Transcript

Conversation with Michael McCloskey

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Summary

Michael McCloskey is the founder and president of GreensKeeper Asset Management. He is one of those rare-to-find people who has a flare for both numbers and writing, which he, according to his own admission, learned while studying law. In fact, he has a BSc in mathematics, as well as both a JD and an MBA degree. After spending the initial years of his career working as a lawyer, Michael joined Sprott Securities as an investment banker, where he gained industry experience, before founding GreensKeeper in 2010. Today Michael lives in Mississauga, Canada with his wife and two daughters.

Although Michael has loved the market since he was a kid, it was in the early 2000's that he came across the annual letters of Warren Buffett and, like many others, was soon inspired to pursue the path of value investing. He has attended several Berkshire Hathaway meetings since then, and during the last years has also taken his daughter along with him.

In fact, family plays a big role in Michael's life. He takes pride in having a great relationship with both his sister and his brother, James, who is also his partner at GreensKeeper. James' outgoing personality and communication skills complement Michael, who describes himself as fairly introverted, very well.

From the way Michael talks about his interns, it is clear that he is very passionate about teaching. He is proud of his students, whom he calls alumni after they've completed their internship with him and proudly displays on his website.

Based on the same principle of sharing wisdom, Michael recently decided to write and publish a research report on Visa. As a long-time shareholder of the company, this gave him the opportunity to do a deeper dive again and analyze the industry. Moreover, he used writing as a help to clarify his thinking and test himself in a sense. In the report, he analyzed the different disruptors in the payment networks industry and the possible risks Visa could face in the future.

Ultimately, Michael came to the conclusion that it is more likely than not that the payment networks are going to continue to survive and thrive, and he has not found anything wrong in the numbers. Nevertheless, he is aware that there's a lot of uncertainty around the business and its economics, which is why he plans to continue closely observing any changes in the industry.

Going into detail about some of these risks regarding the credit card networks, Michael talks about potential competition like China Union Pay, and their difficulties in trying to recreate networks similar to Visa and MasterCard. He also talks about Buy Now Play Later plans and makes a comparison to credit cards on various levels, such as the gross volume of the two markets.
An interesting point is also made about how the network of networks effect of Visa and MasterCard often leads to smaller competitors having to be plugged into their already existing big networks.

Reflecting back on his time spent studying mathematics, Michael admits that what he misses most is the certainty of knowing there is an answer and realizing when you get it right. This is in stark contrast to the world of an investor, where one has to make decisions based on imperfect information.

Who is Michael McCloskey?

Guy Spier: (00:00:00)

So, welcome everybody. Today I've got Michael McCloskey, to have a conversation with him about many topics, not least of which I hope will include credit card networks, Visa, MasterCard, and perhaps even AmEx and one or two other companies. But I just want to get the introduction to Michael. Michael, and I'm just reading this from his wonderful website, you should know who he is. Michael has s got 25 years of experience in the securities industry. He's one of those few people who's a JD and an MBA. He worked at Sprott Securities; Eric Sprott is an extremely well-known guy. Michael has done IPOs, he's done debt and equity financing, he's done M&A, a whole bunch of legal stuff. But Michael is also, he studied mathematics, so that's a something to my own heart, and did an MBA. So, he is one of those people who's kind of got both sides covered.

Guy Spier: (00:01:04)

I know many people, well, I know some people who are good with numbers and math type topics but can't really express themselves very well or write very well. And I know people who write extraordinarily well, but you try and flash a number at them and they're not so great with numbers. So, that's Michael. He's now running a fund not dissimilar to mine. And this year at the Berkshire meeting I got to meet, I got to see you in a new light, Michael, because I saw you with your daughters, which is a whole different thing. And what's so special is that I saw you as a protector. So, Michael has these two lovely daughters, well, actually it was just one daughter, and the other daughter was a friend. So, maybe you'll talk about your other children. But I saw you as a strong male protector, I saw you in a different light, which is wonderful. But there's the introduction. I'm just going to give Michael the opportunity to respond to that and maybe correct anything that I got wrong. So, blast away.

Michael McCloskey: (00:02:07)

No, you nailed it Guy. And you're very kind, so thank you for that great introduction and the opportunity to speak today. I was looking forward to today. I was mortified when Chantal first came up to me at ValueX and said, “Oh, Guy read your memo on Visa, and he wants to do a podcast with you.” And I'm a fairly introverted guy, so I'm like, “Okay”, <laugh> the short reaction was almost panic. And then I said of course I'd do it because you've been so kind. And I've gotten so much from what you created with the ValueX community. But we can go on this discussion wherever you'd like. My career, Berkshire... So, I'll tell you a couple stories about Berkshire. You know, I used to go to the meeting. I've gone years, I've gone about five times. I've gone in the past, on my own. And it wasn't nearly the experience. It gets better every year. And having met you and other people within your network, you know, the other events this year, Matt Peterson's event and Anuj I ran into again, I hadn't seen him for years and he sat with us and it’s just wonderful.

Michael McCloskey: (00:03:13)

And my daughter originally was like her dad, she was into sciences in her undergrad, and she was going to be a doctor, that was her plan. And then, I think in her first, end of her first year of university undergraduate, she said, “Papa, I don't think I want to be a doctor anymore.” You know, it just didn't appeal to her. And I said, “What do you want to do?”, and she said, “I don't know”. And I said, “Well, come on, let's go to Omaha.” And this would've been I guess two years ago, maybe three years ago. And there was a conference beforehand, I think Robotti and Company put on and I took her to that because she always knew I invested, but she didn't really know what I did. And you know, she knows I was in love with Charlie and Warren. And so, when I took her to that, I said, “Look around this room”, and there were maybe a hundred people and I said, “There's only three women in this room and it shouldn't be that way, and it doesn't need to be that way. And this is an amazing career, if it appeals to you.” And I wasn't trying to say, you know, “do exactly what I do”. I was just saying if she had an interest. And so that started her journey and she really enjoyed the meeting, and I've introduced her to some people and now she's working for one of Canada's Bank.

Michael McCloskey: (00:04:15)

So, I'm extremely proud of her as you can tell. So, I brought her again this year with her friend, who's also on that path. She's her best friend. And I just had a call with her friend last night. She has an opportunity in the industry. And so yeah, I just, I enjoy teaching and I think that part of that is just Warren and Charlie, you know, exposing other people to the value investing religion. And I'm proud of them. And I really enjoy watching them grow up and broadening this community. And it's, you know, when I talked to them about what they enjoyed the most about the meeting and it was the people. I mean, they were in awe of you and Chantal and, you know, Matt and all these great people, because they're so welcoming and friendly and so smart. And it's intimidating for young people when they're around these people and they're literally in awe of you. And yet, you know, I think most of the people in the community are totally down to earth and quirky. I would say we're all a little bit quirky. And so, Berkshire and the community around it, I think you've talked about what you've built around the meeting itself. It'll be interesting to see if that continues decades from now, but, you know, kudos to you for what you're doing.

The Connection to Berkshire Hathaway

Guy Spier: (00:05:29)

Well, that's really kind. You know, I have a question that I won't ask you right away, which is to kind of try and figure out how you came into my life. But before we go there, and we went to the Berkshire meeting, so maybe you can give the story of your relationship to Berkshire Hathaway, how long you've been coming to the meeting, when you discovered the company, if you want to share whether you own shares or not.

Michael McCloskey: (00:05:54)

Sure. So, I'll start with your last question. I do own shares, and like you, I've read your annual reports, it is public information. I see it as ballast. It helps me to feel comfortable taking more risk with the rest of the portfolio. And I know it's going to do fine and maybe it's not going to give me the best return. Although, it was fortuitous when I started my fund right around the time I started, it was trading at just a hair over book value. This would've been 2011, I believe, late 2011. So, it was cheap. I thought it was, fundamentally it was cheap, but I haven't sold it. And, you know, I think it is going to continue to compound for years to come and it's served us well, especially in what's happened over the last few months. So, I do own it.

Michael McCloskey: (00:06:36)

My journey, I mean, I'm a math geek. I was always a math geek. And I fell into law because I didn't get into business school, which was the whole purpose of going to the undergraduate university that I did, and partied a bit too much and didn't get in. So, my roommate from undergrad was a lawyer or was going to law school. And I said, that sounds like a good idea. And on a lark, I wrote the LSAT and got in and did my MBA. And so, I actually practiced law, which helped me to write. I mean, you talked about the analytical side. I was a terrible writer in university, but law really taught me that words matter, how you structure things, how you think about things, on top of learning the securities law. So, that was very helpful part of my career.

Michael McCloskey: (00:07:22)

But I've always loved the market since I was a kid. I think a lot of us have that bug. And so, when I joined a group of young men and women in the early thirties to buyout Eric Sprott, we did a management buyout of his investment bank when he separated that from his asset management business. I was fortunate enough to cover the financial services sector. And one of our analysts there, Jason Donville was his name, he was a partner of mine, he was a Buffett fan. And so, I'd always heard about Warren and Charlie, but I'd never really known about him. And he had this binder on his shelf, and it was the annual letters from Warren all the way back from the seventies and maybe even the partnership letters in the sixties. And so, I said, "Can I borrow that?", because he was always talking about Buffett return on equity. And so that started my journey, just starting to read those letters.

Michael McCloskey: (00:08:09)

And then I discovered the intelligent investor in the essays of Buffett, and it just clicked. And many investors have talked about whether or not it makes sense, and maybe that's the mathematician in me, it just made sense. And so, since then, again, I, you know, got into this investment business thinking I knew what it was all about. I knew nothing, and I figured it out. And then even after a few years of figuring it out until I discovered how they do it and how they teach, that's how it should be done in my opinion. And so that's been my journey and how I found them. And I've been going to the meeting, I think I've gone five times. The first time was probably in '06 or '07, that timeframe.

Guy Spier: (00:08:50)

Fascinating. It's always interesting to hear how people come into the Buffett orbit. I can tell you that was, I have to confess that there are a couple of years in 96, 97 that I missed, but other than the COVID years, so in the last 25 years I've been to something like 22 or 23 of the meetings.

Michael McCloskey: (00:09:10)

It's impressive.

Guy Spier: (00:09:11)

And what is really amazing for me is that, I mean, so this is my 23rd meeting or 22nd, I don't remember exactly what number, and I come away with really profound learnings. And I think that, but they're not necessarily intellectual learnings, they're things that I can put into action. And so, I mean, I could share my learnings from Berkshire. But yeah, and it was fun. So, for the viewer's interest, for the first time I had my, we have a new title for Chantal. Her title is, just for fun, chief of staff. There's a story behind how we got to that. She could also have any other title that she likes, but she's extraordinarily well organized. And so, we put on a meet and greet, which was a really interesting experience. It was really, really fun to do. And we will modify that next year. I can update you sometime Michael, on how we're going to modify it. It'll be way better next time, because it was a bit of a crazy time, at least for me.

