don't know what the economics are now, but in 2002, once the rates went below 12 or 13,000, they were not making any money.

They were losing money. Once the rates went over 30 or 40,000, they were just super normal profits, exponential profits. But the exponential profits, you didn't know what would happen the next day because every day these prices fluctuate. But there's a particular nuance in the shipping business that I understood, and I understood this because a friend of mine in the real estate business explained this to me, he said, "when you build these large office towers in the US, in China's probably much faster, but in the US it takes three to five years to get the permits and build these 20, 30, 40 story buildings". What happens is that when office space is very tight and fully occupied, all the real estate developers rush out to build new buildings.

They all rush out to build new buildings at the same time. The banks finance all of them at the same time because everything looks great. It's a booming business, they can see a hundred percent occupancy. Then five years later, all these buildings come on the market at the same time. What happens is the occupancy and the rents collapse at the same time. In this kind of high end office buildings, you have this boom and bust cycle of very high occupancy and then low occupancy, then high occupancy and low occupancy just keep going back and forth because the property developers just think whatever's happening right now is the way it's going to be forever. The people who are in the shipping business are even worse than the property developers. They believe everything that's happening right now is the way it's going to be forever.

What happens is that when these VLCCs are trading at 200,000, 250,000 a day, they all go to the Korean shipyards and place a huge number of orders for ships.

They say, build me the ships. Same like the building. It takes three years, or four years or two years to build the ship. By the time the ships are built, all these ships get delivered at the same time, those rates collapse, and then they go scrambling again, and they got a bunch of bankruptcies. The business goes through the ups and downs. Now, one of the things that happens is that when rates go to 5,000 a day or 10,000 a day, scraping off ships increases a lot because they're losing money. What they do is, they take the old ships and just scrap them. They make some money. The size of the fleet goes down at the time when the rates are low.

As the fleet size goes down, it sets up the conditions for rates to go up. Then when the capacity goes down, the rates start going up. You cannot bring in more capacity because it takes three years to build a ship. The only thing that can happen is price goes exponential. Anyway, I bought Frontline at a point when these prices were at 5 or 10,000 a day, the stock had collapsed, and it was trading at something like I think at about \$6 a share. Just like with the Tesoro, a few weeks after I bought it, it was trading at \$4 a share, lost one third, not as bad as Tesoro, but one third is gone. Then it went from \$6 to \$9 in a short time. I wanted to just capture that spread.

It was above the liquidation value of the company. I sold the company anyway because of the very high uncertainty in rates. This company, if I had held the stock throughout, even with all the recent collapse in shipping, it would've been a (40 times investment from four to 160 I'm sorry, not, 40) it'd be from six to 160, about 30, 35 times my money. Another company, which I just wanted to talk about is Teck Cominco. This is again low risk, high uncertainty. During the financial crisis commodity prices collapsed in 2008. They went to nothing, right? This company, Teck Cominco, like the IBM of mining, they have huge reserves of metallurgical coal and huge reserves of Iron ore and lots of trade with China and such.

But they had done an acquisition just before the financial crisis; large acquisition. They had taken a bridge loan to close that acquisition. Then the financial prices happened. They couldn't refinance. All the prices collapsed, and this stock went from \$50 to \$4. It dropped by more than 90% in seven weeks. When I look at the company, it's again, like the refineries. They had all these different minds and assets all over the world. Some of them were the lowest cost minds you could imagine. The banks did not want to take over this company. The banks don't want to be in the shipping business. The banks were probably going to do what I would call extend and protect, which is they would take some fees and penalties from them, but they would extend their loans. In fact China came in as an investor in Teck Cominco.

In a few months, the stock was up seven times. We bought at 4 or \$5, we sold at \$30, and then it kept going. It went to \$50. We didn't capture all of it, but we kept most of it. Anyway, that was the third criteria, which is the low risk, high uncertainty. Then the fourth criteria is what I call bankruptcies, reorganizations

public LBOs, special situations. How many of you have heard of Sam Zell? Raise your hand if you heard of Sam Zell.

