VGI PARTNERS

PRIVATE AND CONFIDENTIAL

14th February 2019

2019 DAILY JOURNAL ANNUAL SHAREHOLDERS' MEETING

"Part of our secret is that we don't attempt to know a lot of things. I have a pile on my desk that solves most of my problems. It's called the too hard pile. I keep shifting things to the too hard pile. Every once in a while, an easy decision comes along, and I make it. That's my system – everything is in the too hard pile except for a few easy decisions, which I make properly."

- **Charlie Munger, 14th February 2019**

We were fortunate to attend the 2019 Daily Journal Annual Shareholders' Meeting with its Chairman, Mr. Charles Munger. Mr. Munger (age 95) spoke for forty-five minutes before opening it up to the Q&A session, which lasted just over an hour and covered a range of topics.

An estimated 700 people attended the meeting this year in Downtown Los Angeles.

We believe the following notes are an accurate depiction of the meeting, however we have omitted discussions on topics unrelated to investing and business success.

We hope that you enjoy reading these notes as much as we enjoyed attending the meeting and putting them together!

****

Munger: As many of you have come from a great distance today, I'll speak briefly on a number of topics that may interest you and then I'm going to take questions.

It's amazing the number of people at the meeting of the little Daily Journal Corporation, which after all is a small operation. We've got two businesses: one is a steadily declining legal newspaper now earning about $1m pre-tax and shrinking. The other is a computer software business where we're trying to automate courts and justice agencies and various other governmental departments. This business is now bigger by far in terms of prospects, customers, and employees than the shrinking newspaper business.

Sydney
39 Phillip Street,
Sydney NSW 2000
T +61 2 9237 8900

AFSL 321789
SEC Registered
www.vgipartners.com

New York
600 Madison Avenue, Suite 2101
New York NY 10022 USA
T +1 212 937 4700

Tokyo
Representative Office
Level 8 Tri-Seven Roppongi
7-7-7 Roppongi Minato-ku
Tokyo 106-0032, Japan
T +81 3 6629 3515

How are we doing? That's hard to judge, but within the software business we have a lot in the pipeline that's quite important to us – Australia, Canada, California. We're talking big, big markets and we're getting some significant volume and have some very pleased customers.

How in the hell does the little Daily Journal attract the government of Australia? Australia is a big place, but I've gotten to love Australians and I think we're going to succeed in Australia mightily. It takes a long time and it is hard work. Not everyone can do this because of the mass of complexity.

We would never be where we are if we didn't have Jerry Salzman (CEO) do what he's done over the last ten years. Everyone else would have failed at this. Now Jerry is 80 and we both use canes – when I'm not in a wheelchair I use a cane. The idea of taking on the whole world when the Chairman is 95 and the Vice Chairman (J.P. Guerin) is 89 and the chief executive who does all the work is 80 and uses a cane, it's a very peculiar place.

What's happened, of course, is that we're standing for some combination of basic morality and sturdy common sense. It's amazing how well Berkshire Hathaway and the Daily Journal have succeeded with nothing but basic morality and sturdy common sense. But of course, when people talk about common sense, they mean uncommon sense. Every time you hear that someone has a lot of common sense, they mean uncommon sense. It's much harder to have common sense than is generally thought.

One interesting example: the investment world involves an enormous amount of high-IQ people trying to be more skilful. You could hardly imagine another activity that gets so much attention. And weird things have happened.

Years ago, one of our local investment counselling shops, a big one, was looking for a way to get an advantage over a different investment counselling shop and reasoned as follows: we've got all these brilliant young people from Wharton and Harvard and so forth and they work hard trying to understand business and market trends. We just ask each of these brilliant young men for their best idea and create a formula for this collection of best ideas and outperform averages by a big amount.

This seemed plausible to them because they were ill-educated. That's what happens when you go to Harvard or Wharton.

[Laughter]

And so, they tried it out and of course it failed utterly. They tried again, and it failed utterly again. And they tried a third time and it also failed.

Of course, what they were looking for is the equivalent of the alchemists centuries ago, who wanted to turn lead into gold with a magic wand. This counselling shop was looking for the equivalent of turning lead into gold and of course it didn't work. I could have told them, but they didn't ask me.