Guy Spier: (00:10:18)

And what this podcast allows me to do is kind of to grab you for like an hour and a half, or however long we get, and just ask you all these questions, grill you in ways that, and dive deep on things that I would not necessarily otherwise be able to do. Can you tell the story, the first time I remember engaging with you properly was at a Jeffersonian meal in Toronto, but can you tell the story about how you ended up in my life from your perspective?

Michael McCloskey: (00:10:46)

Sure. Well, it's kind of like law school; it was just fortuitous. I have a friend in Toronto who runs a fund, Dan, I'll leave his last name out in case he doesn't want to be disclosed. And he knew John Mihaljevic, I may not be pronouncing that right, and his brother. And so, he introduced me to the two of them, and John's brother did an interview of me in Toronto and Dan said, "Well, I've been going to this conference" – I think that you and John used to run ValueX together originally when it was in Zurich and Klosters.

Guy Spier: (00:11:16)

That's right.

Michael McCloskey: (00:11:18)

And so, Dan had managed to secure an invite. And I think the year after he went, or maybe two years after, he said, "You should come to this, Mike, you'd really enjoy it." And it's like your invitation to the Jeffersonian dinner, my initial reaction is, "now why do I want to do that?". I'm fairly asocial and almost antisocial. But I decided to go, and I enjoyed it a lot. So, Dan was my introduction. Thank you, Dan, for including me. And I came that first year and I came away, it was intimidating, Guy, because there's 70, 75 people that are extremely smart. I'm, as I said, I'm not that social. But I remember you saying something, I don't remember if it was the first year, but it was something to the effect that, you know, welcome to the land of misfit toys, that old Christmas special that I used to watch as a kid.

Michael McCloskey: (00:12:10)

And so, it was kind of like, it was a place where I was like, I actually think I like these people and maybe I'll go back. It was a little bit scary. And I kept going back and working at it, you know, because of my own personal social quirks, and now like I love it. And I put in the time, and these are people that I trust and because of the principles you've created where it's confidential, no one's there with an agenda, we're there just to learn and help each other. And you've created this wonderful community, and I've made some great friendships and gotten to know you better and other people. And so, again, it's kind of like the rest of my two earlier careers, you know, I just accidentally fell into it and it stuck. And so, I plan to keep coming until you throw me out.

Guy Spier: (00:12:54)

<laugh> You know, nobody gets thrown out unless they behave really egregiously, so that's not going to happen. But the reason why that's an interesting story for me is that what we all have got to do more of, I think, is be who we are – we certainly have to be who we are – but be who we are for the world to see. And when you start doing that, you start attracting people from afar into your life and into your circle, that is a wonderfully highly selective group of people. And so, from all of the people in Canada, from all of the people into Ontario, I've got somebody in your case you, who's coming to Switzerland every year, who's got so much to contribute. And there's so much that one can assume already about the mindset from the Berkshire Hathaway meetings, from value investing, from being about substance and not about show, all those things.

Guy Spier: (00:13:58)

But what is exciting for me is that, you know, I put myself out there in various ways, and then you select yourself in. And so, there's this feeling of an acceleration and a feeling of, in a certain way, hive mind, using other people's minds or benefiting from other people's minds. I mean, this wasn't even direct. It was Dan who said, "Michael, you should consider going to this conference." And so that's just super exciting for me and interesting and fun. I want to go back to your website, to your company, because first of all, I see that you work with your brother and that's fascinating and I'd love to hear more about that. And then I want to ask you about some of your research associates. But your brother is very prominently displayed on the website next to you. Tell me about your brother.

Importance of Family

Michael McCloskey: (00:14:54)

He's got a big personality. So, my brother has two jobs. He's a real estate agent as well, but he has some spare time, and the real estate industry is cyclical. So, I've always said to James, if you have any interest and some capacity, I'd love to have you work with me, because we both, I'm very close with my brother and my sister. Family's very important to me, as you can tell from my relationship with my daughter. And so, my brother is the polar opposite of me in many ways. And one is that he is the life of the party. I mean, he would walk into any room and know everybody there and people would love him. And so, our personalities are just very different, so we just complement each other so well. And so, James is really out there just telling people that, you know, I'm the math geek who actually is good with numbers and, you know, knows how to invest money. And he's out there building relationships and telling people about our firm and what we do and me. And that's a part that I'm very uncomfortable with, and I can do it, but I don't like doing it. So, I try and avoid it as much as possible. So, you know, my brother's been a godsend to help create awareness for the business.

Guy Spier: (00:16:03)

And for those of you who are listening from a car or something, so I'm looking at a photograph of James and first of all, he's got kind of a square jaw. And I see in the bottom of the profile that he was a member of the veneer club champion football team. So, it doesn't necessarily say that he's a big football player, but you see a guy who's quite gregarious, and in that way probably the polar opposite of you, Michael. And it's funny because what you said about being out there and talking to people is something that I feel like I identify a lot with, and for the longest time I'd have inquiries, new business inquiries coming in and I was too afraid to call them up, and I'm still afraid to call them up, Michael, it's just hilarious.

Michael McCloskey: (00:16:56)

Maybe you’re just worried of rejection, Guy. And don't answer if that's too personal.

Guy Spier: (00:17:00)

No. Yeah. I mean, would you like to be my therapist? <laugh>

Michael McCloskey: (00:17:05)

No. <laugh>

Guy Spier: (00:17:08)

I'm sure that's a part of it. It's fascinating because when I tell people that I'm an introvert, many people are like, “you're not an introvert”. But I think that the skill, the extroversion that I learned are kind of skills that I learned in order to get along in the world, they don't come naturally to me, if you like. And I'm much happier being a creature quietly on my own. And by the way, either now on this podcast or some other time, I believe that there are techniques that one can bring to bear on minds to the extent that your and my mind are similar, that can help us to do better on the extroversion front.

Guy Spier: (00:17:50)

And I think that that Warren, that's why Warren Buffett has that – and this is a kind of a, this is not a new idea, I've heard it many times – the Dale Carnegie graduation certificate. Because he was also extraordinarily introverted, perhaps a little Asperger's, and he didn't know how to get along with people. And he had understood that getting along with people was part of what makes your success in life. And then the Dale Carnegie stuff really helped him to acquire the practical tools to do it. And that's why he's so good at remembering people's names. He realized because, you know, Dale Carnegie's got a whole chapter on the most beautiful sound in anybody's mind is the sound of their own name. And so, Warren kind of went for that. And actually, none of that stuff comes naturally to him. There's hope for all of us. If Warren can do it, then the rest of us can do it, is what I think.

Guy Spier: (00:18:47)

So, what I'd put to you, I don't know if I hit pay dirt with this, is that it's not what you think it is. So, the skills to be, so, first of all, somebody like you will never have a big social battery. So, you know, my wife and I, maybe it's like your brother and you, my social battery lasts about two hours, even in the best of circumstances. Like even if I go out with you, you know, I'm good for like two hours, and then I need to go do something else. Whereas Lory, my wife, she's good for about five or six hours or more. I'm never going to get beyond the two-hour social battery, but there are things that I can do to engage with people better. And part of it actually is just to select the group. So, you know, we're all perfectly social at ValueX, because <laugh> we're amongst like-minded oddballs, you know?

Michael McCloskey: (00:19:40)

But even within ValueX, Guy, I won't say the name, but I was sitting beside someone, I had a really good chat this year and I hadn't spoken with him much in prior years. And during a break, he said to me, “I need to go to my room for a sec.” I'm like, “Sure”, and he says, “I'm just, I'm really introverted. And I need a rest.” And it was really just, you know, that stimulation. And he knew himself and I thought that was terrific. Like with our group it's okay, I get it.

Guy Spier: (00:20:05)

Absolutely.

Michael McCloskey: (00:20:06)

People exhaust me and I suspect that they do you, so in small doses it works, and just know thyself.

Guy Spier: (00:20:14)

Yeah, exactly. And, you know, people exhaust me, but then at the same time I have an extraordinary amount of time for total weirdos if I enjoy their mind. And so, Lory, my wife, you know, I have all these weirdos that I want to bring over for dinner and I'll forgive them all sorts of other things – I've just insulted most of my friends at this point, because I've just called them all weirdos – but I'll forgive them all sorts of, you know, things that can be quite unpleasant actually in a general social setup. So, while I have a short, my fuse is way longer for people that I'm genuinely deeply interested in, if they have things to say that I wouldn't hear elsewhere. What you've described with your brother is two very different personalities who are able to get along. And I just want to honor that because I don't think that that necessarily comes easy in many families. And I'm just curious, were there ever times when you did not get on with your brother and were there times when your rivalry was strong? And if there are, how have you managed that relationship?

Michael McCloskey: (00:21:23)

Yeah, it's funny, I've never really thought about it as an adult. But sure, when we were younger, so I was always very socially awkward, and he was always gregarious. So, he had a lot of friends, and I was, to be honest, I was jealous of that. And so, whenever I had a friend, you know, I was probably pretty protective of that relationship, and it created friction. And if he wanted to play, then I would, you know, get mad and call my mother and say, James is doing this. And there were probably other times where I piggybacked on his friendships, even today, I mean, my brother's closest friends are friends of mine because I just leverage his magic, he's a human magnet. But I mean, as kids you fight, but as an adult no, we've always been fairly close.

Michael McCloskey: (00:22:09)

And same with my sister. Her personality is kind of between my brother and I. And I mean, she's the smartest of the three of us and very successful in her own way. But my parents I'd say, Guy, that, you know, this moving a lot more to my mom is like, they did a great job of just showing us unconditional love. And when we were brats and needed to be corrected, they did that. But family was very important to them and to us. And so, my brother and sister and I, like we would literally give each other our last dime and shirt off our backs. And as adults we have great conversations because we're honest with each other and they're intelligent and I value their opinion. So, I'm fortunate that I'm very close with my family. And it's a big part of my life.

Guy Spier: (00:22:54)

I would actually be very interested to do a deep dive with you on that because I think that, you know, Leo Tolstoy said that happy families are all happy in the same way, but unhappy families are all unhappy in different ways. I don't know if that's true or not, but to get to a place where you are in a basically happy family is perhaps obvious to those people who are in happy families but is not obvious to people who are not in happy families. And I happen to think that that is not given. I think that in many cases you can work at it. You can't overcome a drug abuse; you can't overcome mental disease, and there are some families that are broken by those things. And I think that if God forbid violence occurs, then it may be hard to overcome those. But bar those three things, I think that you can learn to become better. There are so many of these things which are a bit like learning to ride a bicycle.

