

What Do the Best Investors Do That the Rest Don't?

by Gary Mishuris, CFA

Charlie Munger, the Vice Chairman of Berkshire Hathaway and Warren Buffett's partner said something simple yet profound at the 2017 Berkshire Hathaway Annual Meeting: "A lot of other people are trying to be brilliant and we are just trying to stay rational. And it's a big advantage." Some might think that becoming an excellent investor requires off-the-charts intelligence or some highly proprietary model that leads to an edge that nobody else can replicate. That is not what experience has shown.

Here are some traits and behaviors that have allowed investors to excel over the long-term:

- 1. Temperament.** Temperament is the most important quality for an investor to have. My observation of many investors over my 15+ years of professional investing has led me to believe that temperament cannot be learned, but rather it is an innate characteristic of one's personality. Some people are able to remain rational and continue to follow their process even under great duress or during periods of external upheaval. Others get swept up in the emotion that typically runs amok during such circumstances, and abandon their discipline.
- 2. Ability to do nothing most of the time.** Most of the time there are few good investments that combine sufficient business quality with a large margin of safety in the form of a large gap between price and intrinsic value. That doesn't mean that great investors are spending all of their time relaxing on the beach – to the contrary, they are typically avariciously reading and studying business and industries, preparing for the moment when securities of companies they understand well can be purchased at attractive prices. It does mean that they make investments infrequently, and that most of the time when they look at a potential opportunity they end up passing. Those who are unable to maintain this state of low activity frequently end up making questionable investments to satisfy their desire to do *something*, and more often than not it is their brokers who are the biggest beneficiaries of their elevated activity levels.
- 3. Accumulation of mental models.** Understanding different disciplines helps great investors look at questions of business analysis in new ways. While studying economics and industry-specific information can certainly help, the best investors also use insights from other fields to reach better decisions.
- 4. Focus on process over outcome.** Benjamin Graham wrote: "In the short-term the market is a voting machine, but in the long-term it is a weighing machine." What he meant was that in the short-term security prices fluctuate purely based on the opinions of market participants, and can deviate widely from the underlying business values. In the long-term, it is the company's assets and cash flows that determine its value and exert a force of gravity upon the price of its securities. With security prices available on a minute-

by-minute basis, the run-of-the-mill investors focus on analyzing randomness – allowing themselves to become happy or sad over short-term price fluctuations that are disconnected from whether they were fundamentally right in their investment analysis. The best investors work hard to not be affected by the short-term price fluctuations, and instead focus on both improving their process and consistently executing it. Over the long-term their performance is a result of the quality of their process and of the consistency with which they execute it.

- 5. Minimizing behavioral biases.** Behavioral biases are pervasive and nearly impossible to eliminate, but the best investors work hard to be consciously aware of them and to take specific steps to mitigate them. As I wrote in [*Behavioral Defense in Decision Making*](#), there are a number of steps one can take to stay as unbiased as possible. One of my favorites is to consciously seek out the strongest possible opposite point of view that contradicts my thesis. If done well, this can lessen the impact of many biases, such as anchoring, over-confidence and base-rate neglect.

I frequently get asked by prospective investors about what my ‘edge’ is as an investor. Sometimes I think the answer that they are looking for is some proprietary model, some black-box that spits out superior answers that nobody possesses, or an ability to know what the future holds based on some deeply proprietary network of sources. The real answer is less exciting, but nonetheless quite effective. It is the combination of the traits and behaviors that I described above. I would add a sixth one to the list – staying humble while maintaining your confidence. History is littered with many seemingly great investors who fell apart and produced disappointing results for their clients just as they had accumulated the greatest amount of assets after a good run of performance. Perhaps some of them were never as great as they seemed, but in other cases I can’t help but think that it was a combination of hubris and complacency that led them astray.

The best investors stay humble – always thirsting to learn and improve as well as accepting that they are fallible and can make mistakes. This helps them to be on guard against the traps of complacency and overconfidence. Some view this posture as inconsistent with confidence in one’s abilities – after all, this is an industry where some think that the best investors are supposed to be on CNBC or on the cover of some financial magazine telling the world how great they are, which seems incompatible with a humble, introspective approach. Believe me, the people I admire most as investors have rejected this false dichotomy, and are able to balance humility with confidence and competence in a way that allows them to continue to improve for many years.