

Warren Buffet Comes Clean

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“If you have a harem of 40 women, you never get to know any of them very well.”

Warren Buffet

Warren Buffet's quote is another way of saying that diversification means you don't know any of your stocks very well. Along these same lines, Buffet said, “Wide diversification is only required when investors do not understand what they are doing.”

Everyone would hate to think that she didn't know what she was doing when investing. But ample evidence suggests that not only individual investors* don't generally know, but also most money managers. ** So, what is Warren Buffet talking about?

According to a report from Dang Li, an MBA student at Goizueta Business School in Atlanta, Buffet clarified his position in an interview he gave to students from Emory's Goizueta Business School, Atlanta and McCombs School of Business at the University of Texas, Austin on 2 15 2008. The group was invited to visit Buffet for a Q&A session. Dang reconstructed the [conversation](#) to the best of his ability from his notes and those of others.

Emory:

“....., there seems to be a lot of debate in the community regarding diversification vs. concentration. I know where you side in that discussion, but was curious if you could tell us more”

Buffett:

“I have 2 views on diversification. If you are a professional and have confidence, then I would advocate lots of concentration. For everyone else, if it's not your game, participate in total diversification. The economy will do fine over time. Make sure you don't buy at the wrong price or the wrong time. That's what most people should do, buy a cheap index fund and slowly dollar cost average into it. If you try to be just a little bit smart, spending an hour a week investing, you're liable to be really dumb.”

Other luminaries ([Jack Meyer](#) from Harvard Management Company and [David Swensen](#), the manager of Yale's endowment) advocate a similar approach for the general investor.

For those of you who are still holding out for the investment manager who can 'beat the market,' or even try picking stocks yourself, Warren Buffet's words are prophetic. Most individual investors and professional money managers simply aren't able to perform magic over the long term like Buffet, a rare individual.

What is the chance you can pick a Buffet before he is a Buffet? It's about as likely as a free vacation offered in Florida without strings. For most of us, it isn't going to happen. As Rick Page, author of a book of the same name says, "*Hope is not a strategy.*" For more realistic investing and scientific approaches, please see [Asset Allocation: Just a Buzz Word?](#)

*Between 1986 and 2005 the average equity investor made 3.90% while the S&P 500 index made 11.93% (each on an annualized return before inflation). Source: Dalbar, Inc.

** 80% of managers of mutual funds perform *worse* than their relevant index in any one year.