Guy Spier: (00:23:58)

And my sense is that, you know, some families get to it naturally, but if you're a family that has not gotten to it naturally, don't think that all is lost. It may be that you just, you know, some people kind of just were lucky to be able to ride a bicycle first try, and other people need some training wheels and some coaching and some other things. We had a family therapist come into our life in our family about two years ago and he's been extraordinarily helpful. I'll name him, his name is Philip Trenchard, he's based in London. He'll be happy for the shoutout. But we go to him with all sorts of things. And early on in the relationship with my wife, we learned all sorts of active listening techniques for the relationship with her. But I think when you go beyond that, I think that's a place of extraordinary richness. And funnily enough, it's only because I'm looking at your website that I see that.

The GreensKeeper Alumni

Guy Spier: (00:24:49)

So, I'm going to go somewhere else on your website, which is that you got some, first of all, I love the look of the guys you got working for you, and you also put the graduates down, which I just think is lovely. So, you call them alumni, which I think is just great. So, I'd love to hear about your junior analyst program and the alumni of your junior analyst program.

Michael McCloskey: (00:25:17)

Sure. So, the whole thing started in March of 2020, I mean, it was when the pandemic happened. And one of my daughter's friends who you met in Omaha, Sarah, needed a job. And she has a good mind and she's a good worker, and so, I said, “Sure, why don't you come work with me for the summer?”. And part of that just comes from Warren and Charlie's generosity over the years of teaching. I like to teach, I like to share the wisdom, you know, I didn't invent it. I'm just telling people what I've been taught by our heroes. And so subsequent to making her an offer, the government of Canada said, you know, because of the pandemic we're really looking for jobs for students. They're really having a hard time, and the government made subsidies available. So, I said, oh, why not? You know, out of pocket wasn't that much. And if I can handle one, I can handle two.

Michael McCloskey: (00:26:14)

And then, so I made an application and then they reached out to me and said, you know, can you take more? So, I ended up hiring four that first year, which was a little too ambitious, because they exhausted me and I'm in my fifties now, so it was difficult to keep up with them. And to create a program, I'd never really had a formal training program. So, it was all new to me. And so, I had four of them work for me that year, and they were all graduates of, I'll give a plug to the Ivey School of Business at Western, which is my Alma mater, although I didn't get into the business school, and my daughter reminds me that she did, to this day. <laugh> But it's a fantastic school. And it has a place in my heart, the school, because it was some of my best days.

Michael McCloskey: (00:26:54)

And so, I just had four young people that I think had the attributes to be really good investors. They were numerate, they were curious, they were smart, they were hardworking, they were readers. So, they checked all the boxes. And that's how it started, Guy. You know, I hired them for four months and then they went off back to school. And then I was a little smarter the second year and only took two because it was more manageable for me. And I created a bunch of materials that we go through over the first two weeks. And it's really just fundamentals: how I value a stock, you know, how to look at investing from a value investor's perspective, return on capital, all kinds of reading, psychology, like *The Psychology of Human Misjudgment* by Munger. I just took all of the key learnings and gave them pieces of it. And then we just picked stocks all summer. So, that started, I guess I've had eight of them. I have two this summer with me. And the firm's growing. So, you know, potentially one of these people will join us full time in the future.

Michael McCloskey: (00:27:59)

And, you know, another one that worked for me that very first year was in Omaha as well. He called me – hello Parker – he called me, and I told him that I was going to Omaha, and he says, he's working in the business now, and he said, you know, “Someone on my firm mentioned, ‘Are you going?’”, and he said no. And I'm like, “Are you an idiot?”. Your firm is telling you that it's okay to go, you're going to love it. So, we ended up meeting him in Omaha very briefly, but of the eight, I guess I've got two now, but of the six that have previously worked for me, all six are still in the financial industry. And most of them are not necessarily value investors, but they're in the industry. So, I think I've had a good track record of identifying people with the right skillset. And when they talk to other people, like they enjoy the experience. So, I get a lot out of it, you know, I really do. And I get their work product too. So, you know, it's not charitable, you know, and I pay them. It's been a good experience for me, and I really enjoy it.

Guy Spier: (00:28:56)

Well, I like the title of junior analyst because my experience that I wrote about in my book with a full-time analyst is that it can lead to difficulties in the relationship for all sorts of reasons. And the idea of a junior analyst kind of like makes it clear with the title that this, you know, the professional expectation is that the person will move on perhaps to a different firm to become a senior financial analyst. And I find it interesting that Warren Buffett had analysts of various different kinds working with him, but they were, they kind of moved on to other jobs at some point or other. So, that's kind of just interesting to me. And it seems like you're perhaps following a similar kind of model. I would also tell you that I suspect that each one of these people, I mean, I would not just suspect, you've put them on your website, so you're an ambassador for them, and I'm sure that they become ambassadors for you.

Guy Spier: (00:29:51)

And I kind of, I haven't called anybody who's, I call them interns, I haven't called them analyst, but I kind of explained to them that the benefit to me is that 10 years down the road, if they're in some meeting where my name comes up, that person will be able to say, that graduate as you call it, or alumnus will be able to say, “Yeah, I know exactly how Guy is in the office, I spent X amount of time with him. So, let me tell you how it is actually.”, which is always a good thing. But it was really pleasing to see actually, I really enjoyed, and you've got them prominently, so you're not kind of hiding them in the background or something.

Michael McCloskey: (00:30:28)

No, I'm proud of them. I'm proud of them and the fact that they're thriving. And like I said, they still call me on occasion for advice. And I like that. And it just makes me happy. I have no agenda. As you say, maybe one of them will come back to the fold eventually, once, you know, they discover what they want to do. And they're just starting their journey. So, I get a lot out of it emotionally. And so, thank you for noticing that.

A Research Report on Visa

Guy Spier: (00:30:52)

Yeah. So, I'm going to move on to this kind of document that you produced in 2021 on Visa. We're going to dive into, I guess you could call it a stock pick for you, but you also produced a very, very nice kind of research report that was well researched. It was thoughtful, it's dense with insight and information.

Michael McCloskey: (00:31:16)

Thank you.

Guy Spier: (00:31:18)

I'm curious if you can tell a little bit the story of how and why you decided to make that report. So, I guess we'll do, we can dive into the rationale for Visa and we're going to sort of like end or take the second half of our conversation into financial services and all of that. But it's just interesting to me, you're an investor, your clients probably don't care. They probably say, “Michael, invest our money as you see fit”, but you chose to write this idea up. And I'm just curious what drove that thinking.

Michael McCloskey: (00:31:58)

Yeah, there were a couple reasons. One of the things, this may surprise you, you talked about it a few years ago of a memo that a fellow ValueXer, I think it was Bryan, had put out on an industry. And I think you called that a white paper, I remember you talking about it.

Guy Spier: (00:32:15)

Correct.

Michael McCloskey: (00:32:16)

And it was the idea of just throwing it out there, knowing that it was an unfinished document, to share with other people and get their reaction to make it better. And so, I did it for a couple reasons. One, I've been a shareholder of Visa for a very long time. And so, you know, everyone thinks they're going to be disrupted, or recently that was the narrative. So, it gave me the opportunity with the stocks pullback to do a deeper dive again and say what's happening in this industry. And I find that, you know, just with my personality, I like to write, not as much as our friend, Vitaliy, but I do like to write because it clarifies thinking. And when I'm writing a section, if I'm uncertain about what I'm writing or I'm not clear, that tells me that I don't know the topic well enough, go back to the Feynman method. So, one, I did it for my own. It's testing myself to say, do you really know what you're talking about? And if not, let's get it right before you put it out there. Secondly, there's an institutional platform called sum zero. I'm not sure if you're familiar with it.

Guy Spier: (00:33:20)

Of course.

Michael McCloskey: (00:33:21)

So, they will give people like you and I free access if we publish twice a year, or we pay thousands of dollars. And I'm a value investor and a cheapskate, so I don't want to pay thousands of dollars, I'll put ideas out there. But really, you know, when it was to clarify my thinking, but secondly is, and it's scary to do this. I even posted it I think on our ValueX WhatsApp chat. And that was scary for me because I don't want to look stupid in front of these people. And I respect them and they're extremely smart and they, you know, a lot of them probably know this company better than I do. I think, you know, I think you've owned the credit cards, one of them, for some time. So, you know, that pressure makes me take it seriously. And when I put it out there, you know, I reread the memo in preparation for this talk. And since then, I listened to a bunch of podcasts recently on the industry, and there's a couple things where I've changed my mind a little bit.

Michael McCloskey: (00:34:13)

So, it was really that putting yourself out there, as scary as it is, to try and learn. And if I'm wrong, I'd rather know that I'm wrong before the market tells me that I'm wrong and then change my thinking and change my position. I still believe in the thesis, you know, I'll always reserve the right to change my mind. But it was really what you said about putting an idea out there and then waiting for or allowing other people to give you feedback or criticism. And Twitter's great for that too. I put it out on Twitter, and you get some really, I mean, you get some nasty stuff and that's fine. That's just the way the world is. But even the people that really disagree with you, if you take away that initial reaction to just dismiss them or, you know, saying this person's an idiot, and listen to what they're really saying and saying, are they right? If you keep that open mind and do the work and try and understand it from their perspective. A lot of people said they'll be disrupted by what's happening in India or Brazil. And I did the work, and I came to a different conclusion. And that's a long answer to your question, but that's really why.

Guy Spier: (00:35:22)

Yeah. And just for the listener's interest, that was Bryan Lawrence, who has now got a wonderful podcast with Stig Brodersen. And what Bryan said, the original white paper that I saw from him was on the oil industry. And what Bryan said was it was a little bit like downloading a little piece of his brain. And you are, you're sharing a little piece of your brain with other people. And the feedback is fascinating. And I have this formula, which you're welcome to adopt with, you know, you don't have to pay royalty or even attribute or anything, which is to invite, and I got this from Bryan, is to invite the reader to provide commentary. And that the commentary would be reincorporated into future versions of the document. So, it becomes kind of a group learning exercise, kind of like a group Wikipedia that's kind of managed by one person. And what I found was that when I quote the comments in subsequent versions of the document, not all, some are introverts, but many love to be quoted, they like that. And that actually adds to the information flow, which is kind of fascinating.