At least one person, the professor. Well, I think you should extend an invitation to Sam to come speak to your class. Sam is called the Grave Dancer. He dances on the graves of companies that are left for dead. If you get a chance to invest with Sam, generally speaking, it's going to go well. Warren Buffett, Sam Zell, and the Pritzker's, these are some of the very best people on the US tax code. They know US Tax Code better than anyone else, way better than Donald Trump. They know the tax code. I don't think Sam Zell has ever send much of a tax bill to the US government because he's just so efficient with the way he runs his tax affairs. Anyway, this story is interesting story, but it goes back about 26 years.

In 1990, there was an insurer called Mission Insurance that went bankrupt. When this insurer went bankrupt, they had 630 million in NOLs (net operating losses). These net operating losses that the company has, have a lot of value if you can bring that shell company into a company that has profits, because you can shield 630 million of profits because of that loss. Sam was able to buy that company for like 30 million because it had nothing other than the losses, and you have to find something so he bought the 630 million of losses for 30 million about seven, eight years after the bankruptcy. This was in 98 or 99. Then there's another investor, Martin Whitman from Third Avenue, who also bought some of the shares in this Mission insurance. Then the two of them went looking for a profitable business that they could join with this operating losses, so that they would suddenly have no taxes on the business.

They found a barge shipping company on the Mississippi River, Like Tom Sawyer on the Mark Twain on the Mississippi River. They found this barge company, which used to send goods up and down to Mississippi, and it was profitable. They said, Okay, we'll buy the barge company. Now the barge company is not going to pay any taxes because we got these NOLs, and that's how we'll make our money. Then what happened right after they bought the barge company is the barge business went to debt. The rates collapsed, and the barge company went bankrupt. They now had bankruptcy to the power of bankruptcy. I don't know whether you teach them professor, how to calculate bankruptcy to the power of bankruptcy, but it's not good. They had two bankruptcies now instead, one.

Instead of having 630 million in NOLs, they now had 800 million in NOLs, even higher. Then they went looking for another company that they could buy, so they could take both these things and pair it together. They had a company called Daniel Steel holding, that was trading at \$1 share. Then they found a waste to energy recycler. What this company does, it's a plant where you put garbage in on one end, and you get electricity on the other end. It's a German process. There's a bunch of these plants in the US which convert waste materials, garbage into electricity. The economics of this purchase was this

company had 2 billion in assets. It had 2 billion in debt, and they bought it for 30 million. It was very highly leveraged, but it had this kind of energy business, and they thought that they could tie it in.

They tied it in, and then they needed some capital. Then they started to do a rights issue. That's when I found them. The stock was a dollar. By the time I was able to invest in them, it was at \$9. It had already gone up like nine times. Then did two rights issues. They bought another company. Basically in about 13 months, I had a double and I sold it, basically if I had kept the position, it was about a 40 X from that dollar price they had, and about a four x from where I had bought. As you can see, we have all these companies that are in these weird places.

They're not great businesses, but they do well. Then the final one I want to talk about, which is the fifth model is upside without downside. I also call this playing the bubble. What happened in the late nineties, the dotcom boom was in a big way, and everyone thought it's going to be transformational, it's going to change everything. These companies like pets.com, et cetera, they had huge valuations. Even Amazon was a huge valuation, Yahoo, all these companies. Now, I had spent some time in technology. I knew that the internet was important, but I also could not tell which company would make it and which company would not make it. I was definitely not interested in buying anything which I was even trading at 10 times earnings. I like to buy things at three times earnings, or even better, like Fiat one times earnings, that's even better.

