

The Profoundly Simple Wisdom of Walter Schloss on Producing Towering Returns

What You'll Learn

1. Walter Schloss' performance record vs Buffet
2. Walter Schloss on his investment philosophy
3. Walter Schloss on buying stocks
4. Walter Schloss on selling stocks

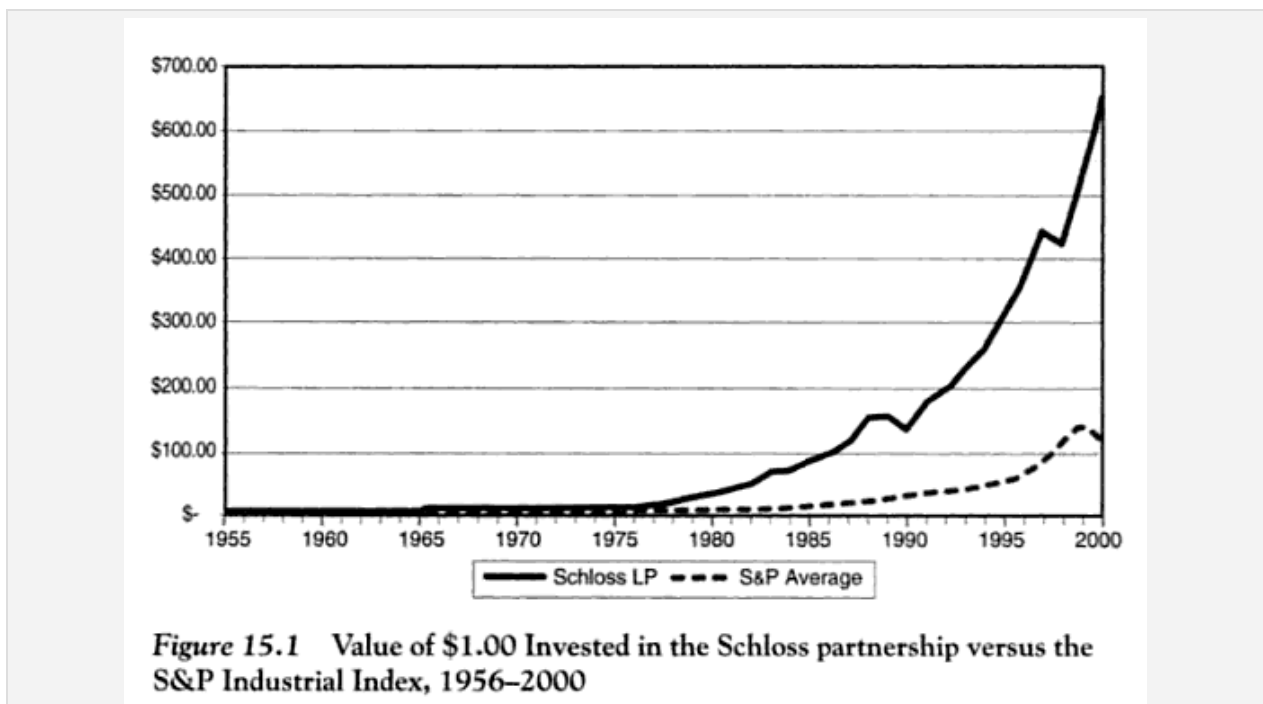
I've shown you [how small investors can beat the professionals](#) on Wall Street by not playing with the same rules.

Walter Schloss was such a man.

OK... well he was a professional, but not in the normal sense.