Guy Spier: (00:36:34)

The other thought that comes up for me that, forgive me if you've already heard me say it. So, David Perell is not a friend. I've never met him. I haven't done any of his online courses, but he talks about two things. He talks about many things. He writes essays online, he's a teacher. But two of the big lessons that I have from him, one is this idea of learning in public, which is not just his idea, but it's also, it's the same as the white paper idea, which is that the minute you expose your work to the world and you overcome your fears and your imposter syndrome and all of those things, you set in motion an extraordinary dynamic. And I was expressing this to somebody else, but it's so powerful, Michael. So, we're all, most of the time, being consumed by the algorithm. Our attention actually is the product that is being delivered to advertisers via Facebook, whatever social media and other things that we use. But when we create content of any kind, now we can put the algorithm to use for us, because when we post that content on Twitter or on YouTube or wherever it is, YouTube now wants to get eyeballs and will find your particular version of crazy. So, you know, they'll find the only other person in this world who has strong family values and is really interested in the credit card networks, you know. <laugh>

Guy Spier: (00:38:09)

And so, David Perell has this wonderful chart in which, what technology does is that the average gets worse, but the people who are good get really, really good. And he kind of talks about this, for example, dieting habits in the United States. So, a lot of junk food in the United States, and a lot of people have very, very bad health around bad eating habits. But you also have in the United States some of the fittest healthiest people around. So, the people who focus on the right things can get the very, very best. So, the way we benefit from this new environment is not by allowing it to consume us and deciding who we want to be, and then putting ourselves out there. So, I want to honor that, because having, you know, it's easy to talk about it, but it's really, really hard to do.

Guy Spier: (00:39:01)

Just briefly, I talked about two lessons from David Perell, the other thing that David Perell says is that never before has there been such an extraordinary return to writing. And it's really the same idea, but the key is, you know, I have so many people who get in touch with me, and they want to have a one-on-one conversation. And kind of what I want to tell them is write your questions down, write your thoughts down and don't just expose them to me. It's a very inefficient way to talk to somebody or to engage. You sit down and, who knows how many people have read your Visa write up. I'm sure many, and I'm actually curious, tell the story of the document. Who did you meet through the document that you have not met otherwise?

Michael McCloskey: (00:39:49)

Well, Twitter is an amazing resource, I think they call it FinTwit, people like us that use it to help us with work and, you know, complete strangers have read it and provided comments and even direct messages privately, where we've talked about the economics of the business or what's happening in the industry. I don't really have much of a social media profile. I mean, I put things out there, but, you know, I probably added a hundred and something followers right after the memo went out. So, somebody's reading it. And, you know, most of the comments were very respectful, and some people agreed with me, and some didn't. So, you know, are these people, I don't even know some of them, I still don't know who they are <laugh>, but I've had some pretty intelligent conversations with a few of them and thoughtful conversations. And it got me to think about a few things differently, and it made me better, you know, in terms of understanding the business and the potential threats. And in ValueX there were a few people that when I shared it came back with different thoughts, and some people in our community look at some of the disruptors like Gagen and Stripe. So, I'm still learning. But it was, I got something out of it, you know, once you get over that fear, like you said, and you put yourself up there, it can be very helpful.

Guy Spier: (00:41:07)

So, I hope you'll forgive me for these questions. I'm curious why you did not put an email address for yourself or somebody at your firm in the document, or is that an oversight?

Michael McCloskey: (00:41:21)

Well, I don't even know if it's an oversight. I guess the way I figure it is if someone wants to find me, I'm out there, it's pretty easy for them to find me. And I'm not really putting this out there for the purpose of marketing that, you know, I'm some genius, and this is a great stock idea. It's really, I'm there to give you my thesis and share my thinking on the name. And if you can come back to me with something different, then that's really what I was looking for. I wasn't looking for customers by putting this out there and if I get one terrific. And maybe it's, as my brother would say, I'm just a bad marketer. <laugh> You know, I probably should have had my- <laugh>

Guy Spier: (00:41:59)

So, now maybe without you requesting, I'll be your therapist for a second. And so, the audience, I don’t know if the audience will see how, so isn't it fascinating – I'm imagining our audience here with me – how you went straight to associating putting your email into the document with marketing? Which is funny. That might be a consequence, but I believe that out of the, you know, they say if you get a letter written to you, a thousand people thought the same thought, that's something, I read that somewhere. And what I would suggest is that there were many people with other comments, and interesting comments and insights, that they didn't rise to the level of wanting to figure out where to find you, but if they could have just clicked on an email, they might have written, “Hey, I'm the CEO of MasterCard. I'd like to talk to you”, <laugh> or something like that. And so, it's really not so much about marketing your fund. It's about actually generating more conversations, more interesting conversations. And so, for what it's worth, look, you know, I think it's a really wonderful piece.

Michael McCloskey: (00:43:15)

Thank you.

Guy Spier: (00:43:16)

And by the way, that's what prompted me to want to talk to you. And I can talk a little bit about, well, I've learned that in podcasting, you don't want to talk to people who haven't written something because they haven't figured out their thoughts. So, now you talk to them and they're kind of not clear. Whereas when people have written something, and by the way, Michael also writes a wonderful investor letter, then you know that you're going to get something really good. But so in my experience, when I go to the effort of producing a white paper myself, or in collaboration with somebody, or with a third party, not only is their email in there, but I actually want to capture every single time somebody sees it, because it's kind of like that person looking at it may not realize it, but they're part of my future, so to speak. I don't know when I might want to email that person and say, "I know you looked at my white paper on zero management fees, and I thought you'd be interested in this", or "I'd like you to respond to something".

Guy Spier: (00:44:12)

So, interestingly enough, one of the people at this year's ValueX, for the benefit of the audience, he's in the public domain so no problem talking about him, his name is Syed Balkhi, and he did a review of our website. He's the CEO of a company called OptinMonster. And the first thing he said, so he said, "You're not capturing 90% of the visitors coming to your website." And my response was kind of not dissimilar to you, I was like, "Well, they're all riff-raff anyway, and I don't want to capture them." And he said, "No, you're wrong, you do. Because you don't know when, you know, you're playing the long tail, you're playing a numbers game." So, we could go on and on about it. I think that, you know, I'm sure that by Googling or Twitter or going to GreensKeeper website, you'll be able to find Michael and you should, if you have any interest in payments networks, credit cards and various other topics associated with it, you should read it.

Risks in the World of Payment Networks

Guy Spier: (00:45:18)

So, I'm going to dive in with a bunch of questions that I have, if that's okay with you. And just to set you at ease, I am not, you know, this is not like the interrogation, you know. <laugh> I think that I've studied payment networks for 20 years. And sometimes I think I really understand them and then something happens, and I think, "Oh, maybe I don't understand them at all." And so, maybe that's the first question I'll ask you. So, a company that I follow quite closely, and I have enormous amount of respect for them is Ruane Cunniff. And I had noticed recently that they had sold out of all their credit card networks. Why on earth did they do that? <laugh>

Michael McCloskey: (00:46:12)

Well, you'd have to ask them, but my recollection, I don't know if it was something that I read or someone told me, was that they just saw so many people coming at the credit card networks, all these FinTech disruptors and all this technology, and UPI in India, Unified Payments Initiative, or Pix in Brazil. And I think it just scared them that perhaps the moat was being eroded and perhaps the future is going to be more difficult for the credit card networks. And I think they said specifically, if I'm remembering correctly, that there wasn't anything in the numbers that they saw, but it was really just that overall environment was giving them pause as to whether or not the future is going to look much like the past.

Michael McCloskey: (00:46:54)

And I think Charlie Munger said within the last couple years, with his usual witticism, that if you think you know what payments are going to look like in 10 years from now then you're delusional. And so, when somebody with a mind like Charlie says that, you know, there's a lot of uncertainty out there. And I came to the conclusion that it's more likely than not that the payment networks are going to continue to survive and thrive, but boy, there's a lot of people coming at them because of the economics. And it's such a big part of the economy and it's so profitable that there is a risk that somebody breaches the dike and changes the game. But I don't think that's probable, but it's possible. So, I'm watching it like a hawk. But I think that's the conclusion they came to. And, again, I can't speak for them, but that's my understanding of the thesis.

Guy Spier: (00:47:42)

And for the listeners' benefit, what I'm going to do here is not ask Michael to kind of go through the business or explain the business, even. I'm just going to assume that you either know the business or that our conversation about the business will, if you decide you want to learn more, you'll go and read up on it. Because, you know, first of all, it would be a five-hour seminar to go through all of the interesting and very unusual economics of payment networks. So, let me go to, and I'm kind of like attacking the subject from all these bleak angles. You know, Russia is no longer part of the Visa or MasterCard networks. And I happened to talk to an Indian friend who was very excited because Russia is connecting up to other credit card networks or other payment networks. How do you see the fact that a whole country has just been pushed out by sanctions of Visa and MasterCard? And maybe I'll just add in there, China until recently has had a its own version of Visa and MasterCard, called China Union Pay. I think it's called China Union Pay. And they've kind of kept Visa and MasterCard out.

Michael McCloskey: (00:49:04)

Yes.

Guy Spier: (00:49:05)

So, you know, are these competing systems, are they so powerful if they can just be shut out of a whole country just like that?

Michael McCloskey: (00:49:13)

That's a big question. So, there's a couple issues there. Look, any government can keep Visa and MasterCard out of their jurisdiction if they choose to, with a stroke of a pen. That's the reality. But if you're in Russia and you want to travel the world, you want to be able to use a payment network. And Russia when they invaded Crimea five or six years ago for the first time, whenever that was, I think they knew that there was some risk there. So, they created their own system. I think they call it Mir, is the payment network in Russia. And they mandated by law regulation that transactions had to go through those rails and not the Visa, MasterCard rails. But you know, subsequent to the recent invasion of the Ukraine, Visa and MasterCard have basically cut them off. And I don't know if that was the companies doing it or sanctions from the US government. You know, I've read articles of Russians that are in Vietnam or the Maldives, and now they're living in hotels because they can't access their Visa or MasterCards.

Michael McCloskey: (00:50:15)

So, I think China is watching that with great interest, and other countries, you know, India is watching it because it can be weaponized, right, with MasterCard and Visa, AmEx too, to a lesser degree. These are global networks and if you can be cut off by them, do I really want to put my citizens in that position, if for one day we do something and, you know, anger the American authorities or the global authorities? You're seeing it with the SWIFT network too now, with the Russians, where SWIFT is basically, credit cards are networks for consumers and businesses, but between the banks, the tens of thousands of banks around the world, there's this messaging system called SWIFT. And I think Russia's been cut off from that. So, I think long-term thinkers like the Chinese are probably going to say, "Well, should we not create another system?". It's difficult because of the ubiquity of US payments and the strength of the US dollar as a reserve currency, but not impossible. So, that is a long-term risk.

Michael McCloskey: (00:51:16)

But fundamentally, step back, payments are a local phenomenon. Whatever payment system you have within your own home country is a custom that's developed over many, many years. When you look at North America using credit cards and debit cards are just, they're accepted everywhere, they're used by merchants or consumers everywhere. That's the benefit of the network effect. When I pull out my wallet and take out my Visa and my MasterCard, I know it's going to be accepted pretty much everywhere. I know what I'm getting. But certain cultures, in Germany I think, and potentially in Switzerland, I think it's more a cash-based culture where credit is not as well accepted, and maybe I'm wrong on that, Guy. And then you go to places like India, where you've got a big rural population, not as wealthy as the West and you have plenty of unbanked people. So, that payment system hasn't really existed, and you have the small kiranas or shopkeepers, they don't have the margin to give, that funds the credit card network.

