7258 WEALTH
MANAGEMENT

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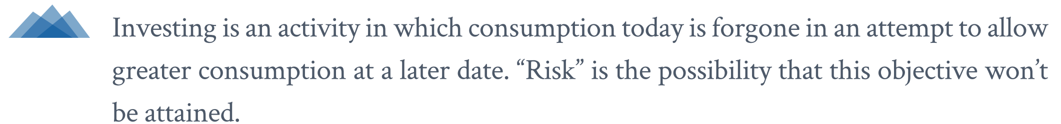
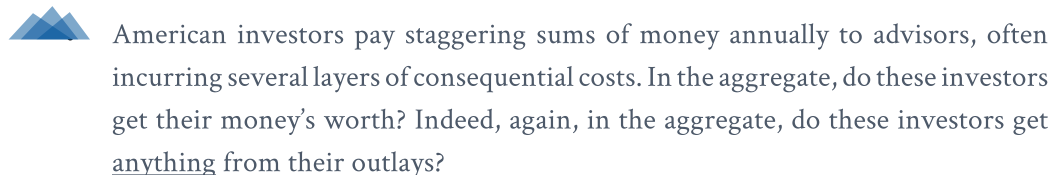
Golden Nuggets from the Oracle of Omaha

The text below was taken directly from the Berkshire Hathaway 2017 Chairman's Letter, written by Warren E. Buffett. The notes in italics below represent 7258's commentary.



Investing is an activity in which consumption today is forgone in an attempt to allow greater consumption at a later date. "Risk" is the possibility that this objective won't be attained.

While Wall Street largely defines risk as volatility of returns, 7258 has shared Mr. Buffett's view of risk since our firm's inception (https://www.7258wealth.com/our-clients-and-their-goals).



American investors pay staggering sums of money annually to advisors, often incurring several layers of consequential costs. In the aggregate, do these investors get their money's worth? Indeed, again, in the aggregate, do these investors get anything from their outlays?

Investors must consider the total cost of portfolio management: advisor fees, fund expenses, manager fees and tax costs – each of these can and should be controlled/considered. All too often, prospective clients ask about advisor fees and ignore the rest.

Berkshire shares have suffered four truly major dips. Here are the gory details:

PERIOD	HIGH	LOW	PERCENTAGE DECREASE
March 73 - January 75	93	38	(59.1)
10/2/87 – 10/27/87	4,250	2,675	(37.1)
6/19/98 – 3/10/00	80,900	41,300	(48.9)
9/9/08 – 3/5/09	147,000	72,400	(50.7)

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This table offers the strongest argument I can muster against ever using borrowed money to own stocks. There is simply no telling how far stocks can fall in a short period. Even if your borrowings are small and your holdings are not immediately threatened by the plunging market, your mind may well become rattled by scary headlines and breathless commentary. And an unsettled mind will not make good decisions.

In the next 53 years our shares (and others) will experience declines resembling those in the table. No one can tell you when those will happen. The light at any time can go from green to red without pausing at yellow.

The evidence suggests investors do not handle volatility well; many will sell into market weakness. While buying high makes people feel better, selling low is destructive to the accumulation of long-term wealth. The first week in February was a short test (more like a pop quiz) of an individual's ability to live comfortably with the amount of equity exposure in their portfolios.

Though markets are generally rational, they occasionally do crazy things. Seizing the opportunities then offered does not require great intelligence, a degree in economics or a familiarity with Wall Street jargon such as alpha and beta. What investors then need instead is an ability to both disregard mob fears and enthusiasm and instead to focus on a few simple fundamentals. A willingness to look unimaginative for a sustained period – or to even look foolish – is also essential.

There is no better example of this right now than people abandoning value stocks in favor of growth – just like they did in the late 90's. Note that the 98-00 pullback in Berkshire shares (see the table above) was not related to a bear market; this was primarily a result of the dot com bubble when value was out of favor. 2018 feels awfully similar to 98-00.

From Kipling's If:

"If you can keep your head when all about you are losing theirs . . .
If you can wait and not be tired by waiting . . .
If you can think – and not make thoughts your aim . . .
If you can trust yourself when all men doubt you . . .
Yours is the Earth and everything that's in it . . ."

Our favorite Buffett adage: be greedy when people are fearful; be fearful when people are greedy.

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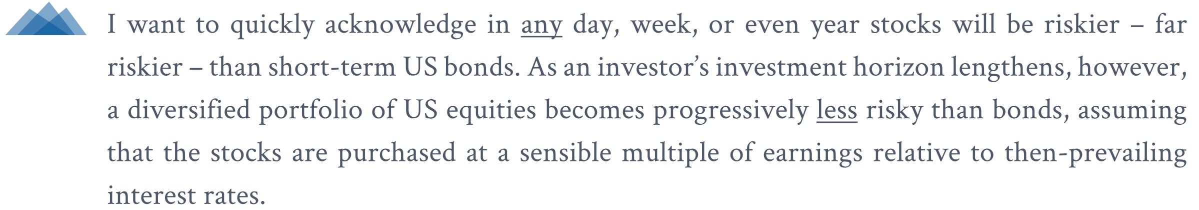

I want to quickly acknowledge in any day, week, or even year stocks will be riskier – far riskier – than short-term US bonds. As an investor's investment horizon lengthens, however, a diversified portfolio of US equities becomes progressively less risky than bonds, assuming that the stocks are purchased at a sensible multiple of earnings relative to then-prevailing interest rates.

While we have concerns about the equity markets, we completely agree with Mr. Buffett here. The question in our minds is whether the current market is trading at a sensible price-to-earnings multiple. Markets are certainly priced to perfection . . . but they've proven they can stay that way for long periods of time . . .until they aren't.

It is a terrible mistake for investors with long-term horizons – among them, pension funds, college endowments, and savings-minded individuals – to measure their investment "risk" by their portfolio's ratio of stocks to bonds. Often, high-grade bonds in an investment portfolio increase its risk.

Inflation has been benign for a long period of time and bonds aren't the best investment in an inflationary environment. The longer the time horizon, the higher the requisite equity exposure.

Performance comes, performance goes. Fees never falter.

Enough said.

The Berkshire Hathaway 2017 Annual Report can be found at: http://www.berkshirehathaway.com/2017ar/2017ar.pdf