

Buffett, Mary & Clark, David - Warren Buffett and the Interpretation of Financial**Statements, Scribner, 2008, [Equity Investing] Grade ★★★★★**

The authors have written several books on Warren Buffett's investment approach. The "Buffettology" books are the more well known. The title of this book is inspired by Ben Graham's seminal book on the subject of using financial statements to find undervalued stocks. What makes this book intriguing, of course, is one of the author's family name.

Mary Buffett is a former daughter-in-law of Warren Buffett. David Clark belonged long ago to a group of "devoted students" of Buffett's in Omaha before he got famous. His notebooks on Buffett's thoughts back then are the foundation of this book. Continuously throughout the book, the authors explain in detail what Warren Buffett does when he analyzes companies. What distinguishes companies with a durable competitive advantage in the financial statements according to Buffett? You almost get the feeling that you are looking over Mr. Buffett's shoulder, watching him read an annual report with eagerness. One has to admit, it is quite fascinating.

But is it a true description of Buffett's research? That is my main worry with this book. I don't know. During the years, I have seen plenty of book recommendations from Messrs Buffett and Munger. But never once have they mentioned one of Mary Buffett's books. I might be wrong, but that makes me somewhat suspicious about the book's reliability. To be fair, it is in line with other author's descriptions of what Buffett is focusing on. The difference is in the degree of detail.

Anyway, I enjoyed reading this book. Its outline is similar to the books in "The little book of..."-series. It is well written, an easy read and has beginners as a target audience. They will learn a lot. And even seasoned investors may find some goodies, although I occasionally found it too simplified. The constant referring to "Warren" is probably annoying even for fanatical Buffett fans. The book is admirably structured with 57 chapters

in less than 200 pages, which almost makes it a reference book.

The authors go through every major item in the Income Statement in great detail and describe Buffett's interpretation of different outcomes. What are the genuine signs of a true value creating business? A typical sentence is *"What he has found is that companies that have excellent long-term economics in their favor tend to have consistently higher gross margins than those that don't."* Perhaps that's not surprising. But it gets very interesting when the authors states some key levels for Buffett, e.g. above 40 percent gross margin. All together, I found a total of 11 levels of key indicators that Buffett considers important. The authors conclude with a major section on valuation at a rather basic level. Although basic, it is reminiscent of the "back of an envelope"-approach mentioned in the book *Snowball*. I have used some of these key levels in my screening process for segmentation issues. I believe they add some value in discovering potentially superior companies.

In addition to the key levels, experienced investors may appreciate some new Buffett wisdoms, e.g. *"Warren has learned over the years that companies that are busy misleading the IRS are usually hard at work misleading their shareholders as well. The beauty of a company with a long-term competitive advantage is that it makes so much money it doesn't have to mislead anyone to look good."*

A friend of mine recently calculated how many of Berkshire Hathaway's current holdings exceeded those 11 key levels mentioned in the book (not Ted Weschler's and Todd Combs'). The majority passed 7 levels or more. Some exceptions on the negative side were POSCO and Tesco. Maybe some of those levels are dated or dismissed? It seems that he is more prepared to buy capital-intensive companies, like BSF, nowadays. Even the Mastermind's thinking evolves over time... Big Blue, anyone?

Michael Persson, February 25, 2014