"What are Superinvestors Good For?"

To Focused Compounding Free Members:

A lot of you reading this have been to sites like GuruFocus. You have read stories about David Einhorn's latest failures or Warren Buffett's latest stock sales. Einhorn wrote a book ("Fooling Some of the People All of the Time") you can read. And there are several books written about Buffett ("The Snowball", "Making of an American Capitalist", etc.) you can read too. So, why follow the quarterly ups and downs, buys and sells, of these superinvestors?

Mohnish Pabrai has written some articles for Forbes in which he talked about three strategies for beating the S&P 500. One was a "cannibal" approach (buy stocks that are buying back their own stock). Another was a spin-off approach. And then there's the "shameless cloning" approach. Pabrai backtested an approach where you continually take the biggest percentage idea you don't already own from each of nine value managers he likes and use that to clone a portfolio of high conviction ideas. So, is cherry picking the highest conviction ideas from your favorite superinvestors the best approach? What would that look like today? My Focused Compounding co-founder Andrew has mentioned that Allan Mecham is his favorite investor. What are Mecham's highest conviction ideas?

This is where things get a little subjective. Mecham's top position is Berkshire Hathaway. But, Buffett picks his own stocks and files a list of those stocks with the SEC. So, maybe you want to steal Buffett's own stock ideas – in which case you might not also want to clone owning Berkshire itself. Mecham's 3 next favorite ideas are: Alliance Data Systems, Cimpress, and Spectrum Brands. But, he hasn't added or reduced his holdings in the first two by much recently. Spectrum Brands – on the other hand – is a brand new position. In fact, if we looked not at what ideas Mecham owns the most of, but instead at what he has bought the most of most recently – we'd be focused on Spectrum Brands and Monro.

So, which ideas do you cherry pick? The ones he owns the most of? Or the ones he's buying now?

There is another way to do this. Start by jotting down a list of your favorite investors. Five names will do fine. Then, make the top percentage position in each of those five portfolios your next five stocks to research. So, your planned research slots number one through number five are filled with the top positions at the funds you like best. Then, your planned research slots number six through number ten are filled with the second to top positions at those same funds.

Where do you stop?

I don't think it makes sense to go beyond 5 funds or 5 stocks at each fund. If an investor isn't one of your top 5 favorites – don't spend time on him. And if he didn't like a stock enough to make it one of his top 5 favorites – don't worry about it. But, doing what I just described can create a research pipeline of 25 stocks to start with. You'll have stolen these ideas from other investors. But, the final decision to buy or not to buy won't be the result of cloning. It'll be a decision you make yourself after careful research. Hopefully, this will give you the conviction to hold the stock when the reputation of the superinvestor who first bought it plummets along with the stock.

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