Michael McCloskey: (00:52:16)

So, every country is different. But if you're a consumer and you want to travel the world, so you talked about China Union Pay. So, they kept out Visa and MasterCard because they wanted to build their own home champion, China Union Pay. But when a Chinese traveler travels outside China and wants to use their China Union Pay, China Union Pay doesn't really travel the world unless they connect to the Visa and MasterCard network, which is what they've done. So, when you present your credentials, it just piggybacks on those rails. Because it's very difficult to build that network effect globally, across, you know, tens of, well, I'd say millions of merchants, and hundreds of millions or billions of consumers. So, the fact that it already exists everywhere, most disruptors just tend to latch onto their system, because it gives them distribution and solves that pain point. I mean these networks have built up since the 1960s or whenever it was that they launched in California.

Guy Spier: (00:53:16)

You know, there's this amazing phenomenon, we all know it through the QWERTY keyboard, and we could all get a Dvorak keyboard if we wanted to. And apparently Dvorak is far more efficient, and I don't know one person who's actually used a Dvorak keyboard because, and you know, the QWERTY keyboard is demonstrably inferior in all sorts of ways, but it's become the standard. And, you know, that's different to just choosing to drive on the left or on the right. This is kind of like it's demonstrably worse. It's not actually clear to me that the way payment networks, the Visa and MasterCard payment networks work is demonstrably worse. I studied economics for the last two years of my undergraduate degree. And one of the areas that I enjoyed very much was financial economics. And what I experienced or learned around credit cards or plastic that you pull out, payment systems, is that there's some incredibly subtle and complex economics at work there.

Guy Spier: (00:54:20)

And just to share with you in the audience, cash requires you to have cash balances. If you have a credit card, that is either you have some bank saying that you're good for the money and that bank is going to make sure that it finds that money from you, whether it's already in your account, or you have to pay late, or it's going to charge you an interest rate. So, the consumer, when he pulls out or she pulls out a credit card, the amount of cash that they have available for the transaction is predicated on the relationship with the bank. Long story short, the propensity to be willing to pay for whatever it is with your card is very, very different to whether you have cash. And a simple example would be, I'm about to buy a new washing machine and the washing machine costs $800. And I don't walk around with $800. So, now am I going to go to the ATM and pull the $800, or am I going to pull out my credit card and know that the bill will arrive in three weeks' time? And if I don't even have the cash then, then I can just pay interest until I have the cash. So, I can focus on whether or not I want the dishwasher right now, rather than run around and think about it, go to the bank, all of those things.

Guy Spier: (00:55:39)

So, I think that many people don't, they see it just as an alternate to cash. They don't see that it's kind of a very, very different way of paying that's actually creating opportunities for the merchant, because it is increasing the propensity to pay. So, it makes it easier for the merchant to make the sale. It's also creating opportunities for the bank because it's creating the capacity to lend to that consumer and earn interest margin on the lending. So, that's a fun little introduction, but to turn that into a question, and this kind of goes to your legal skills or legal knowledge, if you want to own any one of these credit card networks, you are constantly going to be litigated against by a whole slew of people starting with the merchants, but also consumer groups, also public servants. And they will latch on to some aspect, so they'll latch on, for example, to the discount rate. And they'll say you guys are taking a 1% royalty on all consumer transactions. You guys are ripping off the whole economy. You bastards, we're going to nail you. There was something in Australia, I mean, it's exhausting following it. What's the answer? Is it just that when you own these companies, you're just going to be constantly doing this. And every now and then somebody comes along in a country and says, so we'll jump to, at some point to Chamath Palihapitiya who famously said that within a year or two, the credit card networks would be dead, which kudos to you-

Michael McCloskey: (00:57:20)

He's talking his book.

Guy Spier: (00:57:23)

<laugh> But this is not Chamath Palihapitiya, this is governments, this is powerful Congressman and Senators who hold these companies up in front of committees and Congress and accuse them of ripping the consumer off, for example. So how do you approach all of that?

Michael McCloskey: (00:57:43)

Well, litigation and regulation are two of the biggest risks with the company. And Visa's paid, and MasterCard and Amex have paid huge settlements in the past, but to go back to your example, Guy, you talked about buying a washing machine. So, you have got convenience when you go there, assuming that you're not a revolver, that you don't carry the revolving debt and get charged interest, and that you pay your bill every month, how much does it cost you to use your credit card as a consumer?

Guy Spier: (00:58:13)

You're asking me?

Michael McCloskey: (00:58:14)

Yeah.

Guy Spier: (00:58:15)

I pay on my AmEx platinum card; the fees have just gone up to $600 a year. So, you have got to be a member.

Michael McCloskey: (00:58:23)

But what are the rewards against that?

Guy Spier: (00:58:26)

Potentially zero if I pay my bills on time.

Michael McCloskey: (00:58:31)

So, I have a cash back card that I use in Canada with my bank, Scotiabank, and I get 1%, some of the premium cards in the US, the card by JP Morgan, you're paying less than zero as a consumer. You don't have to walk around with $800 cash to buy your washing machine and worry that somebody robs you or that you misplace it and lose it. And you get money back. So, there's a misperception from a lot of people within FinTwit, or even regulators, that Visa is taking a 1% margin out of the economy. The reality is, let's use round numbers, let's say there's a $100 transaction. And the take rate, the merchant discount rate, is about 1 to 3%, it depends on the channel, whether it's card not present or present. And two thirds of those economics go to the issuing bank, your bank, because the consumer's bank potentially extends the credit. About a third goes to the merchant's bank or the merchant acquirer. Visa just sits in the middle and takes 20 beeps I think it is, their average transaction is something like 8 cents. But they do that about 7,000 times a second, every day of every year. So, I mean, it's an amazing business. But Visa's job is really to play the referee. All they want is volume.

Michael McCloskey: (00:59:46)

And so, the merchants, the retailers don't like the system from the perspective that they're funding it. They like the fact that you, as a consumer can show up and not have to carry cash and you're going to spend more with a credit card. So, they want to accept credit cards, they just don't want to pay for it, or they don't want to pay as much for it. But to the consumer, in my opinion, the consumer doesn't see the cost or care about the cost because they don't bear it. And the issuing banks are making money, you know, that interchange is going to them. They're rebating a portion to you through your rewards, but they're still keeping some of the economics. And if you're like those 40% of credit card users that don't pay their balance every month, they're paying high interest rates to the bank, which is as a consumer a terrible idea. I read something in a book, that I should actually give a plug, Leif Erik recommended it to me, he's a new VALUEx-er and it's called *The Pay Off*.

Guy Spier: (01:00:44)

Oh yeah. It's on my *to read*.

Michael McCloskey: (01:00:46)

And it was written by the former CEO, and I think the investor relations or public relations person, at SWIFT. And so, it really talks about the payment industry and the history. I'll get the numbers wrong, but something like 40%, 30 to 40% of all bank revenue profits are in some way related to payments. And so, the regulators, you don't want to undermine your banks who are fighting money laundering, you have got to know your client. And in Europe, what I understand as the book explained it, in Europe because there's been so much more regulation and interchange has come down, the banks aren't as profitable. And so, they're weaker. They're structurally weaker because payments are so profitable in the West. So, you know, it's easy to haul the Visa and MasterCard CEOs in front of

Congress and chastise them because that's political theater, I get it. But the reality is the system works incredibly well for consumers, it works well for the issuing banks, and it works well for the retailers. They just don't like the price and they want interchange to come down.

Michael McCloskey: (01:01:53)

In Australia where the regulators have regulated down interchange quite a bit, what actually happened, my understanding is, well, the consumer was actually not any better off. They took away the rewards, and you started to have to pay to use a credit card. And it was really a wealth transfer from the merchants, because their costs came down, you know, from the banks that were previously, the bank issuer was making a lot of the profits, to the retailers. And the consumer was no better off. So, there's unintended consequences and it's easy to chastise them, but the system really works. And you know, that's not to say there won't be fee pressure and lawsuits and all that. But because for the vast majority of people it works, I think it's going to be intact. And you know, another thing we haven't talked about that I think is important is fraud. And there's a lot of fraud and people trying to get your, you know, if you're walking around with money in your pocket, people can take it away from you.

Michael McCloskey: (01:02:50)

I've been a bank customer with my bank for 25 years and I've had three issues in 25 years and two of them were this year. Before I came to ValueX, I always do a trip to somewhere new. And I went to Istanbul this year and I woke up one morning – and I get notified whenever there's a transaction that's suspicious or over a certain dollar amount – and there was one in Istanbul. And so, I contacted Visa immediately. They put a hold on my card, canceled my card and that they said, "Well, we'll do an investigation". And you know, when I get back home, every transaction that I had done on my trip was there except for that one. And it was just gone. They didn't even talk to me. It was gone. It was dealt with.

Michael McCloskey: (01:03:30)

And the second one was, I was in Nebraska Furniture Mart in Omaha. And I got a charge for Walmart, Canada. And you know, I'm a snowbird, my wife and I go to Florida for the winter, and we weren't in Canada. So, you know, that doesn't look right to us, and I inquire and sure enough, it's not us. And so, it's still being dealt with, but it'll get dealt with. So, as a consumer, you know, that's a benefit to me to know that Visa, if there's something that goes wrong, Visa's going to handle it, or my bank's going to handle it, versus dealing with cash. So, for all those reasons, I don't think the credit cards are going away. I've gone on too long. I'll let you ask a question.

Guy Spier: (01:04:08)

No, no, what's dangerous here is that I happen to agree with you on all of these things. I think that when I realized, so there's a guy called James Currier who's a venture capitalist, and he's got something called *The Network Effects Bible*, and he talks about different kinds of networks. And the value of a network that has so many interconnects, and when you think about how many merchants take Visa or MasterCard on the one side, and how many, so you get all these people who create competing payment systems like Venmo or PayPal. And then you discover that what they have to do is interconnect to Visa and MasterCard. And so, in the process they make Visa and MasterCard even more valuable because, and that was kind of like, every now and then I think that I really see it.

Guy Spier: (01:05:04)

So, just to go back to the litigation for a second. What I figured out was that yes, it is not as nefarious as the many legislatures say, but there will continuously be litigation. That is just one of the costs of running the business, but it's not actually a huge risk, because you constantly have situations like the

Australian situation where the way the industry adjusted was that the consumers were worse off. But you know, of course then the litigators and the legislatures have moved on to another topic, because they don't really care. They got an issue that got them popularity and then over the ensuing decade, they quietly reset the system basically. So, I don't think that litigation is issue. It was a huge insight for me to realize that all of these competing payment networks end up interconnecting to the existing Visa and MasterCard network, and a huge insight for me that a bit like the Dvorak versus QWERTY keyboard, if we were designing a payment system from scratch, then we might do it differently.

