

Invest like the masters: Warren Buffett

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[Warren Buffett](#) | [David Dreman](#) | [Peter Lynch](#) | [James O'Shaughnessy](#)

Want to invest like a master? Then look to the works of Warren Buffett, Peter Lynch, David Dreman, and James O'Shaughnessy. These four gentlemen are all great investors, and all of them have either written books on how to invest or, in Buffett's case, produced years of informative shareholder letters. Remarkably, none are shy about sharing their market-beating techniques. In this feature, we examine how each of these wizards thinks and we spell out what each looks for in a stock. But that's just for starters. We've also scoured the markets for stocks that our famous investors might be interested in buying right now. To provide a truly continental perspective, half of our picks come from the U.S. and half from Canada.

We think you'll find a few of these gems to be just right for your portfolio. Remember, though, that not even a great investor beats the market each and every year. To make sure that a given stock is right for you, take out your magnifying glass and examine any investment in detail before putting your money down. Remember that you should spend at least as much time thinking about what could go wrong as what could go right. After all, that's what the best investors do.

Warren Buffett

The greatest investor in history likes to buy quality companies trading at reasonable prices. Oddly enough, the firm that may best fit that description is his own,

When he was five, Warren Buffett set up a gum stand outside his home and sold Chiclets to passersby. Now 76, Buffett still knows how to make a buck. He's the second-richest man in the U.S. (trailing only his friend, Bill Gates) and is starting to give away his fortune to charity. Along the way to his billions, Buffett studied and worked with the venerable Benjamin Graham, the father of value investing, before opening up his own hedge fund in the 1950s. But most people know Buffett as the principal owner of Berkshire Hathaway, which he runs out of a small head office in Omaha, Neb.

Buffett started buying stock in Berkshire Hathaway, then a distressed textile firm, in 1962, when its shares were trading below \$8 per share (all prices in U.S. dollars). Today Berkshire Hathaway is a sprawling conglomerate with large insurance operations and trades above \$96,000 per share. The trip from \$8 to \$96,000 represents an average annual gain of about 24% over more than 40 years. Talk about the power of compounding!

In recent years, Buffett has moved away from buying publicly traded shares in favor of acquiring entire private companies in friendly transactions. Nonetheless, he continues to buy a few public stocks — usually in quality companies trading at reasonable prices.

If you want to benefit from Buffett's stock-picking acumen, the simplest route is to invest in his company. (If \$96,000 for a Berkshire Class A share sounds a mite steep for your wallet, you can choose instead to pick up "B" shares for only about \$3,200 apiece.) In recent years the stock has stalled, partly due to fears that Buffett may not live much longer. Nonetheless, Berkshire Hathaway is the epitome of a quality company. It trades at a below-market price-to-earnings ratio (P/E) of 14.3 and a low price-to-book-value ratio of 1.5. In our view, it's a bargain without Buffett and a steal with him.

Another way to cash in on Buffett's eye for a deal is to buy what Berkshire Hathaway has been buying. Berkshire has bought into several public companies over the past year. By delving into regulatory filings and news releases we selected 10 such stocks for Buffett's best stocks. We wanted to reassure ourselves that the stocks haven't gained too much since Berkshire Hathaway's recent purchases, so we show each stock's price appreciation over the last year. Amazingly, you can buy many of these stocks at or below the price that Buffett recently paid.

While we don't think that buying Buffett's best stocks will automatically produce 24% returns, we do think that our list is a good place for any Buffett-style investor to start looking for prospects. For more insight into

Buffett's style, read his frank and funny annual letters to shareholders. You'll find a free archive of them at BerkshireHathaway.com.

Buffett's best stocks

Company
Industry
Price*
P/E
ROE
1-yr. Gain

ConocoPhillips

Oil and gas
\$59.53
5.5
25.8%
-14.9%

Home Depot

Home improvement
\$36.27
12.4
23.6%
-4.9%

Tyco

Conglomerate
\$27.99
17.3
11.4%
0.5%

United Parcel

Delivery services
\$71.94
19.6
24.1%
4.1%

General Electric

Conglomerate
\$35.30
22.0
17.4%
4.8%

Anheuser-Busch

Beer
\$47.51
19.7
55.7%
10.4%

Wal-Mart

Discount stores
\$49.32
19.3
22.1%
12.6%

Torchmark

Insurance
\$63.11
13.2
15.0%
19.5%

Wells Fargo
Bank
\$36.18
15.4
19.7%
23.5%

USG
Building materials
\$47.07
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Source: yahoo.com, Sept. 29, 2006
*In U.S. dollars
**Recently emerged from bankruptcy