And the issue is very simple, it's a simple question: why did that plausible idea fail? Just think about it, you've all been to fancy educational institutions. I bet you there's hardly anyone in the audience who knows why it failed. If you ask that question at a department of finance in a leading place, they're not going to answer it right. I'm going to leave you with that question because I want you perplexed.

[Laughter]

It does show how hard it is to be rational on something very simple. How many crazy ideas people have, and they don't know why it doesn't work even though they've been properly educated.

By the way, my definition of being properly educated is being right when the professor is wrong. Anybody can spit back what the professor tells you. The trick is to know when he's right and when he's wrong. That's the properly educated person. And of course, they're frequently wrong, especially in the soft sciences.

Another issue of course that's happened in the world of stock-picking, where all this money and effort goes into trying to be rational, is that we've had a really horrible thing happen to the investment counselling class. And that is these index funds have come along, and they've basically beat everybody. And not only that, the amount by which they've beat everybody is roughly the cost of running the investment operations. So, we've got a whole profession who are essentially being paid through accomplishing nothing. This is very peculiar, this is not the case with bowel surgery or even the criminal defence bar.

How is that profession handling this terrible situation, as index investing gets more and more popular. The simple answer is they're handling it with a lot of denial. They have a horrible problem that they can't fix so they treat it as non-existent. This is a very stupid way to handle a problem. So it's wrong to have all these people just in a state of denial and doing what they always did, year after year, and hoping that the world will keep paying them for it even though indexes are virtually certain to do better.

It's a very serious problem. Think about how much, say, New York, needs the flow of money from finance. Think about what would happen to Manhattan if there weren't any fees for investment management or trading spreads and so on.

So it's unpleasant for big investment counselling jobs, some of them shrink and some go out of business. And the value investors, many of whom I know because we came from that tradition, who are honourable are quitting. What worked for them for years stopped working and they're honourable people, so they quit. They're also rich, so that makes it easy.

[Laughter]

But those who aren't rich sure have a hell of a problem. It costs about $50,000 to send your kid to pre-school in Manhattan, not deductible, and that's just the start of an endless series of vast expenses. So if your game is money management you have a serious problem. And I don't have any solution for this problem.

I do think that if everybody did index investing it wouldn't work, but for another considerable period, index investing is going to work better than active stock picking.

Now at a place like Berkshire Hathaway or the Daily Journal, we've done better than average. Now there's a question on why that has happened. The answer is pretty simple: we tried to do less. We never had the illusion we could just hire a bunch of bright young people and they would know more than anybody else about canned soup, aerospace, utilities, or so on.

We never had that dream. We never thought we could get really useful information on all subjects like (CNBC's) Jim Cramer tends to have.

[Laughter]

We always realised that if we worked very hard, we could find a few things where we were right, and a few things were enough, and that was a reasonable expectation. That's a very different way to approach the investment process.

If you had asked Warren Buffett the same thing, to give you his best idea this year, and you just followed his best idea, it would have worked beautifully. But he wouldn't try to know a whole lot, he'd give you one or two stocks. He had more limited ambitions.

I'm 95 years old and I practically never have a transaction. And the answer is that I'm right and they're wrong. That's why it's worked for me and not for them. So the question is if you want to be more like me or more like them.

The idea of diversification makes sense to a point. If you don't know what you're doing and want the standard result and not be embarrassed, of course you need to diversify. Nobody is entitled to a lot of money for recognising that because it's a truism, like 2+2=4. But the investment professionals think they're helping you by arranging diversification.

But the whole trick of the game is to have a few times when you know that something is better than average and invest only where you have that extra knowledge. And if you get only a few opportunities, that's enough. What the hell do you care if you own only three securities and J.P. Morgan Chase owns a hundred? What's wrong with owning a few securities?

Warren always said that if you live in a growing town and own stock in three of the best enterprises in the town, isn't that diversified enough? Of course it is.

The Fortune's Formula which became so famous and told people how much to bet on each transaction if you had an edge, and to vary your bet with edge, of course it's true. It's perfectly possible to buy only one thing or two or three because the opportunity is so great and it's such a cinch. The whole idea of diversification in looking for excellence is totally ridiculous, it doesn't work. It gives you an impossible task. What fun is it to do an impossible task over and over again? I find it agony! Who would want to do it?