I was not interested in buying these businesses, but there was a bank in Silicon Valley called Silicon Valley Bank. good bank. It was a normal bank, except that they had one thing. What they did was, see, in Silicon Valley, what happens is that if you are a landscaper, a gardener for Google, they'll give you stock options. If you are a chef for Google, you'll get stock options. If you are a waiter in a restaurant, they'll give you stock options. Stock options is like breathing in Silicon Valley. This company, Silicon Valley Bank, whenever they made loans to all these dot-com companies, besides getting all their loan terms, they always got warrants and the companies didn't care. They gave them warrants. Every time they would do some loan or some deal, they would get these warrants from these dot coms.

They never disclosed how many warrants they had, what warrants they had, and what the strike prices were. No disclosure, they only said that we just get warrants. They were the unknown element to what these warrants were worth. But the bank itself was trading at a very low valuation, just slightly above book value and very well-run bank, even now, it's existence has done well over the years. I said, Okay, this is the way to play the bubble, which is to buy Silicon Valley Bank. If those warrants turn out to be useless or worthless, we don't lose any money. We still have the bank, and it turned out to be something. Then we have a huge run. Basically, I think we had a two and a half, yeah, we made two and a half times of our money in two and a half years on the stock.

If I had held it a little bit more another year, I would've made five times the money, because then they disclosed the warrant just as the 99, 2000 bubble was speaking. Then they started selling those warrants. They monetized them, which worked great. Then the other company, which was the first company in my portfolio, that went a hundred x was a company called CMGI. They were an incubator of internet businesses. I bought them just slightly above book value, because at that time, people didn't fully understand what that business was doing. They just kept taking stakes in dozens and dozens of internet companies, and then they had to hold basket of them. Then the markets fell in love with these kinds of companies. They took it to the stratosphere, our hundred thousand became 10 million, and I sold almost, nearly at the top, I think maybe 20, 30% off the top I sold.

This is kind of something that comes into play. When you have bubbled, it's probably not the most elegant way to make money but sometimes you can get these upsides without downside situations when that can play out. With that, those are the kind of the five models. We have the huge tailwinds with the idiots who can run the company, and the company does well. Then the second is a huge tailwind, but you cannot have idiots. You need smart people running it, kind of like Amazon and Geico. Then the third is Market get confused between risk and uncertainty. We talk about IPSCO, Tesoro, Frontline, and Teck Cominco on that. The final one was the grave answer. Sam Zell, bankruptcy reorganizations, public LBOs, busted, LBOs, special situations. Those can all work out quite well as well. Then you'll finally have the upside without downside which happened only once to me. The most mega bubble I had in 22 years was in the late nineties with the dotcom, when most of you were still, I think maybe not even in kindergarten, but maybe just in kindergarten. With that, I think we can talk about what you want to talk about.

Professor: Thank you very much. I feel excited. I think I quit my professor job and go into billion aspect, many hundred baggers in Chinese market. I just don't have time. Okay, now I'll open the floor to the students to ask questions. This is one very valuable opportunity. Every word works like quite a lot of money. If you have a question, just press the button push for the speaker in front of you. If the light goes bright, then you are on. All right.

Student: Okay. Can you hear me?

Mohnish: Yeah, sure.

Student: First of all, thank you very much for your insightful speech. The question I want to ask here is that, what do you think is the core competence of an investor? how do investor differentiate from the huge investor group? Thank you.

Mohnish: Okay, Well I think that's a great question. Yeah. I think that the number one skillset that an investor needs to have is extreme patience. In fact, one of the things I learned when I was putting this talk together is like, if I look at a company like Blue Dart, which was the FedEx of India, I held the company for

six years, and it didn't do anything for six years, and I sold it, and it had its run in the next 15 years. There was no good reason to sell it. The number one skill set is patience. If you are the kind of the kind of person who loves to watch paint dry then this is the business for you. If you love to watch paint dry, and so if you are a hyperactive person who's always looking for action this is not the business for you.

I think that in many ways, the investment business is a strange business. I think it's a business that is best for people who are, what I would call gentlemen or general women of leisure, where they have some other activity, which is their primary focus. Investing is a secondary focus, so they don't have a compelling reason to act. Usually, investors hurt themselves every time you trade. Charlie Munger says that you don't make money when you buy a stock and you don't make money when you sell a stock. You make money by waiting. In fact, what some of the things I talked about today show us is the huge advantage that you only learn about a business after you own it.

