4 Warren Buffett Myths Debunked

Description

Thanks to the 14% rally in shares of **Berkshire Hathaway** (NYSE: BRK.A) (NYSE: BRK.B) so far this year, CEO Warren Buffett has once again overtaken Spanish retail titan Amancio Ortega of Zara fame as the world's third-richest person. All told, the Oracle of Omaha now has an eye-popping net worth of approximately $54.6 billion.

It's only natural, then, for people to explore exactly how Buffett amassed his fortune in their efforts to even partially replicate his success. This widespread speculation, however, has resulted in oft-repeated bits of misinformation. As a result, many retail investors fall victim to persistent myths regarding Buffett's investing style.

Here are four such misconceptions, and why they're wrong.

Myth No. 1: Buffett hates share buybacks

In reality, Buffett only loathes poorly executed buybacks, and made as much clear in 2011 when Berkshire announced it would be willing to repurchase its shares at a price of up to 110% of book value.

In 2012, Buffett repurchased $1.2 billion of Berkshire's Class A shares at around 116% of book value, simultaneously raising his limit to 1.2 times. So did this move signal a deterioration of Buffett's long-standing strict criteria for identifying superior investments? Hardly.

In fact, Buffett circumvented the move when he devoted an entire page of Berkshire's 2011 shareholder letter to explaining his stance on stock repurchases, with the following paragraph summing things up nicely:

> "Charlie and I favour repurchases when two conditions are met: first, a company has ample funds to take care of the operational and liquidity needs of its business; second, its stock is selling at a material discount to the company's intrinsic business value, conservatively calculated."

Seems Buffett thought Berkshire shares themselves were cheap, and as judged by the soaring share price, he's right on the money, again.

Myth No. 2: Buffett only buys cheap stocks

I find this widespread assumption especially puzzling knowing Buffett himself is often quoted as saying, "It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."

This is exactly how Buffett built his empire and, incidentally, it also helps to reaffirm the notion held by The Motley Fool that winning businesses tend to keep on winning. That's not to say Buffett is willing to pay any price for great businesses, but if there's anyone who knows how to weigh risk versus reward, rest assured it's him. In the end, the overall quality of the business consistently trumps its price — and rightfully so.

What's more, this misconception becomes even more apparent each time Buffett uses Berkshire to acquire new businesses – like when in 2009 Berkshire spent $26.3 billion to buy the remaining shares of Burlington Northern at a 30% premium to their value at the time, and more recently in acquiring **Heinz** in a $23 billion deal, and at a 20% premium to its all-time high.

The bottom line is we need to give Buffett some credit considering he has repeatedly shown he knows a thing or two about getting the most bang for his buck over the long haul.

Myth No. 3: Buffett never invests in technology

Call the man old-fashioned, but it's been reported that Buffett refuses to carry a mobile phone and doesn't keep a computer at his desk. Instead, he subscribes to his own now-famous advice on how to become rich: "Close the doors. Be fearful when others are greedy. Be greedy when others are fearful."

While most of us would be unwilling or unable to follow suit, what better way is there to "close the doors" and form your own opinions than to shun the noise from these popular communicative technologies? Still, that doesn't mean Buffett is entirely unwilling to invest in technology. Instead, he simply refuses to invest in businesses he doesn't fully understand — a stance any investor would be wise to follow.

Take enterprise technology stalwart **IBM**, for instance, in which Berkshire currently holds a $15 billion stake. This holding shouldn't come as a surprise considering IBM trades at under 15 times trailing earnings and less than 12 times forward estimates, has taken advantage of it's reasonable share price with $12 billion in share repurchases over the past year, and has increased its dividend by around 17% each year since 2008.

That brings me to the next myth…

Myth No. 4: Since Berkshire doesn't have a dividend, it must mean Buffett hates dividends

Once again, it's understandable why investors mistakenly think Buffett hates dividends. After all, under his watch, Berkshire has only paid one dividend at $0.10 per share in 1967, and Buffett himself once joked he "must have been in the bathroom when the decision was made."

Sure enough, in his 2012 shareholder letter, Buffett also commented on this confusion:

> "A number of Berkshire shareholders — including some of my good friends — would like Berkshire to pay a cash dividend. It puzzles them that we relish the dividends we receive from most of the stocks that Berkshire owns, but pay out nothing ourselves."

That doesn't mean, however, Buffett despises dividends. In fact, the opposite couldn't be more true: Buffett has long said dividends represent one of four great ways to reward patient long-term investors. However, in Berkshire's case, Buffett just so happens to wield an unrivalled ability to create even greater value for his shareholders by using a combination of the remaining three ways in acquisitions, reinvesting capital in his business, and share repurchases.

That said, Buffett has stated they would be willing to "re-examine [their] actions" if the day ever comes that Berkshire's dividend-free approach consistently fails to provide adequate long-term returns for shareholders.

In the meantime, I suggest you sit back and enjoy the ride.

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Fool contributor Iain Butler does not own shares in any of the companies mentioned in this report at this time. The Motley Fool owns shares in Berkshire Hathaway.

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