My father was a lawyer in Omaha. He had a client whose husband had a little soap company, and he was one of the richest people in town during the Depression. They had the soap company and one of the biggest mansions in Omaha's best neighbourhood. The guy died, and my father sold the soap company. When they sold the soap company, she had a mansion in the best neighbourhood and $300,000. In the 1930s, $300,000 was an incredible amount of money. A little hamburger was 5c, a big hamburger was 10c, and the all-you-can-eat cafe in Omaha would feed you all you needed to stay alive for 20c a day.

She didn't hire investment counsellors or do anything. She just took that and divided it into five chunks, she bought five stocks. I remember three of them because I probated her estate: General Electric, Dow Chemical, and DuPont, I forget the other two. And she never changed those stocks or paid any advisers. She also bought some municipal bonds from time to time. When she died in the 1950s, she had $1,500,000. No costs, no expenses. She said, "I thought electricity and chemistry are the coming things." She bought those and then sat on her ass. I've always liked that woman, my kind of girl.

If you take the modern world where people are trying to teach you how to actively trade in stocks, I regard that as the equivalent of trying to get young people started on heroin. It is really stupid. You see people selling books teaching you to make 300% per year by trading, if you just pay shipping and handling. How likely is the person who makes 300% per year trading to be selling books on the internet to you?

[Laughter]

It's ridiculous and yet I've described modern commerce. And the people who do this every day think they're useful citizens. The advertising agents invent the lingo. In insurance they say: the two people who shifted from GEICO to "McGlotz Insurance Company" saved $400 each. But they don't tell you that there were only two such people in the United States. They mislead you on purpose and I get tired of it and don't think it's right to mislead people as much as we do.

A different story goes back to a different time. This man has this wonderful horse, it's just a marvellous horse, with an easy gait, good-looking, and just works wonderfully, but it occasionally gets dangerous and vicious and causes trouble, breaking arms and legs of its riders. He goes to the vet and asks what to do about the horse. And the vet says it's an easy problem and he's glad to help. The next time your horse is behaving well, sell it.

[Laughter]

Think about how immoral that is. And haven't I just described what private equity does?

[Laughter]

By and large, Warren and I never tried to make money out of the stupidity of dumb buyers. We try to make money by buying and if we were selling horseshit, we didn't want to pretend it was a cure for arthritis. I think it's better to go through life our way than theirs. I think it's always been this way, there's always been chicanery. People just seek out the weakness of their fellow men and take advantage, and you have to get wise enough to avoid them all. You can't avoid them if they're in your family, I have no solution for that one.

[Laughter]

But where you have a fair choice, there are just so many people who should be avoided.

My father had a good friend who was a client and he also had this client who was a big blowhard. He was always working for the big blowhard and never for this wonderful friend whom I admired. And I asked why, and he said Charlie, the big blowhard is an endless source of legal trouble, he's always overreaching and in trouble. Whereas my friend always treats everybody right, when he meets a psychotic, he makes a graceful exit. A man like that doesn't need a lawyer. My father was trying to teach me something and it really worked. I spent my whole life trying to be like that man, and it really works.

Peter Kaufman always tells me that if the crooks only knew how much money you could make by being honest, they'd all behave differently. Warren has a wonderful saying: "if you take the high road it's never crowded."

The Daily Journal Corporation made quite a few millions of dollars out of the foreclosure boom because we publish legal notices and dominated the publication of foreclosure notices in the worst real estate depression in modern times.

We could have raised our prices at the time and made more, but we didn't do it. When your fellow citizens are losing their damn houses, "Charlie Munger, Billionaire, Raises Prices" would look lousy on the front page of the paper. Should you do it? Of course not.

Warren always says it's a mistake to marry for money and it's really stupid if you're already rich. It's really stupid if you're already rich to get a reputation for being a no-good guy.

There's the story about the guy who's been a total miscreant his whole life and the minister at the funeral says this is the time to say something nice about the deceased. And nobody came forward, and then one guy stood up and said "well, his brother was worse."

[Laughter]

There are people like that. When Harry Cohn died the saying was that everybody went to the funeral to make sure he was dead.

[Laughter]

There are a few simple truths that really work. When it comes to the Daily Journal, it's a true pleasure to serve these courts and agencies. They need the automation, other people are trying to take advantage of them in ways we aren't, and as a tiny company we're struggling against the odds and taking a lot of territory. The prospects are good but it's a little slow. But the nice thing when you're rich is it doesn't matter if it's a little slow.