If you do the analysis of a business before you own it, you may know something about it, but you're going to know more about it after you own it. That's when you have an opportunity to perhaps understand which ones have truly multi-bagger possibilities and are the ones that you should not touch. Just let them play out for long periods. Patience is very important, and that's what separates people. In fact, one of the things about stock markets is they're deceptive because if you look at the market or the board, which shows all the stock prices, you see them changing all the time. All the lights are changing and flashing it, all the signals it's telling you is to be active. It gives you all the signals to do something.

What you have to do is ignore all that. For example, one of the rules I follow is, I do not submit any orders when the markets are open. Anytime I'm trying to buy or sell something, I usually sell it, and send it at this time, after midnight to my broker to execute the next day, because there are no price changes taking place, there's nothing taking place. Everything is calm. Then during the time when the markets are open, it's very rare that I will trade. I basically avoid that. You can set up some tricks, if you will, to help you, because everything is designed to make you active. Your broker does not make any money if you don't buy and sell stocks. If you just buy one company and just keep it forever, then I want to make any money, but it's good for you, it's not good for them. All the signals are the wrong signal. Patience is number one. That's what I would say.

Student 2: My question is, among the five categories that you mentioned, what's your proportion like? In your portfolio, how much do you put in these five categories? What are the reasons for the same?

Mohnish: Well, let me put it this way. Charlie Munger says that each of us has a very limited quota of stocks that truly may have the potential to make us rich. There

are very few times that we are going to end up with things in our portfolio that truly got the potential to make us very rich. Usually, it is not apparent before you make the investment. Usually it'll become apparent, maybe after you own the business for some time, it takes some time. I mean, I can think of many examples. When I invested in the business, I thought, I'll get a double and move on, but then I start to learn more about the business. It's the wrong way to think about it by saying, I want to put 10% in number one or 20% in number two, or whatever.

This is an opportunistic business. You need to be very flexible. Like I said, the number one skill set is patience. What that means is, it could be a long time before anything shows up, or it could be that five of them show up in one week. Like for example, during the financial crisis in December, 2008 and January, February, 2009, there were so many ideas coming at me that I literally had less than one or two days to process each one. Whereas normally I will have weeks, even months to process an idea. It's not a good idea to do this top down. I have never done a top down. What I think you need to be is, you need to be kind of a bargain hunter. You go into a bizarre and you're just looking for what looks exciting or cheap.

I'll give you the example of kind of the difference between Ben Graham and Charlie Munger. Ben Graham will go into a supermarket and he'll look for what is the most heavily discounted item, deeply on sale, and then he'll buy that and come out, and Charlie Munger will go into a supermarket and look for the things that he loves. Then he keeps going back every day until what he loves has dropped in price, and that's when he buys it. The Munger approach, in my opinion, is more superior to the Graham approach. But the Munger approach requires patience, and it requires you to understand what you truly like, and then you wait for the right opportunity. It is a very good exercise to make a list of assets that you truly think are remarkable assets, and also make a list of, at what prices those assets would be interesting or exciting for you.

When you have that list, then you just sit back and wait for the world to come to you as opposed to taking my list and trying to go top down. The second thing about top down that doesn't work is it's very unpredictable when these things are available and when they're not available. What is within your circle of competence and what is not? Like the professor said that there are a hundred bagger, I would say, in every market. Definitely in China, you have a huge number of a hundred baggers at any given time. The problem is most of us do not have the ability to see it, because we either don't have the circle of competence or we don't have enough knowledge about this. This is a business where you want to be a student, you want to learn, you are to keep educating yourself.

Every once in a while, there'll be a business that'll show up in your portfolio. Like I can think of right now at least three or four companies in my portfolio that could end up being huge home runs. Now, I cannot tell you which one, I

don't know which one, but I'm willing to be patient and watched and let them play out, because even if one of them is a 10 X, it's worth letting that play out because they're so rare. That's how I would suggest going about it.

