



3 Important Investing Lessons From the Best Investor You've Never Heard of

Description

In 1955 an unknown employee of Benjamin Graham named Walter Schloss quit the firm to start his own investment partnership. A year later, another relatively unknown man named Warren Buffett did the same thing.

While Buffett got most of the attention from that point forward, we can't discount what Schloss did. From 1955 to 1995 Schloss and his son Edwin—who joined his father in 1972—absolutely crushed the Dow Jones Industrial Average. He averaged a return of 15.7% per year, while the Dow gave investors a 10.4% annualized return. And remember, Schloss's results were after he charged investors a 25% management fee on all profits.

That's one of the best 40-year investing records you'll ever see.

The amazing part is how simple Schloss's strategy was. He didn't spend thousands on research or fancy quantitative models. His office was in a closet he rented from investing firm Tweedy Browne. Most of his research came from a well-worn copy of the Moody's Manual.

We can attribute Schloss's success to three main factors. Let's take a closer look.

Buy cheap assets

Schloss didn't care about growth, earnings, or the quality of management, things investors today spend countless hours stressing about.

Instead, Schloss was all about buying one thing, and that was cheap assets, preferably with very little owing against them. If the market was depressed, he would search for the proverbial cigar-butt stocks, but if not, he would be content buying companies trading at a steep discount to book value.

A Canadian stock Schloss would likely be interested in today is **TransAlta Corporation** ([TSX:TA](#))([NYSE:TAC](#)). The stock is trading at approximately 10% under its book value, but that book value is likely understated because of years of depreciating its biggest assets: the power plants themselves. I'd estimate the real replacement value of the assets is likely closer to \$15 per share.

TransAlta is also taking steps to reduce its debt by selling its Australian gas assets to its subsidiary, **TransAlta Renewables**. That transaction, plus a few other steps, will decrease the company's net debt by nearly 20%, all while ensuring investors still get access to the cash flow from the assets because it owns almost 80% of the subsidiary.

Diversify

Many value investors concentrate their portfolios, choosing to only invest in their 10 or 15 top ideas. Not Schloss, who often had close to 100 companies in his portfolio.

Schloss would buy more of something he thought was a good deal, but he knew that he didn't have the same abilities as Buffett to be able to identify the few stocks that had years of outperformance ahead of them. So, he wouldn't even try.

Instead, he had a simple strategy that can be replicated by investors today. Schloss would buy when a stock was cheap, and sell it when it approached fair value. This would sometimes take years to play out, but as any value investor knows, patience is a virtue.

Go against the grain

You'll know you have a true Walter Schloss stock when you buy it and all your friends tell you how nuts you are.

Schloss would often talk about how successful value investors aren't afraid to be loners. It was one of the reasons why he chose to insulate himself from the rest of Wall Street throughout his career. It's hard to think outside the box when everyone in the box is telling you the same thing.

A Canadian stock for true outside-the-box thinkers is **Canadian Oil Sands Ltd.** (TSX:COS). Yes, the stock isn't attractive if you look at it from an earnings perspective since it's losing money because crude is hovering below \$50 per barrel. And the company has wrestled with unplanned maintenance and increasing costs for years.

But looking at it from another standpoint, I can make the argument that investors are buying assets for pennies on the dollar. Including the company's debt, someone buying shares today is paying just \$3.62 per barrel of proved and probable reserves. That's insanely cheap, especially considering that the infrastructure for taking those reserves out of the ground has already been built.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TAC (TransAlta Corporation)

2. TSX:TA (TransAlta Corporation)

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