How did we get rich? Well, when one of the few opportunities came along, we seized it.

If I hadn't made one mistake of omission in the 1970s, the Mungers would have twice the assets they now have. It was really stupid. I blew an opportunity to double my present net worth. That's a normal life, you get one or two situations.

It's been fun for the people on this Board to work on life's vicissitudes. It's peculiar that we're so old. Imagine a place where 71-year-old Gary Wilcox is a young man. Imagine being as old as I am and still having a good time?

There's an apocryphal story that's instructive. A young man comes to Mozart and says he wants to write symphonies. Mozart asks how old he is and he says he's 23. Mozart says, "you're too young to write symphonies." And he says, "but you were writing symphonies when you were 10 years old" and Mozart says "yes, but I wasn't asking other people how to do it."

[Laughter]

Now there's another Mozart story. Here's the greatest musical talent that ever lived and what was his life like? He was bitterly unhappy and died young. That's the life of Mozart. What did he do to screw it up? He did two things that guarantee misery: he overspent his income, that's really stupid, and he was full of jealousies and resentment. If you overspend your income and are full of jealousies and resentments, you can have a lousy and unhappy life and die young. Just learn from Mozart.

You can also learn from the young man asking Mozart how to write symphonies. The truth is not everybody can learn everything. Some people are way better and no matter how hard you try there's always some guy or gal who achieves more. My attitude is: so what? Does anybody need to be the top of the whole world? It's ridiculous!

If you actually figure out how many decisions were made in the history of Daily Journal or Berkshire Hathaway, it wasn't many per year that were meaningful. It's a matter of being there and recognising the opportunity when it comes and recognising that a normal human only gets very few.

Warren and I had tiny bits of money. We always underspent our income, we invested, and if you live long enough, you'll end up rich. It's not very complicated.

Now the question is how to scramble out of your mistakes without them costing too much. We've done some of that too. If you look at Berkshire Hathaway, think about its founding businesses: a doomed department store, a doomed New England textile company, a doomed trading stamp company. Out of that came Berkshire Hathaway!

We handled those losing hands pretty well and bought them cheaply, but the success came from changing our ways and getting into the better businesses. It isn't that we were so good at doing things that were difficult, it was that we were good at avoiding things that were difficult and finding things that were easy.

How many declining newspapers have hundreds of millions of marketable securities lying around and a new business with some promise? We're like the last of the Mohicans.

I'll take some questions now.

Q: Are you investing in the companies led by the CEOs profiled in *The Outsiders*? If not, why not?

Munger: I don't know these companies. Generally speaking, as things have gotten tougher, we've been better at sitting on our ass with the things we have rather than buying new ones. It's been hard to buy new ones. We haven't bought a whole company of any size since we bought the truck-stop operator (Pilot Flying J in October 2017). If you're having trouble with the present time, join the club.

Q: You've said you should hire somebody with an IQ of 130 who thinks it's 120 and the guy with an IQ of 150 who thinks it's 170 will just kill you…

Munger: You must be thinking about Elon Musk.

[Laughter]

Q: How do you assess someone when making a hiring decision?

Munger: I want to have the guy who understands his limitations rather than the one who doesn't. On the other hand, I've learned something terribly important in life: never underestimate the man who overestimates himself.

These weird guys who overestimate themselves occasionally knock it right out of the park. That's a very unhappy part of modern life but I've learned to adjust to it. I have no alternative. It happens all the time. But I don't want my personal life to be with a bunch of guys who live in a permanent state of delusion who occasionally win big. I want the prudent person.

Q: What did you see in Li Lu versus other investors? Why did you give an interview with Li Lu last year?

Munger: I did it because he asked me and sometimes I'm foolish that way.

Li Lu is not normal. He's the Chinese Warren Buffett. He's very talented. Of course I enjoyed backing him. I'm 95 years old, I've given Munger money to an outsider to run once in 95 years and that's Li Lu. That's remarkable but it's also picky.

That's a good way to choose things. If we've got a good thing we can do more of, we're not interested in anything that's not better than that. That simplifies life a great deal, because there aren't many people better than Li Lu. So I just sit. It's amazing how intelligent it can be in life to spend time just sitting. A lot of people are way too active.