Student 3: Well, thank you for a great talk. Mr. Pabrai you spoke about the cyclical nature of the shipping industry. When freight rates are high, ship owners essentially order a lot of ships, and once they arrive, freight rates go down. Do you think the ship owners are going to learn from their mistakes? Or is this going to be a problem that we keep on seeing in that industry?

Mohnish: The ship owners will never learn. The property developers will never learn, humans and our genetic makeup isn't going to change in five years or 10 years or 50 years. We vacillate between fear and greed. As long as there are humans driving action in industries like shipping, you are going to see that vacillation. In fact, there's a good book, it's in fact a work of fiction. It's called The Shipping Man. I forget the name of the author, but I think if you Google it, you can find it. The Shipping Man is the guy with an investment banker in the shipping business who wrote that book. It's a funny book because it talks about the Greeks, it talks about the Norwegians, it talks about all these kinds of Castro characters, the Americans in this business.

It's funny as hell, and it teaches you the business while entertaining you. That author has written a book to read and in fact Frontline, one of the companies I invested in is run by a guy named John Fredrickson Norwegian guy. He has a character in the book who I think is a clone of Fredrickson, which is why I found the book kind of funny. I haven't looked at the shipping business in a lot of detail lately, but it's a challenging business right now. What that means is there's probably opportunity in that business. But I would also say that tread carefully

Student 4: My question is, out of the five strategies you mentioned require deep research in the Business model, and to how much extent you rely on the open data source to the public. Do you have any unique or special channels for information to help you to make the decision?

Mohnish: Yeah, all my data sources are open because I am a very lazy investor. I never meet management; I never talk to management. I never travel to see any plants or anything. I've never done that for any investments. The results still work out. We are not looking for superior information. What we are looking for is superior analytics on commonly known information. For example, I mentioned the boom and bust of the shipping industry, and the gentleman asked me about, is that going to change? Well, number one, it's never going to change because we have humans involved and humans are host on the emotions. The second is the market participants, we have two advantages against market participants.

One is we have analytics which can help us because we have some understandings that maybe markets are missing. The second is that we have patients. Most investors don't have multi-year horizons. I want to buy a stock at 10 and two weeks later I want to sell it at 12, and then I want to buy something

else at 12 and sell it at 15, and I want to keep doing that. Well, good luck. If that worked, they'd be Warren Buffett because the compounding rate would blow away Buffett compounding rate. But clearly, we still have Warren Buffett in place, so therefore that approach doesn't work. If you have the patience and if you have the interest to dig deep. Then what you're going to find is that with commonly held information or no known information, you may come up with insights that others have not

This is what Charlie Munger talks about, the latest work of mental models, you look at things through a different lens to try to see what can be different. Like, I would say that when my friend Guy Spier uses the mental model saying that if Moody's are the great business in the US, what other businesses are like that in the other parts of the world, that's a great model because you may be able to find a business in another part of the world where people have not realized what a great business they have. That's why these things get to where they are. For example, I think all my life, or at least all my investing life, I hated the automobile industry because it's high Capex (Capital Expenditure) it's unionized.

You got consumer taste and you got a lot of things that are not good about the business. But when I studied the business, I spent one time about six weeks studying the business, I realized that many of my underlying assumptions were wrong. That the reason the auto companies problems were for different reasons than what people think they have problems. I did not have access to any data that is not publicly known but I just synthesized it from many different sources to come up with some insights and those insights were helpful. I think the thing is that if you are a curious person, and if you are a person who's very deeply interested in business and how business works and understanding different business or industries then you can do quite well.

Professor: I have a question that's related. Could you tell us a little bit about your lifestyle? How much time you spend on thinking about investment every day? Because the size of your asset and management very easily places you into one of the top 10 active stock funds from China. I know many of those fund managers had life and pressure and are very busy and lot of overwork is not a good lifestyle for those fund managers who are managing the similar size of what you manage. How is the lifestyle different?

