NOTES

How did Warren Buffet design Berkshire?

1. Continuous maximization of rationality, skills, and devotion of the most important people in the system, starting with himself.

2. Create win/win results everywhere. For example, in gaining royalty by giving it.

3. Make decisions that maximize the long-term results, and seek those decision makers who usually stayed long enough in place to bear the consequence of decisions.

4. Minimize the bad effects that inevitably come from a large bureaucracy at headquarters.

Case Study: Buffett's Early Investment in a Tab Card Company

- What is a tab card? Before computers were digital, they read off of punch cards. They were called Mark-Sense Cards, and these were big decks of cards with holes punched in them and they would be stuck in the computer, and they would be read mechanically through the computer.

- The company, Data Documents, was a start-up specializing in tab cards. At the time, punch card printing was IBM's most profitable business due to the high markup on these essential computer supplies. Data Documents realized that by investing in printing presses and operating closer to their customers to reduce shipping times, they could have an edge in the market

- The founders offered Buffett a 16% equity stake in exchange for funding one printing press, but he declined. His decision wasn't because it was a technology company, but because of his investment philosophy. Like a horse handicapper, Buffett asked, "What are the odds that this business could face a catastrophic risk that could cause it to fail?" He concluded that a start-up competing with IBM was highly vulnerable and likely to fail.

- Over time, the business became highly profitable, making 35 million tab cards per month. The company needed more capital to grow their business so they went back to Buffett.

- Now Buffett was interested because the catastrophic risk was gone as they were competing successfully with IBM. Buffett asked for some numbers and was given the information that they were turning 7 times the capital. With each Carroll Press costing $78,000, made $11,000. Basically, their gross profit from the press could buy another one. At this point Buffett was very interested.

- Finally, Buffett asked for 15% on $2 million of sales. The company already had $1 million sales growing at 70% so there was a huge margin of safety. Buffett ended up putting 20% of his net worth on 16% of the company and some subordinated notes.

- The company was later bought out and Buffett earned 33% compounded return for 18 years.

- Lessons Learned:

    1. First step of the investment process is always to ask if the business is prone to catastrophic failure. Start with what could go wrong.
    2. Buffett never built financial models or relied on projections. Instead, he focused entirely on historical data, identifying one or two key factors that most impacted the business - much like a horse handicapper analyzing fact sheets. He gathered historical figures for the company and its competitors, studied them in depth, and used this to make a straightforward yes-or-no investment decision.
    3. He wants 15% day 1 return on investment and starts compounding from there. Not greedy and nothing fancy.

Revisiting one of Charlie Munger's sayings…

"You spend less than you earn. Invest shrewdly. Avoid toxic people and activities. Try to keep learning all your life. And do a lot of deferred gratification.

If you do all of those things, you are almost certain to succeed. And if you don't, you're going to need a lot of luck.

And you don't want a lot of luck. You want to go into a game where you're very likely to win without having any unusual luck."

What If I Was Starting Off with $1 Million by Guy Spier

- Make investments that cannot result in total loss but have a high probability of multiplying the initial capital. Embrace slightly more risk—aim for two bets per year

- Earn your journey: develop your unique approach to research and analysis.
- Utilize resources like Value Line, VIC, Seeking Alpha, the Zurich Project, and ValueX.
- Focus on sub-billion-dollar companies or small-cap stocks.
- Seek out special situations that create compelling valuation opportunities.

Richard Galanti, MBA '82 Arjay Miller CFO Award Winner by Stanford Graduate School

- When you try your best to save money for your customers, they try their best to make money for you.
- Always keep it simple. Do things that are only necessary.
- Maximized common sense.
  - Don't change something that works
  - Pay vendors on time and respect the deal at all times
  - Builds trust which in the long-term builds royalty
  - ...etc
- Be predictable in the paying and receiving of money. Costco is a book-value business that has to be a cash cow.
- Decisions made regarding aspects of businesses are talked about in an extremely simple manner. Nasdaq vs Nyse, Dividend, Buybacks, and others are all mostly 1 or 2 point decision making processes.

Special Situations by Hudson Value Partners

- Special situations are when the sum of the parts are worth more than the whole.
- There are number of cases where special situations are likely to emerge:
  - Merger Arbitrage

    The price discrepancy between market value and the deal price.
  - Bankruptcies, Liquidations, and Restructurings

    The price discrepancy between market value from these events and the actual value of the business.
  - Spinoffs and Divestments

    The price discrepancy caused by a downward pressure from either a) being the smaller player or b) having been underinvested or c) value hidden by being under the parent company.
  - Convertible Securities

    A conservative way to deploy capital to a business when special deal making is possible.
  - Warrants, Contingent Value Rights, and Long Dated Options

    Similar to CS but these are derivatives directly linked to an event.
- An investor should be equipped with foresights to identify these situations and invest accordingly. This is especially favourable for smaller capital pools as these situations are more common and under-researched.

Apollo Investor Day 2024 by Apollo Global Management

- After the Global Financial Crisis (GFC), Athene offered attractive yields to investors searching for them, enabling Apollo to outperform other alternative asset managers.
- The industrial sector, particularly energy, power, and digital infrastructure, is experiencing a significant demand-supply imbalance. Financing in this sector often requires long-term commitments, varied cost-of-capital structures, and flexibility in formats—conditions that traditional banks find challenging to meet. Moreover, these investments often lack an investment-grade rating, creating an opportunity for alternative asset managers to step in.
- In Australia, superannuation funds allow for investments across both private and public markets. This flexibility

addresses the significant demand for retirement products, which are primarily driven by investment-grade fixed income.

- Family offices allocate approximately 50% of their portfolios to private investments. Unlike institutional investors, they are not constrained by consultant-driven benchmarking and are free to tailor their strategies to their specific goals. This independence is a notable market signal.

- The traditional distinction between private (risky) and public (safe) markets is fading. The gap between investment-grade securities in private and public markets is narrowing, suggesting these distinctions may disappear entirely in the near future.

- Given that 90% of professionals fail to outperform market indices, it prompts the question: Is the underperformance due to declining skill levels or a fundamental shift in market structure? The latter appears more plausible.

- A shift from equity to private capital could reshape financial markets, particularly as Athene focuses on originating investment-grade fixed income assets. These assets exceed the yield of public fixed income, providing a competitive edge in origination capabilities.

Joel Greenblatt & Howard Marks Discuss Value Investing by Wharton School

- If you're in the right place, you only need to jump a one-foot hurdle. Focus on playing the games you excel at, so luck becomes less critical.

- Markets can be unpredictable, but solid valuation work is almost certain to align with the market's view over time—2 to 3 years is a reasonable horizon.

- Ask yourself if you truly enjoy reading 10-Ks. If you don't love the process, it’s not worth playing the game half-heartedly.

- Your largest position should be something you're confident won't lose money.

- Operating leverage matters because, in tough times, high fixed costs can become a liability. For example, Greenblatt cites renting trade show spaces—buying at $2/sqft and renting at $62/sqft works well until the trade show stops. Businesses with high operating leverage face significant risks when things go wrong.