Guy Spier: (01:06:08)

I think that one weakness of FinTwit for me is that people come across as very erudite often, but then I realize that there are some basic things that they don't understand. So, for example, many people, they completely separate out the provision of credit with payments, and they imagine payments is just cash. And they don't realize that so much of what drives spending in the economy is the capacity for somebody to step in there and say, "The credit is good. There's going to be a mismatch between when the sale is made and when the cash is received, and I'll step in and make good on that. And you can trust me, and I have enough knowledge of both parties." That's an enormous value to the economy. So, let's – at risk of, well, you won't go down this rabbit hole, but other people might have – how much time have you spent thinking about whatever potential challenge crypto or blockchain has to the credit card networks?

Michael McCloskey: (01:07:20)

Well, I certainly gave it a lot of thought when the stock sold off and there was a lot of chatter. But I think about it every day, whenever I see something new. And, you know, Visa talks about, I know Visa better than MasterCard, they talk about being a network of networks. Whenever there's a potential threat, they just latch onto it, and they plug it into their network. And whether it's Bitcoin, enabling Bitcoin, if you're a buy now pay later, you know, two years ago or a year ago everyone was talking about them displacing Visa or MasterCard. They do something useful; they provide that credit that you're talking about at the point of sale, but again, they have to sign up every single merchant in the world. So, most of them have just partnered with Visa and MasterCard and, you know, use their ubiquity to distribute their product.

Michael McCloskey: (01:08:07)

And those businesses, you know, we don't have to go through the economics, I don't know if that business model works in a rising interest rate environment because there's a lot of losses. But Visa just talks about latching onto every potential threat, whether it's open banking, you know, they tried to buy Plaid and the government blocked that. So, they bought a second-tier competitor called Tink, or a smaller, I shouldn't call them second-tier, a smaller competitor called Tink that was less of a leader in the industry. So, they're just going to continue to play to their strength, which is we have this powerful network and most potential threats I can add to what you're doing, and you can add to what I'm doing. And that's how they transact in the market. And the regulators sometimes they'll block these acquisitions, but they're going to be very tough to displace in my opinion.

Buy Now Pay Later Plans

Guy Spier: (01:08:55)

If you go to companies like Buy Now Pay Later or AfterPay, or if you also go to a company that a member of ValueX has talked about, Cardlytics, these are companies that as best I understand are kind of closing the loop, in that you have on the one side the banks and the consumers, and you have on the other side the merchants, and behind them the producers, and Visa and MasterCard sit between those two. But then if you take Cardlytics, Cardlytics is taking information from merchants and finding a way through to the consumer. In the case of Cardlytics, they develop relationships between merchants on the one hand and banks on the other, and enable the merchants to advertise, or the manufacturers to advertise directly to the consumer in the same way that... What kind of got my mind with these AfterPay type companies is that they're able to offer, they're able to look into, or the manufacturer or the retailer can look into their gross margin and use some of that gross margin to fund the purchasing transaction. So, I think that every time this happens, I get fearful because they're kind of bypassing Visa and MasterCard. That's kind of, I guess what I've just done is give you my understanding of it. I'm curious, you can then either correct or update my understanding with your understanding, and then tell me how you've thought about these things.

Michael McCloskey: (01:10:36)

Yeah. So, Buy Now Pay Later, my understanding is that they take about, I'll use AfterPay, because I believe they're the biggest. So, we talked about the merchant discount rate being 1 to 3%, depending on the industry. My understanding is that the merchant discount rate or whatever they call it for Buy now pay later is actually higher. So, why would the merchant prefer that? Well, they get data which they don't get with Visa and MasterCard. But more importantly, I've read, or I've heard on a podcast that they spend, the amount of the spend that the consumer, he or she makes is up 20%. So, the economics make sense for them. But Buy Now Pay Later they then have to talk to every single merchant that wants to offer this, if they choose not to partner with Visa and MasterCard – and as I've said many of them have, Visa and MasterCard have come out with their offerings where buy now pay later companies can issue a Visa branded MasterCard, and still provide, they're in effect becoming a card issuer.

Michael McCloskey: (01:11:37)

And secondly, when you do Buy Now Pay Later, you know, it's something like you pay in four installments over a month and a half. So, think about that, Guy. If you buy your washing machine and you are a regular payer of your credit card, you're going to end up paying your balance within 30 days, give or take, whereas with Buy Now Pay Later, maybe you get an extra 15, 20, 30 days. What's the difference? If you're paying it off, I don't understand it from the consumer's perspective, why that's better for you. I don't see the advantage. And even if you do use the Buy Now Pay Later system, you have to make those payments, those installment payments, and most of those are made by debit.

Michael McCloskey: (01:12:18)

So, for Visa, I understand that the economics are actually better for them because they get four transactions instead of the one. And so, you still have to move the money, and the easiest way to do that is through the existing network. So, I don't view Buy Now Pay Later as a threat long term. Maybe I'm wrong. And it's tiny, like it's a 200 billion industry and Visa's, it's growing fast, but Visa’s gross volume through their network is something like $10 trillion. And again, these buy now pay later companies aren't making any money at present. So, maybe the VCs will get tired of funding them at one point, or the public will get tired of funding them, or maybe they'll find a business model. I don't know. But I don't worry about them too much.

Guy Spier: (01:13:02)

There's a, one of the early employees of Stripe is a guy called Patrick McKenzie and he lives in Japan and you're smiling, so you you've obviously read some of his things.

Michael McCloskey: (01:13:14)

His blog is fantastic.

Guy Spier: (01:13:15)

Yeah. It's kind of like, you know, Michael, there's you and me, and then there's people like Pat McKenzie and I just wish I had a few of Pat McKenzie's brain cells, I'd just do fine with that, you know. But he's actually done an incredible takedown of Tether, he kind of analyzed Tether. And I think that probably Pat Collison, who's the CEO of Stripe, asked him to look at whether Stripe should interconnect to Tether or not. And I think that based on his analysis in 2019 – I'm so impressed with the guys from Stripe, they're just like, you know, no interconnect to any crypto as I understand from Stripe. So, he did a takedown of Tether, which is just great. And if somebody emails me, I can send you the link. It's still up on his website. But he also did analysis of AfterPay and basically said, "Look, it's consumer financing", and did a careful analysis of what is going on with the pricing. And he said, this is actually credit card consumer debt. I mean, the consumer is effectively paying. I mean, it is not as bad as payday lending, but you're paying a high implicit interest rate when you look at the fees and all the other things that happen. But it's just sort of hidden and allows the consumer to think in terms of four interspace payments, but it's a financing thing.

Michael McCloskey: (01:14:34)

But if you pay on time, you don't pay an interest rate, to be fair to them.

Guy Spier: (01:14:39)

You don't pay an interest rate, but the manufacturer, the retailer is paying the interest and you're effectively paying it through the gross margin on the product.

Michael McCloskey: (01:14:53)

They mark it up?

Guy Spier: (01:14:55)

They didn't have to discount it as much as they would've had to discount.

Michael McCloskey: (01:14:58)

I see.

Guy Spier: (01:14:59)

You know, we would have to, I would want to have read, so as you can see, I do not have the details of his analysis in my mind. There's a, he looks at the relationship between AfterPay and the manufacturers producing the product. And what AfterPay does is that there's an implicit price. You know, the question to the manufacturer is, you know, this marginal consumer that wouldn't buy the product if they had to pay in full upfront, or just had their credit card, but who might pay using an AfterPay solution, how much of a discount are you willing to give us, AfterPay, in order to make that happen? And so, the manufacturer will create that discount, which is the implicit interest rate on the sale. And it's hidden from the consumer in certain way, it's hidden from us. But Patrick calculates that implicit interest rates and he says it's as high as any credit card lending. And it's kind of fascinating. And I think that you make a really, really good point and it's an interesting point. It's a point that we lose so often, which is that the scale in which this is happening is so infinitesimally small in comparison to the gross market volume that these companies are doing. So, you just stated a number $10 trillion, that is, I think that US GDP is 20 trillion dollars. So, kind of that that implies that sort of half of expenditure that is happening in the United States is happening through, were you quoting Visa in this case?

Michael McCloskey: (01:16:46)

Yeah, that was just Visa. I think they do about 10 trillion and I think global GDP, this is 2020 numbers, about 85 billion, sorry, 85 trillion. So, I don't know what MasterCard's volumes are, but a big portion of what do they call it, consumer spending is going through the card rails and they're just taking a clip and it's growing fast, and they've got tailwinds from consumers switching to online purchases and switching away from cash. So, it's an amazing business.

Guy Spier: (01:17:18)

Does the high valuation or the high apparent valuation, so any time you own one of these businesses, you kind of looking at a very steep and sort of like you look at the reported earnings and then you look at the market cap and you go gulp <laugh>, or I go gulp. How does it make you feel?

Michael McCloskey: (01:17:43)

Well, the first time I bought it, I think it was Visa, you know, paying 20 times earnings, I mean, almost made me throw up. <laugh>

Guy Spier: (01:17:51)

Twenty times, that's nothing, man.

Michael McCloskey: (01:17:53)

<laugh> Well, that was 10 years ago. So, there's a couple things. One, I think they're under earning today because cross border travel in particular, that's a very profitable segment for them. They make some FX on that. And that's depressed because of what's been happening with the pandemic. So, I think that's going to normalize. But these businesses are never cheap, but then if you're going to hold it for a very, very long period of time, which I intend to, if my thesis is right, go back to something that I don't know if it was Buffett or Munger said that ultimately the return you're going to get is more a function of the return on the invested capital, or the return on capital of the business, and the initial purchase multiple matters much less depending on the compounding.

Michael McCloskey: (01:18:39)

And these are compounders, and they don't require much capital to run. Unfortunately, they can't reinvest, they make some acquisitions. But it just spews for free cash flow, and they pay a small dividend, and they keep buying back their stock. So, yeah, the valuation's tough because it's never cheap. I think it's undervalued slightly, but it's not cheap. And so, I'm prepared to own it. Now, I wouldn't put 10% of my portfolio into it, because I think there are better things to do, but I think it's a pretty good place and an expensive environment. When I was looking at it that was pre the market pullback, there wasn't a lot, you know, or at least I couldn't find things that I thought were intelligent and I had already owned it for a long time. So, I really just added a little bit to my portfolios, but they're rarely cheap.