Mohnish: I should not advertise this, but it's the best lifestyle you could possibly have. I, maybe, have three or four ideas in a year. Sometimes we don't have any in a year, and sometimes we have many more than that. It varies. If you follow the Buffett Munger model, which I do, your life is going to be fantastic. Here's what happens in the Buffett Munger model. Number one, I have no staff. There are no analysts, there are no associates. If you send me your resume, I'll be excited to read it, but I can help you with a job because there are no job openings because we've never had a job opening. One part of the Buffett model is that

you do not delegate your investment research. Warren Buffett, even today when he buys IBM or whatever he buys, he does all the work himself.

He doesn't have anyone under him doing any of the work. There's no one building spreadsheets for him or anything like that. That's the same thing at the Pabrai Investment funds. I have a few part-time admin assistants who are great, they help run many of the back office things if we have, but even there, we don't have much going on. In a typical month, I don't get any phone calls or any emails from my investors. Zero. Okay. I have about 400 families who have invested with me, and these families basically got selected because I have some very strange rules with how I operate. For example, before people invest I don't meet them and I don't do phone calls with them. The only people who can invest are people who are willing to do reading of their own.

We can give them access to our website, they can read various things, if it makes sense to them, they can invest. That doesn't work for most people, but for the people it works for, since they invested the money without talking to me they are not looking to have a lot of conversations even after that. What I tell my investors is that we have a couple of annual meetings every year where they can come and they can ask any questions they want, and they come from all over the world. I have investors from everywhere, and they show up at the annual meetings. In effect, we are open for business two days a year. It's a lot of fun to meet them and talk to them. Basically, if you don't have any staff, you don't have any HR problems and you have no issues.

What is the reason that Buffett and Munger don't have analysts? Well, the reason they don't have analysts is that the investment business is a very strange business. You need your brain at unpredictable times, and the rest of the time you don't need your brain. If I hired a super smart analyst, someone in the audience here who I think each person knew is exceptional, that person would want to do something constructive with their lives. They would either look to me to tell them what to research, or if I don't give them any direction and say, Listen, just go look and tell me when you find some great talk. Let's say, I just tell them that listen, you work on your own and just figure out when you have a great talk idea and bring it to me.

Let's say I did that, for example. Well, what would happen is that because we have different circles of competence 90, 95% of the time, whatever they come up with, I would say no to it, because 95% of the time, what I come up with, I say no to myself. Since I would've liked this person when I hired them, I would feel bad about saying no all the time because, it'll just be unpleasant. Eventually I would give up and say, okay, I'll buy the stock that you want, even though I'm not sure about it. Then you've just destroyed the model. What you have to do if you bring in people is you have to give them their own pools of capital, so they have full autonomy to do whatever they want, and they don't come and ask you what to do.

That's what Warren Buffett has done with Ted Weschler and Todd Coombs. He just gave them each 9 billion. They do whatever they want, they don't talk to him. That works. When I look at investment operations, like you mentioned a bunch of operations in China, et cetera, I look for violations of the model. Moses came up with the 10 Commandments. We have commandments in investing as well. They come from the guy with the bus behind me, and they come from Warren Buffett, and they come from Ben Graham. They've rewritten the commandments. One should follow those commandments. When I look at an investment operation, the first question I ask is, how many violations are there? The first place I look for violations is team size. I can almost guarantee that the investment managers you're talking about, who seem to be stressed out, are not operating with a team size one. Do they have more than one person on the team?

Professor: Much more than one. Like that team?

Mohnish: Yeah. Like how many? 5, 10?

Professor: No, different firms, they have different structures,

Mohnish: But

Professor: Employ analyst, they also have assistance.

Mohnish: Yeah.

