

From Cigar Butts to Wide Moats

• Warren Buffett's evolution from deep-value bargain hunter to long-term owner of quality businesses

Warren Buffett did not move away from value investing — he broadened it. His shift from buying statistically cheap stocks to owning high-quality businesses reflects a simple idea: the best returns come from the sustained reinvestment and compounding of earnings.



By **OLIVER MÜLLER**,
CHIEF INVESTMENT OFFICER,
ACCRESO INVESTMENT MANAGEMENT

Warren Buffett is often described in overly simple terms. To some, he is the patron saint of bargain hunters, the man who prowled the market for discarded “cigar butts” — those battered, neglected businesses with one last profitable puff left in them. To others, he is the high priest of quality, the owner of Coca-Cola, American Express and Moody's, who taught the world to value enduring franchises over statistical cheapness.

Both portraits are true. Neither is sufficient.

What makes Buffett so enduringly fascinating is not that he chose one creed and preached it unchanged for seven decades. It is that he evolved, decisively and intelligently, while preserving the core intellectual discipline that made the evolution possible. He began as Benjamin Graham's most gifted student, a forensic hunter of undervalued assets trading below liquidation value. He became, over time, the great apostle of high-quality businesses bought at sensible prices. The journey from deep value to what might be called quality at a reasonable price was not a repudiation of his roots. It was their fulfilment.

IN THE BEGINNING

The distinction matters because investors often mistake style for principle. They inherit Buffett's conclusions without understanding the conditions that produced them. They recite the famous lines about moats, pricing power and wonderful businesses, but forget that Buffett's early education was in the harsher arithmetic of balance sheets, hidden assets and downside protection. Equally, there are still purists who speak as if the only authentic value investor is one who buys statistically cheap stocks with no regard for franchise quality. Buffett's career is the most powerful rebuttal to both simplifications.

He learned first from Graham because Graham's method was exactly what the times required. The Great Depression had discredited optimism. Markets were littered with companies whose shares traded for less than their net cash, inventory and receivables. In such an environment, the investor did not need to predict a glorious future. He merely had to observe that the market had become absurdly pessimistic about the present. Graham's genius was to impose discipline on fear. Buy a basket of securities below intrinsic worth. Demand a margin of safety. Let time and mean reversion do the rest.

The young Buffett absorbed this creed with religious intensity. He devoured Graham's book *The Intelligent Investor*. He sought out Graham at Columbia University. He worked at Graham-Newman. In his partnership years, he behaved exactly as the theory prescribed: hunting for “work-outs”, liquidations, arbitrage opportunities and obscure companies selling for less than the value of what they owned. There was nothing glamorous about it. It was systematic, almost mechanical. Buffett was not then looking for great businesses. He was looking for mispriced facts.

That early approach worked brilliantly. It had to. Buffett was managing small sums in an inefficient market. He could fish in ponds too tiny, too murky and too inconvenient for large institutions. He could buy illiquid securities, wait patiently and unlock value through corporate actions or simple repricing. Some of his early triumphs now read like dispatches from a vanished financial world: Sanborn Map, Dempster Mill, a menagerie of half-forgotten stocks whose appeal lay not in any sparkling future but in the gap between price and underlying worth.

THE LIMITS OF CHEAPNESS

Yet the cigar-butt method carried hidden limitations. It was effective, but inelegant. It required constant recycling. A stock bought at two-thirds of working capital might rise to fair value, but it rarely became a compounding machine. Once the discount closed, the investor had to move on and find the next stub in the ashtray. This was investing as scavenging. It could produce excellent results for a nimble operator. It was less suited to the management of ever-larger pools of capital, and less suited still to the pursuit of truly extraordinary long-term wealth.

Buffett's purchase of Berkshire Hathaway itself became the cautionary tale. The textile mill looked cheap on asset values. It was, in Graham terms, statistically undervalued. But it was also a poor business in a brutal industry, devouring capital without durable pricing power. Buffett has since described buying Berkshire as a mistake born of irritation and bargain-mindedness. The lesson was profound: a cheap price could not compensate indefinitely for a bad business. Time, far from being the friend of the investor, could become the ally of mediocrity.

Enter Charlie Munger.

THE MUNGER EFFECT

If Graham taught Buffett the discipline of value, Munger helped him apply it in a more scalable, elegant and enduring way. Munger's intervention is sometimes caricatured as a simple instruction to “buy better businesses”. In reality it was more demanding. He pushed Buffett to move beyond the balance sheet and think more deeply about the economics of the enterprise itself: its brand, its customer captivity, its pricing freedom, its capital intensity, the habits it created, the returns it could sustain over long periods and the competence and integrity of the people running it.

Phil Fisher had already sketched part of this terrain. In his book *Common Stocks and Uncommon Profits*, Fisher directed investors toward qualitative inquiry — management quality, research culture, market position, the capacity for long-term growth. Munger, who admired Fisher, effectively translated this sensibility into Buffett's framework. The result was not a rejection of value investing but an enlargement of it. Intrinsic value was no longer just a matter of present assets. It was increasingly

“**Buffett was managing small sums in an inefficient market.**”

“**He could fish in ponds too tiny, too murky and too inconvenient for large institutions.**”

“**He could buy illiquid securities, wait patiently and unlock value through corporate actions or simple repricing.**”

about the discounted value of future cash flows generated by a business with favourable economics.

This is where the intellectual shift becomes clear. Graham's world prized assets you could count. Munger and Fisher pushed Buffett toward economics you could not always touch but could often infer. A newspaper with dominant local reach, a confectionery brand with emotional loyalty, a soft-drink company with global distribution, a ratings agency embedded in capital markets — these businesses might not screen as cheap on conventional metrics. Yet if they could reinvest capital at high rates, defend margins and remain relevant for decades, they might be far cheaper than they looked.