Q: What would single-payer healthcare mean for healthcare companies?

Munger: Well, it will be a hell of a mess. It'll still be a big business, but it'll be a hell of a mess. But the existing system is so over-expensive and over-complicated and has so much unnecessary cost and overtreatment of items best left alone. On the other hand, it's the best system in the world in terms of the quality at the top.

It's a very complicated topic. I find it demoralising to see that in Singapore they spend 20% of what we spend, and their system is way better. They do it with more common sense, but it was created by one Chinese guy with total control (Lee Kuan Yew), so of course it's more intelligent than the outcome of our political process.

There's much to be demoralised about and our politicians aren't good at fixing a system like that. If you don't like it now, I can confidently predict you won't like it in the future either.

[Laughter]

Q: What influence has the philosophy of Stoicism had on you?

Munger: A lot. Including Epictetus, who started as a slave. I like those old Stoics. And part of the secret of a long life that's worked as well as mine is not to expect too much of human nature. There's almost bound to be a lot of defects in life, and having your life full of seething resentments and hatreds is counter-productive. You're punishing yourself and not fixing the world. Can you think of anything more stupid?

I have a rule for politicians and it's the Stoic rule. I always reflect that politicians are never so bad that you don't wish them back. The California legislature used to be full of crooks who were bribed with prostitutes, then the legislature changed and I wished we had the old crooks and prostitutes back.

[Laughter]

You laugh but for you young people there will come a time when you wish Nancy Pelosi and Donald Trump had been immortal.

Q: What have you read recently that's fundamentally changed your viewpoint?

Munger: There are few 95-year-olds changing their viewpoints on things. But sometimes there are amusing anecdotes I read and like. But I like the old ones too. Storytelling really works to get a message across.

Look at our modern politicians and then think of Abraham Lincoln. Who reminds you of Abraham Lincoln in either party?

At one point, Lincoln was hired by someone whose business partner had died with a widow and was owed by that partner. The surviving partner said to Lincoln I want to collect that money and Lincoln said you'll need a different lawyer to wring money out of that poor widow. What a story. No wonder he's remembered.

Q: Why haven't Berkshire's principles been copied more?

Munger: I think one reason is because it looks impossible. If you're at Procter & Gamble, with its culture and bureaucracy, and you ask how can you make Procter & Gamble more like Berkshire Hathaway, it would go immediately into the too-hard pile. There's just too much momentum.

But your question raises an interesting thing. One of the reasons we've been so successful is that there's almost nobody at headquarters so there's no corporate bureaucracy. Not having a bureaucracy is a huge advantage if the people who are running it are sensible people.

Bureaucracy has a standard bunch of evils and stupidities and avoiding it is hugely important. The tendency of successful places, particularly successful governments is to have more bureaucracy even though it's counterproductive because the bureaucrats benefit from more of it. The individual bureaucrats, they're benefitting from more assistance, more meetings etc. What looks like poison to us from the outside, looks wonderful to them. That's the tragedy of modern life. Successful bureaucracy creates failure and stupidity and that's the tension of modern life.

With some of these places if you go in and fire a third of the people, the place works better. They're doing the Lord's work, but you wouldn't think so if you were working there. There's a lot of horror and waste in bureaucracy but it's inevitable. It's as natural as old age and death.

Q: You have spoken about the importance of fishing in waters with ample fish; which seas would you be fishing in today, other than China?

Munger: There are others I'm sure but it's hard for me to believe there can be any better for the Mungers than China.

By the way, the water is fine in China. Some very smart people are wading in and in due course I think more will wade in.

The great companies in China are cheaper than the great companies in the United States.

Q: Where would you suggest looking for long term investing ideas where compound interest can work for you?

Munger: My advice for a seeker of compound interest is to reduce your expectations, because I think its going to be tougher for a while. It helps to have realistic expectations. It makes you less crazy.

They say that between the Great Depression and the present time, an index produced roughly 10% per year. But that's before inflation, after inflation it may be 7%. The difference between 7% and 10%, and the consequences, are hugely dramatic over that long period of time.

If that 7%, in real terms, was achieved through the period of the greatest boom in history; starting now it could well be 3%, or 2%, in real terms. It's not unthinkable that we could have 5% returns, pre-inflation, moving forward. The ideal way to cope is to accept if that happens, I can have a happy life, because why should you be unhappy if returns for your generation were not quite as easy as they were for my generation?

