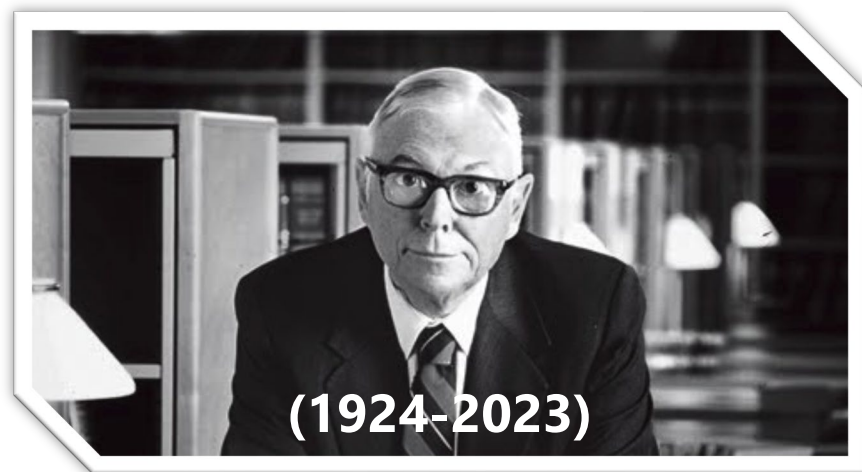




Honoring



CHARLES T. MUNGER

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HONORING A LEGEND

At the end of this past November, we lost an investment legend in Charles Thomas Munger. He passed away peacefully at a hospital in Santa Barbara, CA just 34 days shy of his 100th birthday. If the name doesn't ring a bell, you may recognize his long-time investing partner, one Warren E. Buffett. Together, they grew Berkshire Hathaway into the most famous investment company in the world.

Born in Omaha, NE in 1924, Charlie Munger would go on to study mathematics at the University of Michigan before dropping out to join the U.S Army Air Corps a few days after his 19th birthday. The Japanese had just bombed Pearl harbor a few weeks prior. He was stationed at Marks Air Field in Nome, AK, where he had plenty of time to learn the game of poker. It taught him to bet big when the odds were in your favor and to fold early when they weren't. This was a valuable lesson that translated well during his investing career. You cannot control the cards that you are dealt in life, and no one can predict how the stock market will perform in a given year. You can only make the most of the opportunities that are given to you while being discriminating in the ones you choose.

After the war, he attended Harvard Law School and graduated magna cum laude in 1948. He moved to Pasadena, CA and practiced as a real estate attorney for a number of years before giving it up to manage investments full time. The first meeting between him and Buffett occurred in 1959 at the Omaha Club. A mutual acquaintance arranged for the pair to have dinner, believing the two would have a lot to talk about. The acquaintance was right; intellectual fireworks ensued when both Buffett and Munger reflected on their appetite for investing and a shared belief in the power of compounded returns. As Buffett tells the story, "About five minutes into it, Charlie was sort of rolling on the floor laughing at his own jokes, which is exactly the same thing I did..." It was the beginning of a beautiful friendship.

From 1962-1975, Charlie co-founded and ran Wheeler, Munger & Co., an investment partnership based out of Pasadena, CA. The partnership generated annual returns of 19.8%, easily beating the Dow Jones Index which only averaged 5% over the same period. Munger joined Berkshire as vice-chairman in 1978, serving as Buffett's right-hand man, trusted sounding board, and intellectual sparring partner. To say he worked under Buffett would not be entirely accurate. Charlie came to have a profound influence on Warren's thinking and altered the way he approached investing.

Up until he met Charlie, Warren had practiced an asset-centric form of valuation that focused on investing in low-priced companies trading below their intrinsic value. It was the "cigarette butt" approach that was more short-term in nature, identifying mispriced value that would eventually be recognized by the market. Investors would be rewarded when the stock price grew and reflected its true value. However, if the stock was not sold at this time, investors

would be left holding a company that had mediocre prospects (there were usually semi-valid reasons for the mispricing to begin with).

In contrast to this idea of buying stocks that were undervalued (relative to earnings, book value, or some other measure of value), Charlie believed it better to invest in companies that could generate above-average economic returns over the long run. He emphasized thinking about the quality of the business and the quality of its management. Where classic investment theory emphasized diversification across investments and across sectors in order to minimize risk, Charlie promoted a broader interpretation. Investing across different types of business models – as long as they were high-quality companies – could still counteract the effects of secular downturns in any single sector or business model. This insight helped Berkshire withstand various economic downturns and market cycles over the ensuing decades. It has had a lasting effect on investing theory even to this day. Charlie taught people *how* to think and how to make good decisions – both in business and in investing. His contributions to our field will be taught for generations to come and his legacy will live on.

ABOUT THE AUTHOR



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Bo is Cabot Wealth Management's Research Analyst. He works with the Investment Management team to research investments for Cabot's Growth and Income strategies. Before joining Cabot in 2020, Bo previously held positions in trading and operations at Fidelity Investments and State Street Global Advisors. Bo is a member of the Boston Security Analysts Society (BSAS) and a CFA® Charterholder. He attended Carnegie Mellon University for his undergraduate degree and Boston University for his MBA. Bo enjoys spending time with his family and is an avid motorsports enthusiast.

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