

Miller, Jeremy – Warren Buffett's Ground Rules

Profile Books, 2016, [Equity Investing] Grade ★★★★★

I like this book. It's got a genuine and honest feeling. There are several dozens of books on Warren Buffett. What makes this one special or needed? All other texts on Buffett's methodology are based on how he has conducted his business at Berkshire Hathaway. However, before this Buffett managed money at Buffett Partnership Limited, with a different methodology and arguably with even better results. Investment analyst Jeremy Miller's book is unique as it covers this first period by going through the partnership's investment letters to its investors. The name *Warren Buffett's Ground Rules* refers to 7 rules that Buffett presented for the partnership's original investors and that were meant to facilitate aligned interests between them and him. In asset management having the right investors is a crucial success factor.

The book's structure is simple but well executed. Each chapter is dedicated to a theme. First the author presents the topic and what Buffett's view was. Then follows a number of quotes from the investment letters on the subject and the chapter ends with a short conclusion by Miller. Each chapter is 15-20 pages and as they are very legible it's easy to end up reading "just one more". The only objection is that there is a fair amount of repetition between the discussion and the quotes. The chapters are organized in three parts where the second part is the most interesting. The first part covers a number of introductory and high level topics like compounding, indexing and the partnership structure. The third also includes various topics that although often important and, as always when it comes to Buffett, brilliantly described are on a relatively high abstraction level and a bit dry. The middle part is dedicated to investing. This is where it becomes interesting.

It is relatively well known that the early Buffett was a deep value investor walking in the footsteps of his mentor Benjamin Graham. This indeed was the core strategy but Buffett's implementation was different than Graham's. Although the perception that Graham only saw to numbers and not to the

qualitative aspects of a business is false, most of his focus was still on low valuation multiples in combination with other financial ratios and he diversified broadly. Buffett was from the beginning a focus investor only holding a few of his best ideas in the portfolio and thus had to understand each company in depth.

Instead of diversifying over a large number of stocks the partnership diversified over three different and somewhat uncorrelated types of investment cases that they called Generals, Workouts and Controls – each requiring a different investment methodology. In modern terminology we would name the strategies deep value, merger arbitrage and activism. Generals, the bulk of the portfolio, were stocks that were cheap with regards to either their assets or earnings. Due to the much larger size of the Berkshire portfolio and cheered on by Charlie Munger, Buffett moved on from deep value to compounding franchise stocks. Interestingly this change was already underway in the latter part of the partnership years. The complementary merger arbitrage situations are quite traditional but display Buffett's statistical skills. Activism at its best is value investing with inbuilt triggers. Buffett held large positions in small companies where he saw opportunities for improvements and actively worked to make them happen. However, he didn't enjoy the human drama of activism and subsequently left the area.

Buffett might have been precocious but reading this book you realize that he didn't start out fully formed, he did his share of trial-and-error. Over the years I have picked up bits and pieces about these years. Here things fall into place and by this puts Buffett into perspective. What Lawrence Cunningham's bestseller *The Essays of Warren Buffett* has done for bringing Buffett's writing during the Berkshire era to the public, Jeremy Miller's thoughtful book now does for the writing of the partnership era. In combination they give a much fuller understanding of the phenomenon that is Warren Buffett.

Mats Larsson, September 11, 2016