How should you deal with this? The answer is, that if it's going to be very difficult, you should still work at it. And if that work gets you a lifetime of 6% returns instead of 5%, you should be cheerful about it.

If you want to hit it out of the park easily, you should talk to Jim Cramer.

[Laughter]

Q: Has the Berkshire Hathaway equity portfolio outperformed the S&P500 over the last 5 or 10 years? And if it has not, why wouldn't Berkshire just invest in the S&P500 for its equity exposure?

Munger: I think Warren thinks Berkshire can do a little better than the S&P from this point. I don't think many people can, but he may be right about himself and the team he has in place. It won't be by huge margins, that I can confidently predict.

Q: How do you know when to exit an investment?

Munger: You're not talking to a great exiter. My Berkshire stock I bought in 1966. I've been a good picker; other people know more about exiting. I'm trying to never have to exit. There are styles of investing that work well with constant exits, it just hasn't happened to be my area of strength. I'm not looking for exits, I'm looking for holds.

I've had a lot of pleasure watching Costco march ahead. Such an utter meritocracy and it does so well. Why would I trade that for a series of transactions? I'd be less rich after taxes. I say find Costcos, not exits.

Q: Do you believe Berkshire has been too restrained on buying more Apple stock? Would you buy more now the price has declined?

Munger: I don't think the world will be improved by me making more comments on Apple. I like Apple but I'm not an expert.

I don't know why the stock is going up or down. I know enough about it to admire the place, but I don't know enough to have a big opinion about why it's going up or down.

Part of our secret is that we don't attempt to know a lot of things. I have a pile on my desk that solves most of my problems. It's called the too hard pile. I keep shifting things to the too hard pile. Every once in a while, an easy decision comes along, and I make it. That's my system – everything is in the too hard pile except for a few easy decisions, which I make properly.

Q: When assessing a business, do you place more emphasis on quantitative metrics such as return on invested capital or qualitative measure like brand strength and quality of management?

Munger: We pay attention to both. Generally, we like to pay attention to what is important to a particular situation, and this will vary situation to situation.

We're just trying to have that uncommon sense I'm talking about. Part of our uncommon sense is just to refer a lot of stuff to the too hard pile.

Q: How did you maintain the discipline to live the simple life in the face of temptations?

Munger: I was born this way.

[Laughter]

Q: What role do you think the credit rating agencies and other financial firms played in the Great Recession?

Munger: The behaviour of the leading financial institutions was inexcusably awful. When other people were raking in money, everyone piled in and participated. The standards in lending were disgusting intellectually and morally and, of course, it caused a whirlwind that could have taken the whole of civilisation into a great depression. That's a pretty significant sin and none of those people have been punished. It's unusual that I agree so thoroughly with Elizabeth Warren, but its unusual to have such a big mess and to have no one punished.

Q: Are you concerned about the national debt levels in the US and current political inactivity with regard to the debt levels?

Munger: The whole science of economics 15 years ago had no idea that it would be possible to print money at the present scale and be so awash in debt like we are. Certainly, in a place like Japan nobody dreamed it was possible. And the few people who did predict it was possible didn't predict there would be 20 years of stasis.

There's a lot that's peculiar in what we're doing. If you solve all your problems by printing money it's likely to end in disaster. When it's coming, or how bad it will be, nobody knows. Nobody dreamed 15 years ago we could do as much as we've done now.

Churchill used to say that Clement Attlee had a lot to be modest about. That's how I feel about the economics profession, they have a lot to be modest about. They thought they knew a lot, but it turned out not to be so.

There was a Greek philosopher that said no man steps into the same river twice. The river is different the second time, and so is the man. That's the way with economics. It's not like physics where the same principles apply every time. You do the same thing a second time in economics and you get a second result.

Who knows how much debt we can get by with? No one knows the answer. My personal feeling is that these democracies will eventually borrow too much and cause some real troubles but I don't know when.

Q: What's your take on stock buybacks and do you think politicians should be telling companies what to do?

Munger: Generally speaking, I'm restrained in my enthusiasm for politicians telling companies what to do. I will say however, that when it was a very good idea for companies to buy back their stock they didn't do very much and when the stocks got so high priced that it's generally a bad idea, they're buying back a lot.

