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For Buffett, the Long Run Still Trumps the Quick Return

BY ANDREW ROSS SORKIN

Donald Bowers/Getty Images for FortuneWarren Buffett at a New York book party for "Tap Dancing to Work," by Carol Loomis.

"If somebody bought Berkshire Hathaway in 1965 and they held it, they made a great investment — and their broker would have starved to death."

Warren E. Buffett was sitting across from me over lunch at a private club in Midtown Manhattan last week, lamenting the current state of Wall Street, which promotes a trading culture over an investing culture and offers incentives for brokers and traders to generate fees and fast profits.

"The emphasis on trading has increased. Just look at the turnover in all of the stocks," he said, adding with a smile: "Sales people have forever gotten paid by selling people something. Generally, you pay a doctor for how often he gets you to change prescriptions."

Mr. Buffett, 82, is famous for investing in companies that he sees as solid operations and essential to the economy, like railroads, utilities and financial companies, and holds his stakes for the long run. The argument that the markets are better off today because of the enormous amount of liquidity in the stock market, a function of quick flipping and electronic trading, is a fallacy, he said.

"You can't buy 10 percent of the farmland in Nebraska in three years if you set out to do it," he said. Yet, he pointed out, he was able to buy the equivalent of 10 percent of I.B.M. in six to eight months as a result of the market's liquidity. "The idea that people look at their holdings in such a way that that kind of volume exists means that to a great extent, it's a casino game," he said. Of course, unlike many investors, he plans to hold his stake in I.B.M. for years.

Mr. Buffett was in a reminiscing mood about a bygone era, in part because he was in New York to make the rounds on television to discuss a new book chronicling his 61-year career, which began in 1951 at Buffett-Falk & Company in Omaha. (After lunch, he was going to visit "The Daily Show With Jon Stewart.")

The book, “Tap Dancing to Work,” by a longtime journalist and good friend of his, Carol Loomis of Fortune magazine, is a compendium of articles that she and others wrote in Fortune that creates a series of narratives spanning the arc of his career.

Ms. Loomis, who first met Mr. Buffett in 1967 — and whose long career is a story unto itself — also came to our lunch. Ms. Loomis may know more about Mr. Buffett than he knows about himself. (“There’s nothing here you’re going to like,” she said, after surveying the various pies when the dessert cart came around. She was right: he took a quick look and asked if they served ice cream. They did.)

As we talked about the “good old days” — he spoke of some of his early friends who were successful hedge fund investors, like Julian Robertson, who founded Tiger Management — it became clear that he was less enamored of the investor class of the next generation.

When I asked, for example, if there were any private equity investors that he admired, he flatly replied: “No.”

When I asked if he followed any hedge fund managers, he struggled to name any, before saying that he liked Seth Klarman, a low-key value investor who runs the Baupost Group, based in Boston.

“They’re not as good as the old ones generally. The field has gotten swamped, so there’s so much money playing and people have been able to raise money by just saying ‘hedge fund,’” he said. “That was not the case earlier on; you really had to have some performance for some time before people would put money with you. It’s a marketing thing.”

For a moment, he paused, and then posited that if he started a hedge fund today, “I’d probably grow faster, because a record now would attract money a lot faster,” speculating that his record of returns would attract billions of dollars from pension funds and others. But he then acknowledged a truism of investing that he knows all too well, as the manager of an enterprise that is now worth some $220 billion: “Then money starts getting self-defeating at a point, too.”

Until 1969, Mr. Buffett operated a private partnership that was akin in some ways to a modern hedge fund, except the fee structure was decidedly different. Instead of charging “2 and 20” — a 2 percent management fee and 20 percent of profits — Mr. Buffett’s investors “keep all of the annual gains up to 6 percent; above that level Buffett takes a one-quarter cut,” Ms. Loomis wrote. However, in 1969, he announced he would shutter his partnership. “This is a market I don’t understand,” he said, according to Ms. Loomis.

He believed that the stock market of 1968 had become wildly overpriced — and he was right. By the end of 1974, the market took a tumble. Instead, he remained the chief executive of Berkshire Hathaway, one of his early investments.

“If you want to make a lot of money and you own a hedge fund or a private equity fund, there’s nothing like 2 and 20 and a lot of leverage,” he said over a lunch of Cobb salad. “If I kept my partnership and owned Berkshire through that, I would have made even more money.”

Mr. Buffett says he now considered himself as much a business manager as an investor. “The main thing I’m doing is trying to build a business, and now we built one. Investing is part of it but it is not the main thing.”

Today, Mr. Buffett is particularly circumspect about the investment strategies that hedge funds employ, like shorting, or betting against, a company's stock. He used to short companies as part of a hedging strategy when he ran his partnership, but now he says that he and Charlie Munger, his longtime friend and vice chairman of Berkshire, see it as too hard.

"Charlie and I both have talked about it, we probably had a hundred ideas of things that would be good short sales. Probably 95 percent of them at least turned out to be, and I don't think we would have made a dime out of it if we had been engaged in the activity. It's too difficult," he explained, suggesting that the timing of short investments is crucial. "The whole thing about 'longs' is, if you know you're right, you can just keep buying, and the lower it goes, the better you like it, and you can't do that with shorts."

One of his big worries these days is about what's going to happen to all the pension money that is being invested in the markets, often with little success, in part because investors are constantly buying and selling securities on the advice of brokers and advisers, rather than holding them for the long term. "Most institutional investors, whoever is in charge — whether it's the college treasurer or the trustees of the pension fund of some state — they're buying what they're sold."

Most pension funds probably didn't buy Berkshire in 1965 and hold it, but if they had, they would have far fewer problems today. At the end of her book, Ms. Loomis notes that when she mentioned Mr. Buffett's name for the first time in Fortune magazine in 1966 — accidentally spelling Buffett with only one "t" — Berkshire was trading at $22 a share. Today it is almost $133,000 a share.