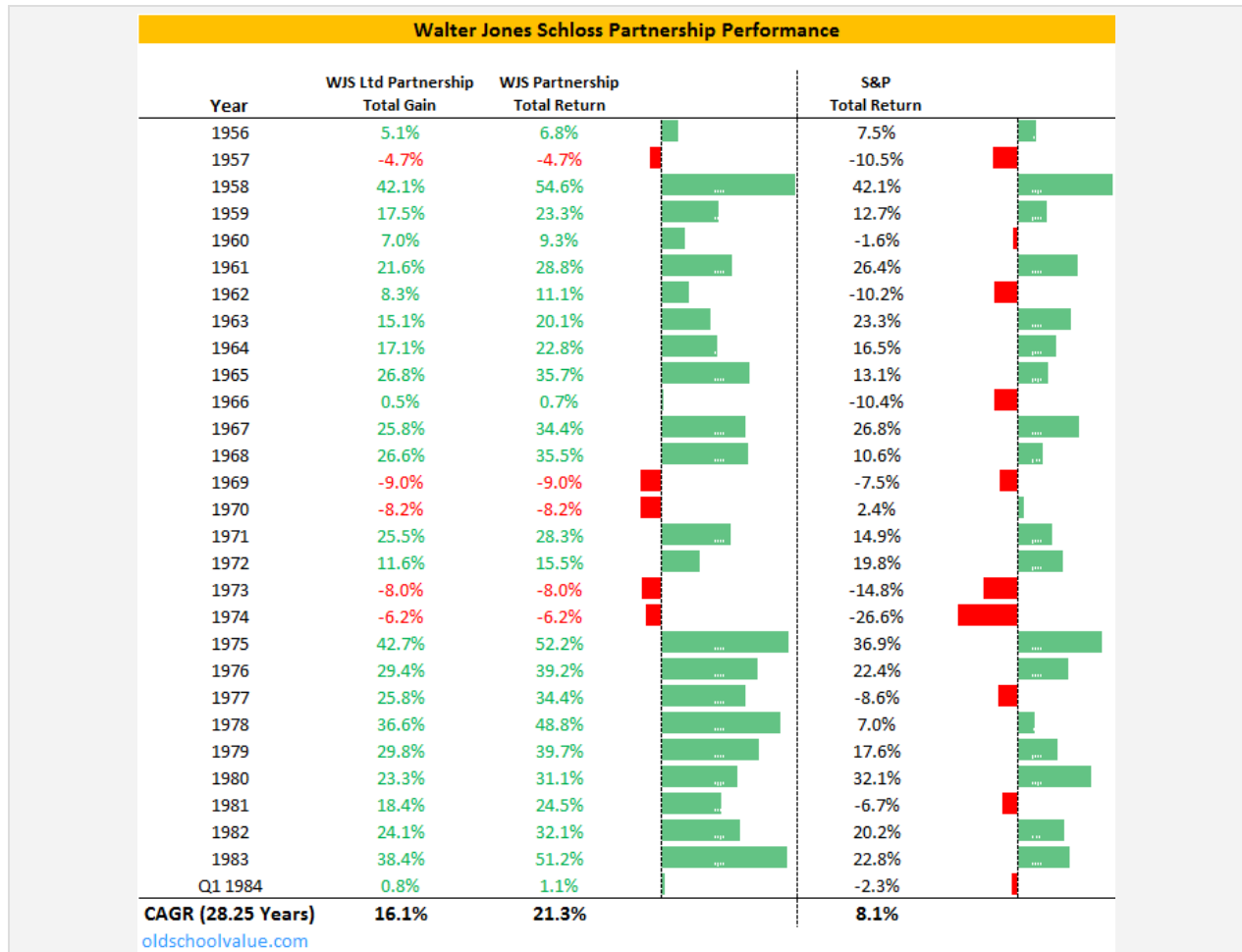
He didn't play by Wall Street rules. He took the unorthodox route of ignoring news, ignoring tips, sticking to cigar butts and holding thousands of stocks over his lifetime.

The result?



Annualized Return of 15.6%

Here's a table view. Unfortunately, data is only available up to Q1 of 1984.



Schloss Partnership Annual Returns 1956 to 1984 Q1 | Click to enlarge

Over this period of 28 and a quarter years, the Schloss partnership returned a staggering 21% CAGR.

