



Book The Snowball

Warren Buffett and the Business of Life

Alice Schroeder
Bloomsbury, 2008
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Recommendation

Warren Buffett is “everyman” as multibillionaire. Despite his vast wealth, he has always eschewed ostentation. He pays himself about \$100,000 annually, which in today’s U.S. economy places him in the upper-middle-class. He lives in the same simple Omaha, Nebraska, house that he bought in 1958 for \$31,500. He prefers an old gray suit to expensive London tailoring. In Buffett’s early days, when he was only a multimillionaire and not a multibillionaire, he walked around with holes in the soles of his shoes. To Buffett, wardrobe doesn’t matter; what matters is making money. He is better at this pursuit than anyone else in the world. In 2008, *Forbes* magazine ranked him as the globe’s richest man, with a net worth of \$62.3 billion. Author Alice Schroeder does a masterful job of chronicling Buffett’s improbable, inspiring life. As a former superstar research analyst, Schroeder uses her expert knowledge of finance and commerce to detail Buffett’s investment philosophy and business activities. *BooksInShort* praises Schroeder’s remarkable skills as a researcher and writer. Her book is packed with fascinating details and trenchant observations about the “Oracle of Omaha.” One of the best business biographies available, this book shows how the world’s greatest investor amassed the world’s greatest fortune, while staying true to his essential self.

Take-Aways

- As a boy, Warren Buffett dedicated himself to becoming rich.
- Now he has more money than anyone else on earth.
- Buffett earned his fortune by being superb at determining a company’s long-term value and earnings potential, his primary investment criteria.
- Buffett never lets the ups and downs of the stock market influence his investments.
- He is always suspicious of stock booms and seldom surprised by stock busts.
- Buffett carefully looks for undervalued companies.
- He avoids Wall Street, much preferring to operate from Omaha, Nebraska.
- Buffett set up his business affairs to operate with a tight center staff. This policy eases his mind about his responsibility to investors.
- Buffett is a complex man with simple taste, a conventional man who has led an unconventional life.
- Buffett plans to give the bulk of his massive fortune to charity.

Summary

The World’s Wealthiest Individual

Warren Buffett earned his vast fortune all by himself. Instead of living amid Wall Street’s bustle, Buffett lives and works in Omaha, Nebraska, a bucolic city in the U.S.

heartland. Throughout his career, backwater Omaha has been Buffett's base, though the rest of the business world sees it as a *déclassé* town of no special significance. To build his enormous wealth, Buffett exhaustively studied the stock market and the world of commerce, learning everything he could about individual companies, and their potential for growth and earnings. This hard-earned knowledge has been his guiding light and his path to becoming the richest man in the world.

“Warren Buffett was a man who loved money, a man for whom the game of collecting it ran in his veins as his lifeblood.”

Buffett's investment philosophy, adapted from his mentor, investment guru Benjamin Graham, is remarkably simple: Look for companies whose stock values are priced less than the organization's "intrinsic" value and invest accordingly. Buffett does not concern himself with the market's temporary ups and downs. He invests for the long term, focusing on companies' sound business fundamentals and capacity to generate superior earnings year after year. Through this straightforward process, he made his fortune. Of course, the "Oracle of Omaha's" legendary expertise in separating commercial winners from losers is much easier described than accomplished. How did Buffett become the world's best company evaluator and stock-picker?

“When Buffett walked into a room, the electricity was palpable. In his presence, people felt brushed by greatness. They wanted to touch him. They became dumbstruck before him, or babbled inane remarks.”

You can find the answer in his single-minded quest, from childhood, to become a millionaire. One of the earliest photographs of Buffett as a little boy shows him proudly holding his favorite toy, a nickel-plated change-maker, a small gizmo with four tubes that dispensed coins. As he grew up, Buffett zealously studied everything he could find about business and investing, including decades-old magazines and newspapers. That he far surpassed his initial financial goal is a testament to his prescience and steely-eyed focus, as well as to his idiosyncratic formula for financial achievement. His story is the classic American tale of hard work that pays off beyond all expectations. How the kid who wanted to make a million actually did that – and more – is a truly amazing tale.

The Early Years

The members of the Buffett clan were Nebraska tradespeople, straightforward, honest, no-nonsense types. Warren's father, Howard, worked in his own father's grocery store in Omaha before attending the University of Nebraska. After that, he sold insurance. In 1930, Howard's second son Warren Edward was born just at the start of the Great Depression. Soon after, Howard opened a stock brokerage, Buffett, Sklenicka & Co. To do so when people were shunning stocks took real courage. However, Howard's business was a winner from the start.

“Howard Buffett quickly gained a reputation as perhaps the least backslapping congressman ever to represent his state.”

