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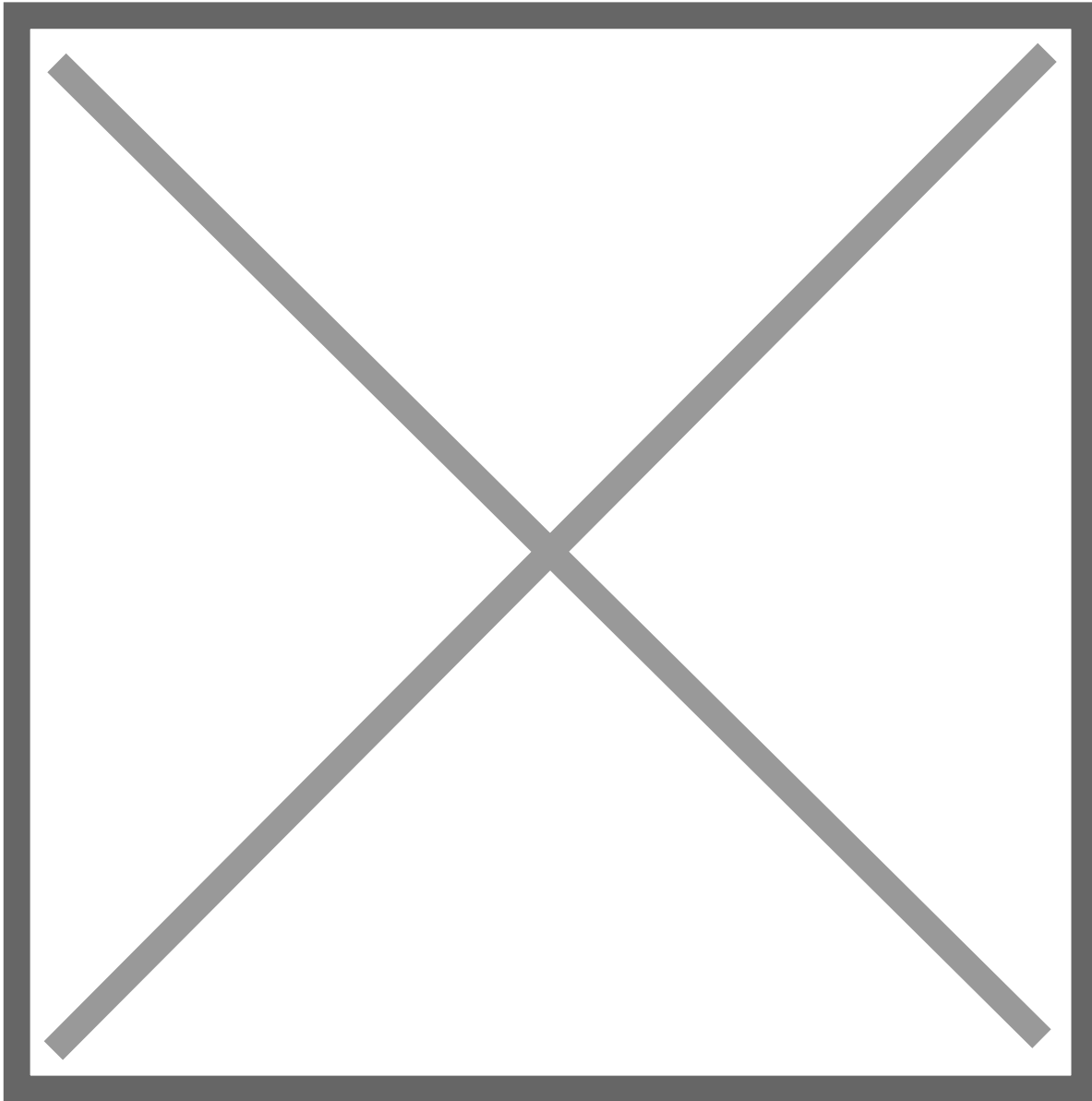
Keep it Simple

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Last week, Berkshire Hathaway released its annual shareholder letter which Warren Buffett has penned every year since 1965. The beauty of the annual letters is how well Buffett communicates complex ideas to a general audience without dumbing down the message.

Brian Fugere, the author of the wildly interesting book 'Why business people speak like idiots' examined annual shareholder letters written by different CEOs. Using the Flesch score – which measures the ease of readability, it was found that CEOs of admired companies with a history of good performance had easy to read shareholder letters (a high Flesch score).

Companies that were later shown to be fraudulent or have illegal insider trading by the CEO had difficult to read shareholder letters (a low Flesch score). The table below summarises the results.



The CEOs with easily readable shareholder letters have done fantastically well for their shareholders as can be seen in the table above.

CEO's with something to hide often use complex and vague language because it creates the illusion of looking smarter than one really is. This was especially clear in Enron's case – their final shareholder letter (before filing for bankruptcy) was incomprehensible. Their aim was to inflate profits and hide losses and shareholders were left holding an empty bag after the accounting acrobatics were uncovered.

This was the similar case in another company called Tyco international which had fraudulent executives. Their shareholder letter, just like Enron's, was incomprehensible and had a low Flesch score.

This of course doesn't mean investing in companies or funds with easy to read shareholder letters will always lead to good results. However, unnecessary complexity may be a sign to head for the door.

Why is all this important? At Tacit, we believe simplicity is an underrated trait in the investment industry. When selecting funds and equities to invest in, people are attracted to complexity because of its inherent appeal. Complexity however creates a false sense of security which can lead to overconfidence. At Tacit, we know the boundary between what we know and what we don't. As Mark Twain said "it's not what you know that gets you into trouble, it's what you know for sure that just isn't so".

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