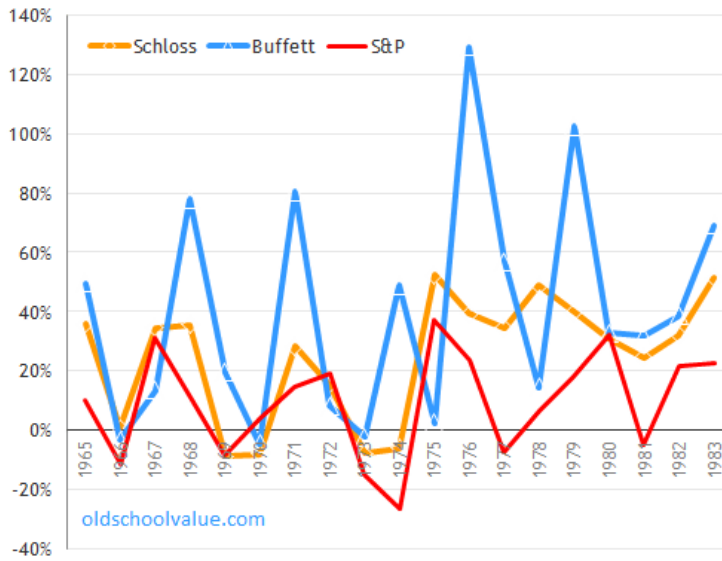
Just to show you how good he was, here's a side by side of Walter Schloss' performance against Buffett and the S&P over their overlapping periods.

Schloss vs Buffett vs S&P

Year	Schloss	Buffett	S&P
1965	35.7%	49.5%	10.0%
1966	0.7%	-3.4%	-11.7%
1967	34.4%	13.3%	30.9%
1968	35.5%	77.8%	11.0%
1969	-9.0%	19.4%	-8.4%
1970	-8.2%	-4.6%	3.9%
1971	28.3%	80.5%	14.6%
1972	15.5%	8.1%	18.9%
1973	-8.0%	-2.5%	-14.8%
1974	-6.2%	48.7%	-26.4%
1975	-2.2%	2.5%	37.2%
1976	39.2%	129.3%	23.6%
1977	34.4%	55.8%	-7.4%
1978	48.8%	14.5%	6.4%
1979	39.7%	102.5%	18.2%
1980	31.1%	32.8%	32.3%
1981	24.5%	31.8%	-5.0%
1982	32.1%	38.4%	21.4%
1983	51.2%	69.0%	22.4%

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Walter Schloss vs Warren Buffett vs S&P



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What's impressive about both Schloss and Buffett is their ability to have a good year even when the market was down.

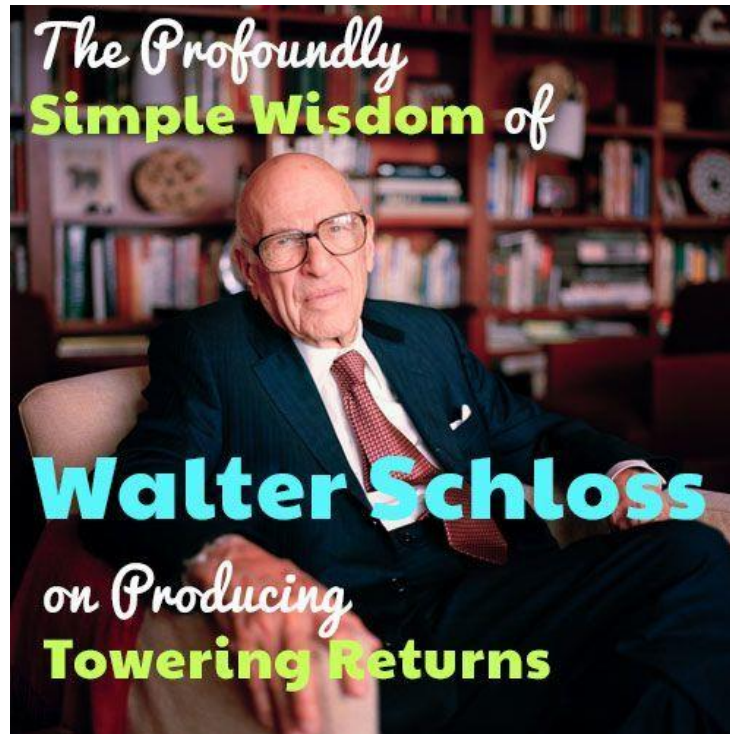
(You can also see why Buffett is a legend. His performance speaks for itself. Sure there are lots of ups and downs, but even in his "down" years are still positive.)

