

Strategy & Corporate Finance Practice

Warren Buffett: An appreciation

As Warren Buffett turns 90, the story of one of America's most influential and wealthy business leaders is a study in the logic and discipline of understanding future value.

by Tim Koller



Patience, caution, and consistency. In volatile times such as these, it may be difficult for executives to keep those attributes in mind when making decisions. But there are immense advantages to doing so. For proof, just look at the steady genius of now-nonagenarian Warren Buffett. The legendary investor and Berkshire Hathaway founder and CEO has earned millions of dollars for investors over several decades (exhibit). But very few of Buffett's investment decisions have been reactionary;

instead, his choices and communications have been—and remain—grounded in logic and value.

Buffett learned his craft from “the father of value investing,” Columbia University professor and British economist Benjamin Graham. Perhaps as a result, Buffett typically doesn't invest in opportunities in which he can't reasonably estimate future value—there are no social-media companies, for instance, or cryptocurrency ventures in his

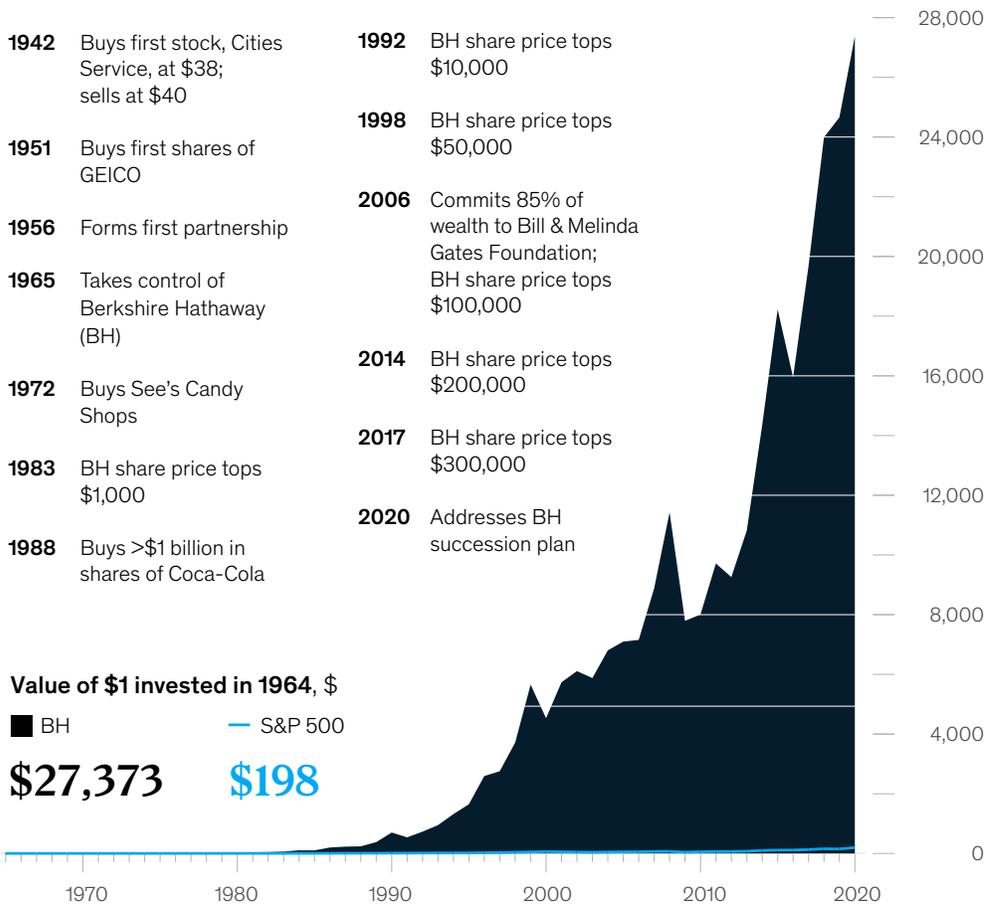
Exhibit

Warren Buffett's decisions, grounded in logic and value, have earned millions of dollars for investors.