THE SEE'S TURNING POINT

See's Candies was the hinge. Buffett has often described the 1972 acquisition as a turning point. On paper, See's was hardly a classic Graham bargain. It did not come with a mountain of excess tangible assets. What it did have was something more valuable: customers who would pay a little more each Christmas for a box associated with ritual, trust and affection. The business required relatively little incremental capital to grow. It converted modest physical assets into abundant cash. It had brand power before “brand power” became an overused phrase in investor presentations.

The revelation was not merely that quality matters. Investors had always known that, in some vague way. The revelation was that quality has arithmetic consequences. A business able to raise prices without losing customers, and able to expand without consuming much additional capital, compounds in a fundamentally different way from a cheap but mediocre business. One produces a burst of value when a discount closes. The other produces rivers of value over time.

That insight helps explain Buffett's later canon: Coca-Cola, purchased heavily in the late 1980s; American Express, whose franchise he recognised long before “platform” became a fashionable term; The Washington Post, bought at a sharp discount to private value but held because of the extraordinary franchise; GEICO, a business Buffett had admired since youth, whose direct model and cost advantage gave it enduring power. In each case, the attraction lay not simply in buying at low multiples. It lay in identifying businesses with moats wide enough to protect returns on capital for years, even decades.

DEFINING THE MOAT

The phrase “wide moat” has since been so overused that it risks sounding decorative. In Buffett's hands, it never was. A moat is not a metaphorical flourish. It is the practical answer to one central investing question: what stops the economics of a good business from being competed away? The answer may lie in brand, network effects, regulation, cost advantage, switching costs, distribution, culture or scale. But unless something protects the castle, abnormal returns invite attack.

Buffett's mature philosophy therefore rests on a harder truth than many admirers acknowledge. It is not enough for a company to be excellent. It must be excellent in ways that endure. Plenty of businesses impress for a cycle. Far fewer can protect their economics through inflation, recession, technological change and management succession. Buffett's genius was to see that durability is what turns business quality into investment quality.

And yet, for all the transformation, the underlying principle never changed. Buffett did not stop being a value investor. He merely came to define value more comprehensively. This is where much of the public debate goes astray. “Value” and “quality” are often presented as rival camps, as if one must choose between low multiples and strong franchises. Buffett's career suggests a more subtle hierarchy. Price still matters. Valuation discipline still matters. Even the finest business can become a poor investment if purchased at a euphoric price. But quality determines what is worth paying for.

NOT ANY PRICE WILL DO

That is why the line most associated with Buffett's evolution — that it is “far better to buy a wonderful company at a fair price than a fair company at a wonderful price” — is so often quoted and so rarely unpacked. The sentence is not a permission slip to overpay. It is a statement about compounding. If a business is truly wonderful, “fair” can be much more rewarding than “cheap” in a low-quality enterprise because the internal economics keep working long after the initial purchase decision. In investing, as in life, what happens after the transaction often matters more than the elegance of the entry.

Scale also forced Buffett's hand. As Berkshire grew, the old cigar-butt strategy became less relevant. There are only so many tiny mispricings one can exploit when capital runs into the billions. Great fortunes, once amassed, require a different operating system. The problem shifts from finding hidden nickels to allocating large sums into durable engines of return. Buffett did not depart from Graham because Graham was wrong. He evolved because success changed the field on which he had to play.

There is also a deeper philosophical thread running through the transition. Graham's method was designed to protect the investor from human folly. Buffett's later method sought, in addition, to partner with human excellence. He increasingly spoke not only about numbers but about temperament, trust and culture. He looked for managers who treated shareholders as partners and for businesses whose reputation was an asset, not an advertising slogan. In the long run, management character is not separate from intrinsic value. It helps determine it.

THE LESSON NOW

For today's investors, Buffett's journey contains both encouragement and warning. The encouragement is that one need not choose between discipline and imagination. The best investing often combines Graham's insistence on margin of safety with Fisher's curiosity and Munger's broader mental models. The warning is that style boxes can become intellectual prisons. Deep value can degenerate into a love affair with low multiples. Quality investing can deteriorate into growth-stock worship with no anchor in valuation. Buffett escaped both traps because he remained loyal to the central question: what is this business worth, and what must be true for that worth to endure?

The movement from cigar butts to wide moats was therefore not a journey from value to something else. It was a journey from a narrow conception of value to a more expansive and durable one. Graham taught Buffett the discipline of value; Fisher and Munger showed him how to turn it into compounding. The synthesis — quality, resilience, managerial integrity and disciplined price — became one of the most powerful frameworks in modern capital allocation.

That framework feels newly relevant in a market increasingly split between expensive excellence and cheap uncertainty. The most rewarding investments are rarely those that appear optically cheapest, nor those commanding the most compelling narratives. More often, they are businesses whose economics are both stronger and more enduring than the market fully appreciates — enterprises capable of compounding quietly, provided they are acquired with sufficient discipline to leave room for error.

Buffett's evolution is therefore less a change in doctrine than a deepening of it. The true discount is not always found in low multiples, but in the market's persistent tendency to underestimate longevity. That insight continues to travel well, far beyond Omaha — and will no doubt form part of the conversation when the Genius of Warren Buffett masterclass convenes in Mauritius on 28 May, an initiative supported by Accresco, where the enduring question remains the same: not what is cheap, but what will remain valuable when time has done its quiet work.