Look at the chart and it proves that you can do well independent of the market.

Now what's most impressive about Walter Schloss' record is that he didn't have a college degree.

So how did he do it?

Well let's get into his brain and find out based on the many quotes I've scoured from the internet.



The Schloss Investing Approach - Quick Summary

Philosophy and Style

Investors are best served using a Benjamin Graham value approach, looking for stocks that are hitting new lows and those trading at a price lower than their book value per share.

Universe of Stocks

Stocks are selected from among well-known "Campbell Soup" companies. Exclude foreign stocks and those in industries with which the investor is unfamiliar.

Criteria for Initial Consideration

- Ten-year track record
- No long-term debt
- A low price-to-book-value ratio
- A stock at or near its 52-week low price
- High insider ownership

Portfolio Construction

- Limit holding of one stock to no more than 20% of entire portfolio
- Well-diversified portfolio of up to 100 stocks
- Holdings weighted based on their perceived values, putting less money in positions the investor is less sure about
- Use limit orders to purchase stocks

Stock Monitoring and When to Sell

In general, try for a 50% profit from any holding before selling. If a stock's price is falling and the company's fundamentals are sound, buy more.

The Schloss Approach in Brief

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The Schloss Approach in Brief | Source: AAI

Walter Schloss on His Investment Philosophy

Keep things clear and simple. There's no need to chase complicated stocks or situations if you don't understand it.

When it comes to investing, my suggestion is to first understand your strengths and weaknesses, and then devise a simple strategy so that you can sleep at night.

I don't like stress and prefer to avoid it, I never focus too much on market news and economic data. They always worry investors.

You have to invest the way that's comfortable for you.

Try not to let your emotions affect your judgment. Fear and greed are probably the worst emotions to have in connection with the purchase and sale of stocks.

I think investing is an art, and we tried to be as logical and unemotional as possible. Because we understood that investors are usually affected by the market, we could take advantage of the market by being rational. As [Benjamin] Graham said, 'The market is there to serve you, not to guide you!'

I like Ben's analogy that one should buy stocks the way you buy groceries not the way you buy perfume

The ability to think clearly in the investment field without the emotions that are attached to it is not an easy undertaking. Fear and greed tend to affect one's judgment.

He goes on further about the way he approaches building a portfolio and protecting his capital.

Don't buy on tips or for a quick move. Let the professionals do that, if they can.

Remember that a share of stock represents a part of a business and is not just a piece of paper.

Prefer stocks over bonds. Bonds will limit your gains and inflation will reduce your purchasing power.

Listen to suggestion from people you respect. This doesn't mean you have to accept them. Remember it's your money and generally it is harder to keep money than to make it. Once you lose a lot of money it is hard to make it back.

Most look at earnings and earnings potential, well I can't get into that game.

I used the same investment approach I used at Graham-Newman finding net-net stocks. It was all about capital preservation because I had to serve in the best interests of my investors. Many of them were not wealthy, and they needed me to generate returns that would allow them to cover their living expenses.

I try to protect myself from permanent loss of capital by investing in stocks that are depressed.

When you buy a depressed company it's not going to go up right after you buy it, believe me.

I like to buy companies with very little debt so it has a margin of safety.

I like to buy basic businesses not high flyers that sell at huge multiples.

I'm not very good at judging people. So I found that it was much better to look at the figures rather than people.

We don't own stocks that we'd never sell. I guess we are a kind of store that buys goods for inventory (stocks) and we'd like to sell them at a profit within 4 years if possible.

Remember the word compounding. For example, if you can make 12% a year and reinvest the money back, you will double your money in 6 years, taxes excluded. Remember the rule of 72. Your rate of return into 72 will tell you the number of years to double your money.

You never really know a stock until you own it.

Walter Schloss on Buying Stocks

Walter Schloss ran with the idea of buying cheap stocks and taking a more quantitative approach. Instead of following every stock he owned, he heavily focused on valuation and buying at a discount to his intrinsic value.

You don't have to perform complex valuations either.