It's questionable at these levels whether it's smart to be buying back stock. Was Eddie Lampert smart to buy back so much Sears stock? No. There's a lot of those types of decisions being made.

Q: What advice would you have for a young person looking to have a long, successful life like yourself?

Munger: It's hard to improve the next generation. The standard result is going to be mediocre. Some will succeed, but they are going to be few. That is the way human significance works, it accrues to the few.

Personal discipline, personal morality, good colleagues, good ideas – all the simple stuff. If you want to carry one message from Charlie Munger it's this: if it's trite it's right.

Q: What is your proudest accomplishment in life and why?

Munger: I don't have a single accomplishment that I am particularly proud of. I set out to have more uncommon sense than most, a pretty limited objective, and I'm pleased I did as well as I did in that game. If I had to do it all over again, it'd be a lot harder. Part of my success was being born in the right place at the right time. I'm not particularly proud of success that came from being born in the right place at the right time. I'm pleased, but I'm not proud.

Q: Why did you buy Wells Fargo in March 2009 rather than October 2008?

Munger: I had the money then and the stock was cheaper. Those are two very important parts of a purchase.

[Laughter]

Q: If you didn't have access to Li Lui and the Chinese exchanges, would you invest in the ADRs of large Chinese companies, which have abnormal ownership structures?

Munger: I don't know much about depository shares. I tend to be suspicious of all investment products created by professionals. I tend not to go where things are being sold to you aggressively.

Q: Are you concerned about the large derivative portfolios sitting on the balance sheets of American banks, given the SEC does not require much transparency with respect to derivative reporting?

Munger: All intelligent investors worry about banks. Banks present temptations to their managers to do dumb things that may look like an easy way to report higher earnings in the short term but is typically a mistake in the long term.

As Warren puts it: "The trouble with banking is that there are more banks than there are good bankers." He's right about that. To invest in banks, you have to go into them when you have a lot going for you as there will be a fair amount of stupidity that creeps into banking.

Q: Do you think early working experience gave you an advantage over other people in the investing profession?

Munger: Absolutely. When I worked for my grandpa as a kid, I was able to see that many of the adults around me were nuts, but also very talented. I could see how much irrationality there was in very talented people. So I got interested in seeking out the patterns and understanding why it happened and learning tricks to cope. I did that as a little kid, of course it helped me. Who is not helped by an early start in a promising activity? And what activity could be more promising than diagnosing stupidity?

Q: What level of discount would you be applying to potential investments today?

Munger: Generally speaking, professional investors have to expect less moving forward than they were getting out of previous conditions.

Q: What was the reason why you didn't invest in some of the companies mentioned in The Outsiders?

Munger: We did have a huge investment in General Dynamics for a long period of time and we made a huge amount of money from it. After the defence business contracted, no one else was willing to sell anything, except General Dynamics, which kept selling at higher and higher prices, and Warren noticed that. We had a huge position in General Dynamics and made a fortune.

We always admired the founder of Teledyne, who was a genius, Henry Singleton, but we admired him from afar. Just one of many mistakes of omission.

Q: What piece of advice would you give to your former self?

Munger: I'd avoid that one mistake of omission that cost me half of my net worth. We can all go back and make some decision better. It's the nature of things you're going to blow one occasionally. My general idea is there's no point fretting about what you can't fix. It's such a simple idea but so many people ruin their lives unnecessarily thinking about it and being envious.

My system in life is to figure out what is really stupid and avoid it. It doesn't make me popular, but it prevents a lot of trouble.

Q: Can you talk a little bit about your circle of competence?

Munger: A hugely important thing is knowing the edge of your circle of competence. It's hardly competence if you don't know the edge of it. If you have a misapprehension regarding your own competency, that means you lack competency. You're going to make mistakes.

You have to keep being determinedly rational and avoid self-delusion. After a life time of observing it, I think the tendency to be rational about one's own competency is largely genetic. I think people like Warren and I were just born this way. Now, it took a lot of education, but we were born with the right temperament to do what we did.

Q: Why is there so little healthcare in the Berkshire portfolio?

Munger: I think we don't understand it well enough and we don't like a lot of what we do understand. Those are two pretty good reasons for not investing in something.

[laughter]

Prepared by

VGI Partners

Los Angeles, California, 14th February 2019