Professor: All sort of things,

Mohnish: All that is hocus pocus. There's no need for any of that. I mean, the bottom line is what is the model? The model is buy things at half off, you have 5,000 stocks in the US and you have several thousand outside the US in China, wherever. We are bargain hunters. Why do you need a team to find bargains? You don't. We didn't talk about it in this talk, but the simplest way to find bargains is to be a cloner. I am what you would call a shameless cloner. I met Li Lu who's a hundred times smarter than me. I say, Li Lu, can we meet for lunch? Occasionally, I'll ask him, Li Lu, what do you own? In a moment of weakness, he'll tell me what he owns, and then I just go buy it, and I'm done.

I don't even need to pay Li Lu. It's great. Probably, a better analyst than anyone I would hire. Then in the US we have 13F filings where every quarter of the people must file what they own. Just figure out who smart people are, look at what they're buying, reverse engineer them. You don't need an analyst. It's fun. I think my job would not be fun if I had many times by the time I get to the office half the trading days over, I mean, in California, the stock market opens at 6:30 in the morning. I can assure you I am drooling on my pillow. I am fast asleep. If I'm not sleeping till two in the morning, I'm not getting up at 6:30 tomorrow morning.

Please don't tell this to anyone. This is just between us. Okay? Tomorrow morning, I will wake up at around 9:00 AM, I may wake up at 9:30 AM there's no alarm. I'll wake up whenever I wake up. There are no meetings because there's no staff and there's nothing on the calendar because that's what Warren Buffett told me, keep your calendar empty, and I have no idea what I'm going to do tomorrow. No idea. But I know it'll be an exciting day because I have so many books to read. I've at least got 30 books on my desk that I want to get to. I'll pick some book, if that's of interest. If some company shows up, I'll read about the company. If I want to watch a movie with my wife, we'll do that. Whatever, man. I mean, the key to life is find Crystal, that's the Moody's of India, and then just go to sleep for 20 years.

That's it. The purpose of this talk is for me to understand that, to become even less active is not even wake up at 9:30 in the morning, wake up at two in the afternoon, who cares? Because we found Crystal and then the guys that own Crystal would make all the money for us, we don't need to do anything. Warren Buffett says that it is not a good idea to get married for money, right? Usually if you marry someone because they're rich, that's a bad thing. Usually, it doesn't work out very well, but it's a terrible idea to marry for money if you're already rich. Okay? That's terrible. The fund managers you're talking about, I would guess that they are wealthy. Are they wealthy? Are they rich?

Professor: Especially for the younger generation of young managers. Yeah. When they get promoted, go up the hierarchy, they become good.

Mohnish: Yeah. The young managers, it's very simple. If you believe in the power of compounding, then a small amount of money on the side can get you to independence relatively quickly. The analysts and the young managers and so on, I think the key is that you spend less than you earn. You put something away, and then that little something can become more and more. Eventually what you want to do is, you want to be your own boss. Forget trying to chase the corporate dream. Forget all of that. I think one should only be in this business if you love this business. In my opinion, the way to love this business, there are some rules. Number one, no staff, number two, no trading during office hours. Number three - don't even go to work when the market is open. Just be a gentleman of leisure or a gentlewoman of leisure. That's it.

I was very lucky that I never worked in the investment business. I didn't even understand the investment business. I kind of stumbled upon it. Because I never worked anywhere, the only models I had was Warren and Charlie. I just looked at how did Warren run his partnership? I set up the partnership the same way. How do they run their life? Oh, if you look at Warren Buffett's calendar, it's completely empty. Let's keep it empty and let's do things that are fun. I think, the reason I'm doing this talk is because it's fun. Number one, it's fun. That has to be fun. Number two, I want to get better at the multi-bagger. I'm using you guys to pound into my brain to be even more patient, to be patient for 20 years. I never held a stock except that one stock by accident for 20 years. I want to

hold something for 20 years and get a hundred x on it. I want to do that, and it'll show up. It might show up when I'm 60, and we'll hold it till we are 80, and I hope that happens.

