Key Questions

Can Buffett's Strategy be Replicated?

by Samuel Snyder, Equity Research Analyst, Key Private Bank

We believe it is important that investors play their own game.

This past week, we had the opportunity to make the pilgrimage to Berkshire Hathaway's annual shareholders' meeting in Omaha with over 40,000 of our best friends, and a few new faces. After waking up well before dawn to secure our seats, we cracked open our notebooks to glean slivers of wisdom from Berkshire's Chairman, Warren Buffett ("the Oracle") and Vice Chairman, Charlie Munger. In five hours of Q&A, we gained an even better understanding of Berkshire's philosophy and what makes Mr. Buffett and Mr. Munger so special. With many revelers in the crowd asking if Berkshire (or any investor) could continue to replicate Buffett's performance, we thought it would be worthwhile to discuss this topic. The answer, in short, is no.

First, we must go back before Buffett, to his mentor, Benjamin Graham. In 1949, Mr. Graham authored The Intelligent Investor, which served as a collection of guiding principles for Buffett. Graham's approach led Buffett to what he later called "cigar butt investing": buying bad businesses at low prices. Several decades after Buffett's initial success, Charlie Munger lead a migration in strategy from buying bad businesses at low prices, to buying good businesses at low prices. While Munger's approach seems like a no-brainer, relative to bad businesses, quality companies tend to be more expensive. Buffett and Munger have somehwat embraced the idea that "you get what you pay for", a view we subscribe to at Key Private Bank.

Interestingly, during the Q&A session, Buffett noted that Ben Graham's approach was very novel when it was introduced providing him with an important investing edge. Given Buffett's early success, many investors followed suit and attempted to replicate his strategy which eroded Buffett's edge over time. This, in our view, is precisely why Berkshire embraced Munger's approach of buying higher quality businesses at low prices. However, we suspect that as time goes on, Munger's strategy will be replicated by market participants and his edge will, once again, be eroded away.

At another point during the Q&A, when asked if investors can expect Berkshire to perform similarly in the future, Munger and Buffett both said "no", and we tend to agree; Ajit Jain and Greg Abel will certainly have their work cut out for themselves as the heirs-apparent to Buffett and Munger.

In sum, as investors, having an edge remains crucial to success. Once an edge is developed, defending it is paramount. Furthermore, as we have stated in previous articles, we believe it is important that investors "play their own game" and invest based on their own principles versus blindly replicating someone else's. We think the Oracle would surely agree.

For questions, please contact your Key Private Bank Portfolio Manager.

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