A precocious toddler, Warren loved numbers and collecting things. His hobbies included counting and measuring. Of course, these interests would stand him in good stead. As a boy, Warren was a *bona fide* businessman. His first products were packs of gum, which he sold to his neighbors. Later, he sold golf balls that he retrieved from the lake at Omaha's Elmwood Park golf course. He also sold popcorn and peanuts at local football games. Warren saved every penny he made. Even as a youngster, Warren avidly read all the investment books and periodicals at his father's office. His favorite library book was *One Thousand Ways to Make \$1,000*. He studied it religiously. He vowed to himself that by age 35, he would be a millionaire.

“Since Warren looked at every dollar as \$10 someday, he wasn't going to hand over a dollar more than he needed to spend.”

During the 1940s, Howard, a rock-ribbed Republican, was elected to Congress. He and his family moved to Washington, D.C., where Warren entered junior high school and became a newspaper boy. In 1944, Warren submitted his first income tax return. By age 14, he had saved \$1,000. Through hard work, he doubled it and purchased a 40-acre tenant farm in Nebraska. As a teenager, Warren also went into the pinball business, buying and installing the machines in local barbershops. Additionally, he became a horse race handicapper, selling a tip sheet he entitled *Stable-Boy Selections*.

“He never hosted backyard barbecues, lazed around a swimming pool, stargazed or simply went for a walk in the woods. A stargazing Warren would have looked at the Big Dipper and seen a dollar sign.”

After high school, Warren briefly attended the University of Pennsylvania, which he did not like. He was shocked when Harvard turned him down. He got admitted to Columbia University, where he took classes with Benjamin Graham, the famous author of *The Intelligent Investor*. He quickly became Graham's star pupil. Warren read and memorized *Security Analysis*, the influential book Graham wrote with Columbia professor David Dodd.

“Buffett had a buoyant optimism about the long-term economic future of American business.”

By this time, Buffett was a regular investor on Wall Street. He focused on companies that kept costs low and always made money, such as GEICO, an insurance firm that sold policies over the telephone. Buffett initially bought 350 shares and later bought many more. After graduation, he returned to Omaha, where he sold stocks for his father's firm and taught investing at the University of Omaha. He married a sensitive, empathetic girl named Susan (“Susie”) Thompson. By 1951, Buffett's capital was \$19,738, which he invested and reinvested.

“The very mention that Buffett had bought a stock could, all by itself, move its price and revalue a company by hundreds of millions of dollars.”

He and Susie lived inexpensively on his earnings as a stockbroker and part-time teacher. This was not hard because Warren was quite cheap. He would wash his car only when it rained, so he could save on water. In 1953, Warren and Susie's first child, Susan Alice, was born. She became known as “Little Susie.” They later had two sons, Howard and Peter.

“Buffett's testimony in Congress as the reformer and savior of Salomon had turned him from a rich investor into a hero.”

In 1954, Buffett and his young wife moved to New York, where he went to work at Graham's investment firm, the Graham-Newman Corporation. He subscribed fully to Graham's investment philosophy of focusing on companies' net worth and purchasing stock in firms that Wall Street undervalued. Graham called such companies “cigar butts.” Buffett studied *Moody's* and *Standard & Poor's*, and “with his prodigious ability to absorb numbers and to analyze them,” he quickly became a sensation at Graham's firm, invariably recommending great buys. Buffett learned a valuable lesson about “capital allocation” – “placing money where it would earn the highest

return.” This became one of his bedrock investment principles. When Graham retired, he offered Buffett a partnership to keep him at the firm. But Buffett had come to New York to be close to Graham. With him gone, Buffett saw no reason to stay. He moved his family back to Omaha.

“Buffett would undertake almost anything from his short list of most-loathed tasks – get into an angry, critical confrontation; fire someone; cut off a long friendship carefully cultivated; eat Japanese food...almost anything – [rather] than make a withdrawal from the Bank of Reputation.”

Buffett Associates Ltd. By 1956, Buffett had \$174,000. Although only 26, he planned to retire and live off the investment income that he could make from his nest egg. He invited some friends and relatives to benefit from his investment expertise. Six initial partners joined the new Buffett Associates Ltd., including his father-in-law, Doc Thompson (\$25,000), his Aunt Alice (\$35,000), and his sister Doris and her husband (\$10,000). Buffett was the seventh partner. As a management fee, he charged his new partners “half the upside above a 4% threshold.” He also “took a quarter of the downside.” Soon others joined the partnership, which made money rapidly. Buffett set up numerous additional partnerships with other investors, including attorney Charlie Munger, who also operated his own investment firm. He eventually became Buffett’s primary partner. By now Buffett was making a large return from each partnership. He constantly reinvested his earnings, so his wealth kept increasing. Indeed, Buffett’s “snowball” was starting to grow substantially.

“In the short run, the market is a voting machine. In the long run, it’s a weighing machine.”

