

Yes, but I Like to Punt!

by Mohnish Pabrai

I was having a conversation with a friend of mine from Australia explaining some of Buffett's investing principles and he interrupted me and said: "***Yes, but I Like to Punt!***" Talking Aussie, he was referring to the moon-shot based model of investing. If it goes well, you have an astronomical return, but if it goes poorly then not much of your principal is left for the next punt. I responded, "*Yes, but punting is a Buffett violation. No punting allowed*".

David had heard the term "Buffett Violation" more than a dozen times during our week together in Boston and asked if I would write down these so called Buffett Violations for him. So, this "cheat sheet" is for David – and if you happen to derive some benefit, that makes it all the more worthwhile. I look upon his simple quotes as the laws of investing, business and life. They are as fundamental as the Laws of Physics.

1. On Punting

- "*Rule No. 1: Never Lose Money. Rule No. 2: Never Forget Rule No. 1*"
(1996)
- "*We're perfectly willing to trade off a big payoff for a certain payoff*"

Both statements are profound. When Buffett ran his private partnerships in the 1956-69 time frame, he ran a very focused portfolio of under 20 stocks at all times. Yet his biggest realized loss amounted to a loss of less than 0.5% of the portfolio. The fixation on first evaluating the downside before looking at the

upside is the reverse of punting. This is not a game of trying to hit a bunch of home runs with wild swings. It is diametrically opposed to the early-stage venture capital approach.

2. On When to Invest

- *“Be Fearful when the World is Greedy and Be Greedy when the World is Fearful.”*

In 1973, Buffett, reflecting on the unbelievably high-priced stock market, wrote:

- *“I feel like an oversexed man on a desert island.”*

In 1974, Buffett, reflecting on the ultra value priced stock market, wrote:

- *“I feel like an oversexed man in a harem.”*
- *“We don't get paid for activity, just for being right. As to how long we'll wait, well we'll wait indefinitely.”*

3. On Sticking to One's Circle of Competence in Investing

- *“Its not important how big one's circle of competence is; knowing its boundaries, however, is critical.”*
- *“I don't try to jump over 7-foot bars: I look around for 1-foot bars that I can step over.”* (1995 Berkshire Annual Meeting)
- *“The key to investing is not assessing how much an industry is going to affect society, or how much it will grow, but rather determining the competitive advantage of any given company and, above all, the durability of that advantage. The products or services that have wide, sustainable moats around*

them are the ones that deliver rewards to investors.” (Fortune, 1999)

4. On Capital Allocation:

- *“We’re not in the steel business, per se. We’re not in the shoe business, per se. We’re not in any business, per se. We’re big in insurance, but we’re not committed to it. We don’t have a mind-set that says you have to go down this road. So we can take our capital and move it into businesses that make sense.” (1995, addressing MBA Students at The University of North Carolina, Chapel Hill)*

It is indeed stunning to hear a Fortune 50 leader and head of one of the largest insurance operations in the world say that they are not committed to insurance! It is a deep statement that every CEO needs to understand.

- *“I am a better investor because I am a businessman and I am a better businessman because I am an investor.”*

CEOs who are good investors and Fund Managers who’ve run a business or two will do better for their shareholders and investors respectively. The cross-pollination impacts are huge – as suggested by Charlie Munger’s Latticework of Mental Models.

5. On The Importance of Investing in Good Businesses

- *“When a management team with a reputation for brilliance joins a business with poor fundamental economics, it is the reputation of the business that remains intact”*

Buffett has a very specific definition of a great business and these great businesses continue to thrive – even with mediocre management.

6. **On The Efficient Market Theory**

- *“I’d be a bum on the Street with a tin cup if the market were always efficient.”*
(Fortune, 1995)

Markets are mostly efficient, but not fully efficient. There is a huge difference between “mostly” and “fully”. In the case of Buffett, this difference is about \$31 Billion.

7. **On being (in)active in the Management of Acquired Businesses**

In 1991, referring to the CEOs of Berkshire’s various businesses, Buffett said in Outstanding Investor Digest:

- *“If they need my help to manage the enterprise, we’re probably both in trouble.”*

8. **On Investment Bankers and other Middle Men:**

- *“My idea of a group decision is looking in the mirror”*
- *“Never ask your barber if you need a haircut.”*

CEOs routinely seek advice from prominent investment banks like Goldman, Merrill, Morgan etc. on whether a particular M&A transaction makes sense. The economics for the banks is simple: they make X if there is no deal and 20-100X if there is a deal. What do you think their advice usually is? Berkshire Hathaway

virtually NEVER engages an investment bank to “advise” it on a transaction. The advice to CEOs role of investment banks in corporate America is fatally flawed.

9. On who you choose to work with:

In 1985, when a graduate student sought job counseling, Buffett said:

- *“I believe in going to work for businesses you admire and people you admire. Anytime you’re around somebody that you’re getting something out of and you feel good about the organization, you just have to get a good result. I advise you never to do anything because you think its miserable now, but it’s going to be great 10 years from now, or because I’ve got X dollars now, but I’ll have 10X. If you’re not enjoying it today, you’re probably not going to enjoy it 10 years from now.”*
- *“I choose to work with every single person I work with. That ends up being the most important factor. I don’t interact with people I don’t like or admire. That’s the key. It’s like marrying.”* (1989, Fortune Magazine)

To conclude, I’d like to emphasize that there is a large body of Buffett’s writings from 1956 to 2002 and hundreds of hours of sage advice he’s given at various Q&A sessions like the Berkshire Hathaway annual meeting that are impossible to encapsulate in a few paragraphs. So this is not even the Cliff Notes version. The interested reader should go straight to the source and start by reading all his Letters to Shareholders of Berkshire for the last 2 decades (posted on the website www.berkshirehathaway.com). Finally, I was unable to find sources on all the quotes, but believe they are accurate.

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