MONEY & INVESTING

A Few Lessons for Investors and Managers from Warren Buffett

by Peter Bevelin (editor)

Buffett's own words, sorted into short lessons: how to judge a business, its managers, and its price.

BEST POINTS FROM THE BOOK

01 **Think like an owner, not a trader: run every decision as if you owned 100% of the business, it was your family's only asset, and you could not sell it for a century.**

That is Buffett's own test in the book. It kills short-term thinking and forces you to judge a share as a piece of a real business, not a blinking price.

02 **Investing means laying out cash today to get more cash back in the future. Speculation is most dangerous when it looks easiest.**

If the plan depends on reselling to someone who will pay more tomorrow, it is not investing. Easy money and excitement are warning signs, not opportunities.

03 **Price is what you pay. Value is what you get.**

A business is worth the cash it will produce over the rest of its life. Follow the cash, distrust rosy forecasts and accounting jargon, and treat the market's quote as an offer, not a verdict.

04 **Judge a business by the cash it generates for each dollar invested inside it.**

Return on tangible invested capital reveals a business's true character. The best businesses turn every dollar invested in them into substantially more than a dollar of value.

05 **Great businesses sit behind a moat. Beware the 'Roman Candles' whose moats prove illusory.**

A real moat - a strong brand, low costs, loyal customers - keeps competitors away, and it should widen a little every year. In commodity businesses, being the low-cost producer is all that matters.

06 **Businesses come in three kinds: the great, the good, and the gruesome.**

The great earn high returns on capital behind a durable moat. The gruesome devour cash, demand that you be smart every day, and live in fast-changing industries - get into a good business rather than trying to look brilliant in a bad one.

07 **In business, the rear-view mirror is always clearer than the windshield.**

Past results are sometimes a useful guide and sometimes a dangerous one. A track record only counts if the conditions that produced it are still in place.

08 **Hire for brains, passion, and integrity - then manage little.**

Buffett puts his trust in people rather than process. Ability without integrity is a liability, and the right people, trusted and left alone, get extraordinary results by doing ordinary things exceptionally well.

09 **You get what you reward for - so fix the yardstick before judging the performance.**

Decide in advance exactly which result counts, measure it clearly, and pay for that result. Reward the wrong number and even honest managers will deliver the wrong number.

10 **Dumb acquisitions cost owners far more than most other things.**

Before any deal, compare it with every other use of the money - including doing nothing. Most takeovers are bought with ego and hope, and the owners pay for them for decades.

11 **Act only when you have an edge, and always demand a margin of safety.**

Know what you understand and stay inside it; the gap between the price you pay and the value you get is your protection against being wrong. Big opportunities are rare - when it is raining gold, reach for a bucket, not a thimble.

12 **Prevention is better than cure.**

Keep it simple, use debt sparingly, ignore forecasts and fads, and treat market swings as a tool, not a guide. Mistakes will still happen - so do the postmortem, and learn most lessons from the experiences of others instead of paying for your own.

THE BOOK, IN SHORT

The premise is in the opening line: 'I am a better investor because I am a businessman and a better businessman because I am an investor.' Peter Bevelin, author of Seeking Wisdom, selected Warren Buffett's own words from decades of Berkshire Hathaway letters and talks and arranged them into fifteen short lessons. Buffett endorsed the result in his 2011 shareholder letter, saying it sums up what he and Charlie Munger had been saying over the years about Berkshire's investment and operating principles.

The investing lessons start with a definition: investing means laying out cash now in order to get more cash back later; anything else is speculation. A business is worth all the cash it can be expected to produce over its remaining life, so the investor's job is to follow the cash, keep estimates rough and honest, and never confuse the market's price with that value. Price is what you pay; value is what you get.

Business quality is measured by return on tangible invested capital - how much cash a business generates for each dollar tied up inside it. Buffett sorts businesses into the great, which earn high returns protected by a widening moat; the good, which earn solid returns on capital; and the gruesome, which are capital-hungry and low-return and punish their owners for years. And since the rear-view mirror is always clearer than the windshield, past results are a guide only when the conditions behind them still hold.

Much of the book is about people and how they are judged. Managers are chosen for brains, passion, and integrity, then trusted and left alone - hire well, manage little. A board's real job is to get the right person running the business. Owners are treated as partners, performance is graded against clear yardsticks set in advance, and pay follows one rule: you get what you reward for.

The closing lessons are about avoiding ruin. Dumb acquisitions destroy more owner wealth than almost anything else, so every deal must first beat the alternative of doing nothing. Risk is handled by prevention: stay inside what you understand, buy only with a margin of safety, borrow little, and ignore forecasts, fads, and market moods. The final chapter admits mistakes will still happen - and prescribes postmortems, so you learn most of your lessons from the experiences of others.

DO THIS WEEK

This week, run Buffett's owner test on one company you own, follow, or work for. On one page write: (1) how much cash it generates for each dollar invested inside it, (2) its moat - and whether that moat is widening, (3) whether its managers show brains, passion, and integrity, and (4) its value versus its price - is there a real margin of safety? Any line you cannot answer is your circle-of-competence answer: do not buy.

Compiled by Peter Bevelin from Warren Buffett's own words, first published 2012 (PCA Publications, 81 pages). Buffett praised it in his 2011 shareholder letter as a summary of Berkshire's principles. Read it for Buffett's core rules, short and direct.