Guy Spier: (01:19:27)

I think that, so two things arise for me from that. One is that I'm still, it's a really hard lesson to learn that I mean there are studies that have been done of hundred baggers and long-term compounders, and the fact of the matter is long-term compounders are almost never cheap, never. So, if you want to own a hundred bagger, you know, and you're an investor who cares about the price, we care about the price we pay for something, because we know that that's important, then you have to find some way to be willing to pay up, basically. And that's an extremely hard lesson for me to learn. For what it's worth. You know, we're talking at a time when many tech investors have been hammered in the market. And I think that one thing that is different for me between this period and ‘99 is that in 1999 there was a concept of vaporware. There are companies that they'd raise money and all they would do is advertise that they had some great product and never even had a product. Whereas I think that so many companies today are really quite extraordinary. It's just that the people who are getting killed just paid too much. So, on the one hand you have got to pay up for compounders. On the other hand, if you pay too much, that's not going to work out for you. Figuring that one out is the name of the game, which is extraordinarily hard, isn't it?

Michael McCloskey: (01:20:57)

It's very hard. And one of the things I love about this business is sometimes you can study these companies and not necessarily transact on them today. You know, my two summer students or interns this year, I said, “If we go through the summer and we don't buy anything, that's okay. But if we go through the summer and can’t identify great businesses that we would like to buy and the price at which we would like to buy them, then that's a failure.” And so, our job is really to build that watch list. And then just, I call my assistant Michelle and say, “Michelle set a stock alert for this price”. And then one day you just wake up and something's happened. And whether it's the salad oil scandal that Warren had, it doesn't matter. Something could happen to these businesses. Something happened to the rating agencies in ’08, where they just came into your strike zone. And then you just update your thinking to say, what's happened to cause this sell off. So, you don't have to own them today.

Michael McCloskey: (01:21:48)

The hardest part about these great businesses, Guy, at least in my experience is just finding that entry point. And you have got to look around the environment and just be ready when the time comes. And you know, I'm paranoid that there's still so many great businesses out there that I haven't done the work on. And I want to be ready for when I get my chance, because then once you own them, you compound them. I mean, somebody complimented you online that they were impressed by the low turnover, the ultra-low turnover in your portfolio. And I think that's fantastic, because you own these great businesses that are compounding in value.

Guy Spier: (01:22:18)

It's just hilarious. An interview appeared in Marketwatch today, and the first point was, he says, “your portfolio's Betty turned over”, and my response to it is, “Yeah, it's pretty pathetic. Isn't it?” <laugh>

Michael McCloskey: (01:22:31)

It's lethargy bordering on slot, isn't that the line that Warren or Charlie uses?

A Detour About AmEx and Mastercard

Guy Spier: (01:22:38)

Well, one of the stocks in there is American Express. And I'm curious because, so I'm curious that the choice for you, you ended up writing up Visa. And I presume that's the one that you own. The choice between Visa and MasterCard at the time, but then also, would you ever consider, or did you consider American Express and or Discover Financial Services?

Michael McCloskey: (01:23:03)

Sure. So, full disclosure, I own AmEx. I don't own it as large. It's a more complicated business because of their closed loop model and we don't have to get into the mechanics. And the lending, it's a harder business to understand, at least for me.

Guy Spier: (01:23:16)

But Michael, the mechanics of the closed loop businesses are just so great. <laugh> Like, anyway, I was just reviewing one of their presentations that we could dive in, but sorry, I interrupted you. Back to you.

Michael McCloskey: (01:23:28)

No, it's an amazing business and it's a special brand as Warren says. So, I do own it. I don't own it in as large a position just because I struggle sometimes to understand the business. I mean, it's complicated as a regulated bank and with a balance sheet that they have. I've never owned MasterCard. At the time I bought Visa, Visa was cheaper and MasterCard, as I understand, grows a little bit faster because of where it is in the world. And so, you and I should probably talk about that offline, because I'd love to learn more about MasterCard. I don't know that business as well. Discover I've never owned, and I've never done a lot of work on it. To me, I just don't – again, I'm ignorant, I may get this totally wrong, Guy – I think that they're a more US centric, and to me the brand is not nearly as good as a Visa or a MasterCard or an AmEx. And so, I'm a bit of a chicken when it comes to investing. I usually prefer to own best in class. And even when I look at the margins between Visa and MasterCard, Visa has better margins. And I don't know if that's because they're bigger or something else or maybe I'm missing something. But no, I've never looked at Discover.

Guy Spier: (01:24:38)

So, I looked at Discover first when it was spun out of Morgan Stanley. And of course, even then actually interesting enough, I was like I said to myself, this is a network. This is fascinating. And kind of the dream or the possibility for Discover was always that it would hook up with say China Union Pay and form a global network. Because you're right, it is in the United States only. And they work really, really hard to keep that network going. So, they have to offer more all around in order to make it interesting for the consumer to use it. And you have this, you know, on the one hand we are Avis, we try harder, but there are these industries where the number one and number two do really well, maybe number three, but at some point, it drops off. Having said that, Discover has shown extraordinary returns. I think that I was also motivated not to own it, for your interest, from just experience from learning from American Express.

Guy Spier: (01:25:49)

And I think that something we haven't touched on, but for me is really important is that the company has, I experienced, and I'll ask you this, I'll say it and then I'll see how you think, what companies I own influence you. You make your bed and then you sleep in it, it's the environment in which you live. And so, I've learned all sorts of things from owning American Express. Many of those things that I've learned, I've actually applied in my own business. American Express used to own Western Union. Western Union, a nice way to put it is it's in the remittance business, and not nice way to put it is they rip off people who don't deserve to get ripped off. And it's not as bad as payday lending. And the answer from Western Union is, "Yes, but they need the service and that's just what they're willing to pay." But American Express kind of said, we don't want that customer base. We're always happy to give that customer base to somebody else. We want a very small number of business owners, high net worth individuals. We want it always to be exclusive. Western Union won't be able to do that, neither by the way will Discover.

Guy Spier: (01:26:56)

And so, kind of like, even though it's had extraordinary returns, do you want to own something that, I mean, Western Union, I don't want to own Western Union in part because I think they rip people off. And Discover doesn't rip people off, but it's just more of a lending business than it is in network or another kind of business. For what it's worth, forgive me, I want to dive into this, and I don't know if this is appropriate podcasting, whatever, but I just want to tell you, this is the kind of conversation that I have with Michael, for those who are interested, at the bar, for example. So, I like to feel like I'm at the bar in Klosters now. You're right, American Express in many ways is more complicated and has more moving parts than the Visas and MasterCard, but there is some incredible economics going on at American Express that is just so awesome.

Michael McCloskey: (01:27:47)

You can see it in the numbers. It's obvious that it's a good business. But when I look at the balance sheet, it just, maybe it's just my mind. I prefer things that are really simple. And so, I own it and it got cheap enough, but I struggle with the analysis, more than I do with Visa.

Guy Spier: (01:28:03)

It is effectively a bank, more of a bank, and it has a lending business to it, also has a deposit business to it. But you know, to look at the economics of some of their quote marketing deals, where for example, they issue a credit card with Delta Airlines and the economics of what's going on with the Delta Airlines margin and Air Miles are there are aspects to it, which is a marketing deal. There are aspects to it, which are a consumer, they do things for the consumer through it. They generate revenues for the network through it. There's complex things going on where there's multiple aspects to why it makes sense. And in a certain way, AmEx is kind of a marketing partner for many businesses in an extraordinary way but at the same time, having all of the economics of what we discussed with the basic credit cards and payments. And so, it's funny, because I don't think I'll ever understand it. And every now and then I get, I tell myself, wow, this is actually not as good as you thought it was. And then more often I go, my gosh, this is just extraordinary, just extraordinary.

Michael McCloskey: (01:29:15)

<laugh> And it takes more capital than the Visa and MasterCard business because of its structure and its funding. And it, yes, that's right. But that doesn't mean it's a bad business. It's just, it's different.

Guy Spier: (01:29:24)

And I'll just share this thought with you, that my thinking has evolved on. So, you and I understand why it's nice to be in high return on equity businesses, but I've actually started thinking that I want to, you know, even better than that is a business that could be higher return on equity, but they choose not to be. So, when you have a high return, high margins and or high return equity that presents target for other people to go after. And if you can somehow convert your business in something that's kind of like scale economies shared, ala Nick Sleep, and you reduce your pricing umbrella, you create less of a target for your competitors and you create a wider moat, because you're giving stuff away to consumers or to suppliers or to somebody. And so, in a strange way, I'm actually now looking for businesses that if they decided to jack up their prices, and if they decided to be more aggressive with their suppliers let's say, they could make a lot more money, but they choose not to. And so, they're kind of like masquerading as low return businesses while building out their moats enormously, which is kind of like what Costco is doing.

Michael McCloskey: (01:30:36)

That's exactly what I was thinking. Yeah.

Guy Spier: (01:30:38)

And a question for me is who else is doing that? And actually, in a strange way, I think that Visa and MasterCard are doing that because I mean, just to go back to that point and I'll make it, and then you make sure that I've made it properly. You know, you asked me the pointed question, does the consumer pay anything to have a credit card? And the answer is if you handle yourself right, and don't get into credit card debt and you pay your bills on time, it doesn't cost you anything. So, actually you could, and you realize that of the total merchant discount a tiny sliver of it is being taken, 20 basis points by Visa and MasterCard. The balance of that merchant discount is being transferred over to the banks for the risk that they're taking on nonpayment and fraud and all sorts of things. And so, you could argue that Visa and MasterCard are front for the banks, with the merchants. <laugh>

Michael McCloskey: (01:31:37)

Yeah. Maybe. I mean, when you look at where Visa and MasterCard really compete it's to get people issuing their cards with their credentials. So, they compete for the banks. And I think they won't say this, but if they had, you know, they want to make sure that the issuing banks are happy more than they want to make sure that the merchants are happy. They want to make sure that, you know, they got into a dispute, Visa got into a dispute with Amazon in the UK, I believe, where Amazon threatened to not allow Visa credit cards. And I mean, that was the third leg of they'd been fighting in Australia, and I think Singapore. So, from time to time merchants revolt, and if they're big enough, they try and use their power like Amazon can. But are they a front for the banks? I don't know. They're tied at the hip <laugh>, I don't have an answer for it.

Guy Spier: (01:32:29)

Something that I don't understand, I mean, the larger merchants do get a better deal from Visa and MasterCard. Why do they have to go the litigation route? Because Visa and MasterCard will deal with the big merchant in a different way.

Michael McCloskey: (01:32:48)

It's hard because when you’re Visa and MasterCard, it's an odd system where they set the interchange rate depending on the channel or the type of payment. And so, they want to, any change that they make to those rates, and you can look at the rate card they're available online, anytime they make that change, it affects every single bank that issues a card. And so, you know, it's not really changing their economics. It's changing the economics of another stakeholder within the ecosystem. And so, their job is really to balance, how do I make sure my banks are happy and the consumers are happy without making merchants too angry, because they're the ones funding it.