At old school value, I've provided guides of simple stuff like a net net balance sheet calculation as well as more complicated Earnings Power Value models which you can see from the list of [best stock valuation methods](#).

The key however, is to know how to value stocks. I've even put together an [ebook on all the valuation methods](#) that I use in detail.

Don't take my word for it though. Listen to what Walter has to say.

If a stock is cheap, I start buying.

Somehow I find it difficult to buy a stock that has gone up.

We like to buy stocks which we feel are undervalued and then we have to have the guts to buy more when they go down.

Basically, we try to buy value expressed in the differential between its price and what we think its worth.

Use book value as a starting point to try and establish the value of the enterprise.

Price is the most important factor to use in relation to value.

We basically followed the idea of buying companies selling below working-capital — at two thirds of working-capital.

Be sure that debt does not exceed 100% of the equity.

[On net-net stocks becoming almost impossible to find] We changed our strategy a little, but remained true to Graham's principle of downside protection. We looked for stocks that were selling below their book value. What we tried to do was to buy assets at a discount instead of buying earnings. Earnings can change quickly, but assets don't, and so the new strategy worked well for a while.

When buying a stock, I find it helpful to buy near the low of the past few years. A stock may go as high as 125 and then decline to 60 and you think it is attractive. 3 years before the stock sold at 20 which shows that there is some vulnerability in it.

When I buy a stock that is depressed it hardly ever turns around immediately.

We like to buy stocks which we feel are undervalued and then we have to have the guts to buy more when they go down.

When I buy a stock, I never visit or talk to management because I think that a company's financial figures are good enough to tell the story. Besides, management always says something good about the company, which may affect my judgment. I know a lot of good investors who like to talk to management and visit companies, but that's not me. I don't like that kind of stress, and if I had had to run around visiting so many companies, I would have been dead after a few years!

We don't put the same amount of money in each stock.

Walter Schloss on Selling Stocks

Walter subscribed to the idea of selling at what he believed to be intrinsic value and didn't focus so much on what the stock did 2-3 years later.

Don't we all get in the habit of looking at past stocks, and if it is 2x after you sold, you kick yourself and say you should have kept it?

Walter is no different but he moves on and focuses on the next stock.

[On purchasing a cement company called Southdown] I bought a lot of it at \$12 or something similar. After two or three years, when it reached about \$28, I sold it because it had reached my calculated value, and I didn't focus too much on its growth opportunities. It reached \$70 a while later. I could only be humble and move on to find the next cheap stock.

But some times you have to take advantage of the opportunity to sell and then say OK, it'll go higher.

As the saying goes, a stock well bought is half sold. I think Ben was an expert in that area.

Selling stocks is hard. But it's a lot easier when you know what a stock is worth.

When you try to sell a car, you wouldn't blindly list the car without knowing what it's worth. You would do your research, look up comparables, look at the quality of your car and price it accordingly at fair value.

Nothing different with stocks.

Each year we buy stocks and they go up, we sell them and then we try to buy something cheaper.

I never put a stop loss on my holdings because if I like a stock in the first place, I like it more if it goes down.

When I buy a stock, I have kind of an idea where I want to sell it.

Walter Schloss Library of Links

I'm not the only one that admires Schloss.

To learn more about the legendary Walter Schloss, check out these awesome links.

- [Comprehensive guide on Walter Schloss](#) (Valuwalk)
- [Barrons Article - The Right Stuff](#)
- [Guide to Walter Schloss Investing](#) (net net hunter)
- [Gurufocus article on Schloss](#) (Gurufocus)
- [An overview of Walter Schloss and links](#) (Basehitinvesting)
- [Walter Schloss on Ben Graham and Security Analysis PDF](#) (csinvesting)
- [Walter Schloss interview with Outstanding Investor Digest PDF](#)
- [The Walter Schloss approach to investing PDF](#) (AAIL)
- [Walter Schloss speech "65 Years on Wall Street" PDF](#)
- [Dozen things learned from Phil Fisher and Walter Schloss](#)
- [Walter Schloss - Keep it simple and cheap](#) (Hurricane Capital)