

Mr. Market

INVESTMENT SUCCESS AND YOU

Warren Buffett's affection for Ben Graham, with whom he studied and worked early in his career, is seen again in this passage from the 1987 Annual Report of Berkshire Hathaway:

Whenever Charlie and I buy common stocks for Berkshire's insurance companies (leaving aside arbitrage purchases, discussed later) we approach the transaction as if we were buying into a private business. We look at the economic prospects of the business, the people in charge of running it, and the price we must pay. We do not have in mind any time or price for sale. Indeed, we are willing to hold a stock indefinitely so long as we expect the business to increase in intrinsic value at a satisfactory rate. When investing, we view ourselves as business analysts – not as market analysts, not as macroeconomic analysts and not even as security analysts.

Our approach makes an active trading market useful, since it periodically presents us with mouth watering opportunities. But by no means is it essential: a prolonged suspension of trading in the securities we hold would not bother us any more than does the lack of daily quotations on World book or Fehheimer. Eventually, our economic fate will be determined by the economic fate of the business we own, whether our ownership is partial or total.

Ben Graham, my friend and teacher, long ago described the mental attitude toward market fluctuations that I believe to be most conducive to investment success. He said that you should imagine market quotations as coming from a remarkably accommodating fellow named Mr. Market who is your partner in a private business. Without fail, Mr. Market appears daily and names a price at which he will either buy your interest or sell you his.

Mr. Market has another endearing characteristic: he doesn't mind being ignored. If his quotation is uninteresting to you today, he will be back with a new one tomorrow. Transactions are strictly at your

option. Under these conditions, the more manic depressive his behavior, the better for you.

But, like Cinderella at the ball, you must heed one warning or everything will turn into pumpkins and mice. Mr. Market is there to serve you, not to guide you. It is his pocketbook, not his wisdom, that you will find useful. If he shows up some day in a particularly foolish mood, you are free to either ignore him or to take advantage of him, but it will be disastrous if you fall under his influence. Indeed, if you aren't certain that you understand and can value your business far better than Mr. Market, you don't belong in the game. As they say in poker, "If you've been in the game 30 minutes and you don't know who the patsy is, you're the patsy."

Ben's Mr. Market allegory may seem out-of-date in today's investment world, in which most professionals and academicians talk of efficient markets, dynamic hedging and betas. Their interest in such matters is understandable, since techniques shrouded in mystery clearly have value to the purveyor of investment advice. After all, what witch doctor has ever achieved fame and fortune by simply advising "take two aspirins"?

The value of market esoterica to the consumer of investment advice is a different story. In my opinion, investment success will not be produced by arcane formulae, computer programs or signals flashed by the price behavior of stocks and markets. Rather an investor will succeed by coupling good business judgment with an ability to insulate his thoughts and behavior from the super contagious emotions that swirl about the marketplace. In my own efforts to stay insulated, I have found it highly useful to keep Ben's Mr. Market concept firmly in mind.

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