Buffett was managing more than a million dollars a year by 1958. His goal was to outperform the Dow by 10% annually. He was doing so well he no longer recruited new partners. Now someone who wanted his investment advice had to solicit him. In 1962, Buffett merged his partnerships into Buffett Partnership Ltd. (BPL), with assets of \$7.2 million. Buffett was now a millionaire. His early \$3 million investment in American Express paid handsomely, but his investment in Berkshire Hathaway, a New England textile firm, initially did not. In 1962, he bought 2,000 shares of Berkshire at \$7.50 per share. Then he bought more. Eventually, he bought the company, as well as the Blue Chip Stamps Company, Illinois National Bank and Trust Company of Rockford, Sun Newspapers in Omaha, See’s candy company and, over time, many more.

San Francisco Susie

While Buffett made himself and his partners wildly rich, Susie became socially active on behalf of Omaha’s poor black community. She also became a part-time singer, making a separate life for herself though remaining deeply supportive of her husband. By 1966, Buffett’s wealth totaled nearly \$10 million, but Berkshire Hathaway was now “on life support.” He tried to sell it to Charlie Munger. But Munger, who deeply respected Buffett’s investment acumen, had no interest in owning a firm Buffett did not want. Eventually, Buffett closed the Berkshire Hathaway plant and laid off the workers. From then on, Berkshire Hathaway became Buffett’s holding company, his main corporate enterprise. By 1974, Buffett, with his many companies, was a business mogul, although a small one. By 1977, his wealth surpassed \$70 million. He was only 47. But Susie wanted more. By this time she had moved to San Francisco, where she now lived alone. She loved her husband, but wanted a life outside Omaha. Warren and Susie remained devoted, and talked daily on the phone. In 1978, at Susie’s urging, Astrid Menks, age 32, began to take care of Buffett, eventually moving in with him. The arrangement was an unusual triangle, but Buffett never felt the need to explain it to anyone. It worked well for all the parties concerned.

Richer and Richer

As the years progressed, Buffett continued to expand his fortune, along with those of his partners and fellow investors. By 1980, when Buffett was 50, Berkshire Hathaway was listed for \$375 a share. By 1983, the Buffetts were worth \$680 million and he was a billionaire by 1985. In 1987, Berkshire Hathaway traded at \$2,950 per share and Buffett was worth \$2.1 billion, making him the ninth-richest person in the United States. By 1991, he was the second richest, with a net worth of \$3.8 billion. Buffett’s initial partners each had made \$3 million for every \$1,000 they originally invested with him. Year after year, Buffett’s fortune (his “snowball”) grew exponentially. By 2008, he was the richest man in the world. Throughout his climb, he watched his expenses and invested carefully, always investing his profits and letting his funds appreciate at compound interest. Buffett never allowed the fickle stock market to dictate to him, particularly when it plunged into high tech. He freely admitted he didn’t understand it, saying, “The software business is not within my circle of competence...We understand Dilly Bars and not software.” Thus, he avoided high tech’s bubbles, booms and busts. Instead, Buffett dictated to the market.

The Salomon Brothers Debacle

Buffett loved money, but he loved his hard-won reputation for honesty even more. In 1991, Salomon Brothers – a Wall Street investment bank in which Buffett and Berkshire Hathaway had a \$700 million investment – tested his reputation. A Salomon executive, Paul Mozer, had engaged in a series of rule-breaking bids in his dealings with the U.S. Treasury. News of his violations hit Wall Street, which went into a fury. It turned out that other Salomon executives, including CEO John Gutfreund, had known of Mozer’s misdeeds. This implicated the firm in the scandal. Gutfreund, who should have fired Mozer and didn’t, had to resign. Salomon’s stock nosedived.

“Balzac said that behind every great fortune lies a crime. That’s not true at Berkshire.” (Buffett)

During this rough period, Buffett put his reputation on the line by assuming the post of Salomon’s interim chairman. He was known worldwide for his probity, honesty, openness and integrity. Thus, his willingness to rescue Salomon Brothers saved it from declaring bankruptcy. During Buffett’s testimony before the U.S. Congress about this affair, he said he had told Salomon’s executives, “Lose money for the firm, and I will be understanding. Lose a shred of reputation for the firm, and I will be ruthless.”

Family Matters

In 2004, Buffett’s beloved wife Susie died of a cerebral hemorrhage. Two years later, he married Astrid Menks, his longtime live-in companion. Also in 2006, Buffett announced that he planned to give away his Berkshire Hathaway stock, valued at \$37 billion. He stated his intention to donate some 83% of it to the Bill and Melinda Gates Foundation “for the betterment of the world.” Buffett did not ask the Gates Foundation to memorialize him. He made only one precondition: It should spend the money quickly to help people in distress.

About the Author

Alice Schroeder, initially a CPA, became a respected research analyst. Impressed with her writing skills, Warren Buffett recommended that she become a full-time writer instead.