Timeline of Warren Buffett's career

- 1942** Buys first stock, Cities Service, at \$38; sells at \$40
- 1951** Buys first shares of GEICO
- 1956** Forms first partnership
- 1965** Takes control of Berkshire Hathaway (BH)
- 1972** Buys See's Candy Shops
- 1983** BH share price tops \$1,000
- 1988** Buys >\$1 billion in shares of Coca-Cola

- 1992** BH share price tops \$10,000
- 1998** BH share price tops \$50,000
- 2006** Commits 85% of wealth to Bill & Melinda Gates Foundation; BH share price tops \$100,000
- 2014** BH share price tops \$200,000
- 2017** BH share price tops \$300,000
- 2020** Addresses BH succession plan



Source: CNBC

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portfolio. Instead, he banks on businesses that have steady cash flows and will generate high returns and low risk. And he lets those businesses stick to their knitting. Ever since Buffett bought See's Candy Shops in 1972, for instance, the company has generated an ROI of more than 160 percent per year¹—and not because of significant changes to operations, target customer base, or product mix. The company didn't stop doing what it did well just so it could grow faster. Instead, it sends excess cash flows back to the parent company for reinvestment—which points to a lesson for many listed companies: it's OK to grow in line with your product markets if you aren't confident that you can redeploy the cash flows you're generating any better than your investor can.

As Peter Kunhardt, director of the HBO documentary *Becoming Warren Buffett*, said in a 2017 interview, Buffett understands that “you don't have to trade things all the time; you can sit on things, too. You don't have to make *many* decisions in life to make a lot of money.”² And Buffett's theory (roughly paraphrased) that the quality of a company's senior leadership can signal whether the business would be a good investment or not has been proved time and time again. “See how [managers] treat themselves versus how they treat the shareholders ... The poor managers also turn

out to be the ones that really don't think that much about the shareholders. The two often go hand in hand,” Buffett explains.³

Every few years or so, critics will poke holes in Buffett's approach to investing. It's outdated, they say, not proactive enough in a world in which digital business and economic uncertainty reign. For instance, during the 2008 credit crisis, pundits suggested that his portfolio moves were mistimed, he held on to some assets for far too long, and he released others too early, not getting enough in return. And it's true that Buffett has made some mistakes; his decision making is not infallible. His approach to technology investments works for him, but that doesn't mean other investors shouldn't seize opportunities to back digital tools, platforms, and start-ups—particularly now that the COVID-19 pandemic has accelerated global companies' digital transformations.⁴

Still, many of Buffett's theories continue to win the day. A good number of the so-called inadvisable deals he pursued in the wake of the 2008 downturn ended paying off in the longer term. And press reports suggest that Berkshire Hathaway's profits are rebounding in the midst of the current economic downturn prompted by the global pandemic.⁵

¹ Theron Mohamed, “Warren Buffett's favorite business is a little chocolate maker with an 8000% return. Here are 5 reasons why he loves See's Candies,” *Markets Insider*, July 12, 2019, markets.businessinsider.com.

² “Peter Kunhardt,” *Charlie Rose*, January 31, 2017, charlierose.com.

³ Tae Kim, “Warren Buffett on judging management: ‘See how they treat themselves versus how they treat the shareholders,’” *CNBC*, May 9, 2018, cnbc.com.

⁴ Esther Shein, “COVID-19 is ‘the digital accelerant of the decade,’ forcing businesses to adapt quickly,” *TechRepublic*, July 15, 2020, techrepublic.com.

⁵ Geoffrey Rogow, “Berkshire Hathaway's profit jumps on market rebound,” *Wall Street Journal*, August 8, 2020, marketwatch.com.

At age 90, Buffett is still waging campaigns—for instance, speaking out against eliminating the estate tax and against the release of quarterly earnings guidance. Of the latter, he has said that it promotes an unhealthy focus on short-term profits at the expense of long-term performance. “Clear communication of a company’s strategic goals—along with metrics that can be evaluated over time—will always be critical to shareholders. But this information . . . should be provided on a timeline deemed appropriate for the needs of each specific

company and its investors, whether annual or otherwise,” he and Jamie Dimon wrote in the *Wall Street Journal*.⁶

Yes, volatile times call for quick responses and fast action. But as Warren Buffett has shown, there are also significant advantages to keeping the long term in mind, as well. Specifically, there is value in consistency, caution, and patience and in simply trusting the math—in good times and bad.

⁶ Jamie Dimon and Warren E. Buffett, “Short-termism is harming the economy,” *Wall Street Journal*, June 6, 2018, wsj.com.

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