Student 1: I have another question on your opinion on the differences between value investor and strategic investor. We noticed that many Chinese companies took equity of overseas companies to help them go into China. Like the China Foshan took equity of Climate Le Meridian. Climate the very big tour tourist and hotel group and help Chinese customers have access to those hotels. China acquires many good film companies in Hollywood. Of course, they make a lot of money in China's film industry. We often typically assume that a value investor is an outsider of the business. They don't want to do anything to help the business. What's your opinion on being a value investor or being a strategic investor? Do you think it will get information on the movement or the action of the strategic investor and go behind with them, like follow their equity taking?

Mohnish: That's a good question and a question I've never thought about before. It's a good question to ask because at least I can think about it and I'll mumble some answers right now. But maybe I'll think about it some more and next year I might have a better answer. Buffett says that "I'm a better investor because I'm a businessman and I'm a better businessman because I'm an investor". There is clearly an interplay and advantage on those. One of the things that happens with entrepreneurs or CEOs who are running specific businesses is they have two things going on. One is, usually their circle of competence is limited to that business. If they're in the hotel business, they understand the hotel business. If they're in the shipping business, they understand the shipping business and that competence can be an advantage because if they understand the movie business in China, they probably have a better shot at understanding the movie business in the US than a person who's not in the business at all.

Domain knowledge is a huge advantage. The disadvantage that strategic investors normally have is they may not understand, or they may not have a good understanding of value investing. For example, a lot of companies buy back their own stock. Now, if you're in the hotel business, it means you understand the hotel business, it means that you should understand when it is undervalued and when it is overvalued. Most company CEOs are not good at understanding when their businesses are undervalued. One of the reasons they don't understand that is because if you are going to be a great leader, you have to be an optimist and you have to be a builder. You always see the grasses green on the other side and value investors are always skeptical. They're always looking for what is wrong.

One of the reasons I sold all these companies much sooner than I should have is because I'm always skeptical about what might go wrong, for example. There are different skill sets. If you have some data which tells you that the CEO of the film company in China is a good capital allocator, then that can be a huge tailwind if you have some data that tells you that. The thing that you have to

evaluate is, are they good capital allocators? Then those are rare. For example, obviously Warren Buffett is good at buying companies. John Malone is good buying companies. Sam Zell is good at buying companies. But lots of the Japanese came into the US markets in the 1980s and they bought all kinds of real estate, trophy real estate all over the country, and they grossly overpaid for it because they looked at their experience in Japan where these properties are much more valuable because they were in a bubble.

They misunderstood what proper valuations were, and they didn't do well, even though they understood real estate in their own country. I think that it's a good idea to follow the strategic investors into other markets. If you can figure out whether they are value guys, they understand value. For example, the deal for Starwood, I forget the name of the Chinese company, the insurance company that was chasing starboard. Charles Starboard is a very prime asset. It's a great asset, but I don't know enough to know whether that would or would not have been a good deal for them. They were clearly paying up significantly more than what the market had priced that company. You would have to understand how those people think and whether they think correctly.

Professor: Other questions? Okay. Alright, well, It's almost two hours. We'll leave 20 minutes for internet discussion to absorb what you said. Today is a great lecture, we have recorded it and myself will have to listen to it again. It's motivating, makes me think about the change of career. Right?

Mohnish: Right. Yeah, and I enjoyed it very much as well, and I look forward to seeing you guys in person next year. Even if you're not in the class, maybe you can ask the professor to let you in.

Professor: Yeah. Everybody's welcome to this class. When you come next year, he'll still be here. Most of them are not graduating. We have also recorded this lecture. We will send you and you should tell us which editor you are using so we can ask him or her to edit this lecture according to instruction. I'll put it on the YouTube in China's version. That will get a better audience. Yeah. Great.

Mohnish: Thank you very much. It was a lot of fun.

Professor: Yeah. Well, timely will see you in person next year.

Mohnish: That sounds great. All right. Bye.

Professor: Enjoy. Good evening. We give you a good applause. Yeah.

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