Michael McCloskey: (01:33:29)

And so, you know, ultimately Amazon being Amazon and given its scale, they came to a resolution quietly, as I thought they would in the UK. And I don't know the economics, I'm sure they got some kind of a price break, because of their algorithms and lower fraud and all that. But subsequent to that, Visa increased the rates on many other large merchants in different categories. So, I think they have to be really careful that they want to keep their bank issuers happy. You know, Visa and MasterCard aren't going to compete on price, where they compete is when Costco puts out its request for proposal for a new card, and you want that business, you want to capture Costco and all their members as card holders. You provide incentives at the time of renewal and that's where they compete, and they'll compete around the edge. But they're not going to undercut each other. It's a rational oligopoly.

Guy Spier: (01:34:25)

I think that, you know, it's fascinating for me that people who are really very knowledgeable and sophisticated financially, often I think get some basic aspects of the payments industry wrong. And I'm not saying that I understand more than them, but I'm very confident that they get some things wrong, and I can see that that's wrong, even if I don't understand everything myself. And it's funny because it attracts people or attracts opinions where people are very self-confidently wrong. Kind of the way Chamath was. I mean, he's, you know, he genuinely believed what he was saying. And he was certainly not getting many aspects of the industry, I mean, before we turn to a couple of questions about mathematics, which is what we're going to close this out on.

Michael McCloskey: (01:35:11)

<laugh> Gosh.

Guy Spier: (01:35:12)

The statistic that I saw, so I don't remember if it's Visa or MasterCard, 10,000 banks are connected into those payment networks, more than 10,000 banks. You can imagine a bank has a minimum of a million customers and has all sorts of things going on. And 10,000 banks, it's just, it's an enormous number. The size of the network probably rivals the telephone network or the mobile phone network. If you think of, and it's worth saying that to the extent that Visa MasterCards signing up, they'll sign up a company that themselves sign up merchants. So, they don't actually know how many merchants they're signing up. They're just signing up an aggregator of merchants. They don't actually know how many interconnects there are. It's kind of insane.

Michael McCloskey: (01:36:05)

Think about how many banks are connected to that and how many merchants are already in their ecosystem. To recreate that as a new FinTech or buy now pay later provider, to have to go around to each of those merchants in the case of Buy Now Pay Later or to get to the consumer, without having to go through those banks is very hard to replicate. And I don't know who came up with this, but there's something about the power of a network increases to the square of the number of nodes. And so, they've got this incredibly powerful machine and they're just wonderful businesses.

Guy Spier: (01:36:43)

You'll really enjoy James Currier's work, *The Network Effects Bible*, and I'll make a note to send it to you.

Michael McCloskey: (01:36:51)

Please.

What is Inspiring About Mathematics?

Guy Spier: (01:36:52)

I'm so grateful to you for spending time with me in this way, and with whoever decides to eavesdrop in on this conversation. So, for everybody, I did not let Michael know that I was going to ask him this question. If there are aspects of mathematics, if so, what do you miss most about the time that you were studying mathematics? What topics in mathematics were most inspiring to you?

Michael McCloskey: (01:37:23)

That's interesting. I think it was the certainty. I mean, calculus was my thing, and I was good at it, but I didn't want to be a professor, and I liked the market, and I liked money. But there was, you just knew there was an answer. And calculus in particular, for me at least, it was about pattern recognition. And the more you did it, and the more ways you find to solve a differential equation or an integral, I could just see it. I don't know how to describe it, Guy, I could just see it. And there was a certainty to knowing that you got the right answer. And one of the challenges as an investor, as you would know, is you're making decisions based on imperfect information. And sometimes it's impossible to know, we're playing in probabilities. And that's very uncomfortable to someone that comes with a mathematical background that loves the beauty of mathematics and the certainty. And the world is messy, and business and capitalism and the world are messy places. And so, it's very different. And so, it's comforting to, you know, go back to when I was studying calculus and it was fun. Like, I liked it because I was good at it. And now I forgot most of it because it hasn't been useful to me. But to me it was, it was just that certainty. It just made me feel good. I don't know how to describe it.

Guy Spier: (01:38:41)

You know, so I was, I realize now in retrospect that I was actually, I was very good at mathematics, I can perhaps even say. But because it came so easily to me, I didn't respect the subject as much. And my perspective, I didn't realize that my perspective was very different to that of others. And I said, well, obviously I'm not going to study that because that's not hard. Or that's kind of like that's not, that's also something for hard work. Hard work is history, hard work is law, cracking open a book of legal texts, because mathematics, that's just playing around, having fun. And I have a real regret over it because if I'd understood, if somebody had said to me, "Hey Guy, this appears easy and fun to you because you happen to have capacity for it. Stick with it, have fun with that." You know, study does not have to be drudgery.

Guy Spier: (01:39:37)

And so, I have this kind of question mark in my mind, through no effort of my own, a very good friend of mine in Zurich happens to be a professor of mathematics, and we just found our way to each other. But I have this question in my mind as to if I would've properly followed mathematics, where I would've ended up. And you know, maybe I'm not all that good at mathematics. Maybe I would've dropped out in first year, undergraduate mathematics or maybe not, who knows, maybe would've gone way further than that. And I would just tell you, and for the audience as well, that I don't know. So, I think Coursera's amazing and there are amazing resources on-

Michael McCloskey: (01:40:17)

Khan Academy too.

Guy Spier: (01:40:18)

Yeah. So, on YouTube I love 3Blue1Brown. It's a lovely guy who explains all sorts of mathematical concepts with these very beautiful videos. And I don't know why it was I had not studied, as a high school student, matrices, vectors, matrix mathematics, eigenvalues. Using matrices to kind of like work in multiple dimensions – and for the listener, that does not necessarily have to be physical dimensions, it could just be with multiple attributes – it's extremely important for machine learning for example. But I found the concepts that I was coming across so powerful. And I actually think that my mind would work differently. And I'd think about the world differently if I'd studied matrices at an earlier age. What it makes me want to do, so you said calculus, I kind of, you know, I was talking to Chantal, my head of what did we call her, my chief of staff, that I just want to go and do an undergraduate degree in mathematics just for fun. Not just for fun, because I think that I'd learn all sorts of things.

So, I didn't realize, and I think it's actually really interesting. So, this is the algorithm working for me, I believe. So, I've been connected to Michael who, turns out I studied law like you did.

Michael McCloskey: (01:41:40)

I didn't know that.

Guy Spier: (01:41:41)

I did an MBA like you did. So, what happened to me is I went into university to study law because I was a science background, maths, physics, chemistry. Actually, I didn't do chemistry, I dropped chemistry for German because I didn't want to be a boring science guy, but I was encouraged to do sciences. And then I sort of said to myself, well I have to go and be, go into business. And how do you go from sciences to business? So, I thought law. So, I applied for law, having never cracked open a legal textbook in my life. And you know, when I was confronted at age 18 with contract law, I actually really enjoyed Roman law. We had some Roman law that we had to do. And that was just really beautiful because there was an aspect to it which was historical. But when I had to go into like contracts and I'm at age 18 and we're reading contracts, this was not <laugh> a happy time for me. So, I switched to economics. But actually, I'm really glad. I mean I learned an enormous amount through my legal studies, no question.

Michael McCloskey: (01:42:43)

You're a polymath, Guy. You could be good at a lot of things. You're really good. No doubt in my mind.

Guy Spier: (01:42:48)

I think now I would've been willing to engage very profoundly with the subject. So, many people like philosophizing about the world. Law is where if you like philosophizing about the world, it comes into contact with harsh reality, and you have to apply those philosophies in practical situations where often there's a winner and a loser. And so, it's kind of like, for people who've thought a lot about philosophy, who philosophized a lot, law gives them a practical way to grasp and to put those things into action. But I hadn't spent enough time thinking about the planet to get to that stage, but no problem. Michael, so your favorite topic is, do you read any mathematics today?

Michael McCloskey: (01:43:39)

No, not really. There's a blog I read on occasion. Like I sent it to Ram because he likes maths too.

Guy Spier: (01:43:45)

So, Ram's another ValuExer.

Michael McCloskey: (01:43:47)

Yeah, no, I've lost most of it to be honest. And I'm not as quick with the numbers in my head. I'm certainly no Buffett where I can do these investing calculations in my head. But I'm numerate and, you know, I can do the basic maths. But no, I've always found it interesting. One of the challenges that I have, and I think you have, is just we find so many different things fascinating. And maybe chemistry didn't appeal to me either. So, we just go to things that we find interesting, but the world is incredibly fascinating. And that's what I love about what we do is you get to discover new businesses. And I still love reading about physics and science. And I read broadly, and so do you, and it's just, it's amazing. We get paid to learn.

Guy Spier: (01:44:27)

<laugh> It is, it's pretty cool. So, if somebody's heard this rambling interview, conversation-

Michael McCloskey: (01:44:35)

<laugh> My apologies.

Guy Spier: (01:44:36)

No, no, I was the one who rambled, not you – and they want to get in touch with you or engage with you, what is the best way to engage with you?

The Art of Writing Books

Michael McCloskey: (01:44:45)

Well, you can reach out to me on Twitter. You can reach out to, I'll give you my email, michael@greenskeeper.ca or our website is, we're in Canada, so .ca, greenskeeper.ca. And we're not hard to find, so feel free to reach out and say hi. And Guy, you've asked me a whole bunch of questions without giving me a heads up. Can I ask you one? And you can edit this out.

Guy Spier: (01:45:09)

<laugh> You can ask it.

Michael McCloskey: (01:45:13)

So, I pulled this out last night.

Guy Spier: (01:45:17)

Right, you were preparing.

Michael McCloskey: (01:45:19)

Well, I was. And I've read it and I'm going to reread it again. And, I just think about, I mean, you signed this for me when I first met you. I didn't realize when I first came to ValueX and it was February of 2015 when you signed it for me. And the book was only published in 2014 and there's so much timeless wisdom. So, if you haven't read Guy's book, and he'll be mortified for me giving him a plug, but you should pick it up, because if you're into this, it could change your life. Think about how much you've learned since you wrote that book. And I can't imagine how difficult it was to write that and to put yourself out there and how much time it took. Would you ever think of writing a sequel someday?

Guy Spier: (01:46:03)

<laugh> Thank you so much for asking the question, Michael. I didn't say I'd answer it, but before I attempt to answer it, I will answer it, but I just want the listener to pay attention to what Michael did. So, he doesn't even realize, you don't even realize you did it and you did it very naturally. And there's huge learning in that. So, what you did is something that one finds a lot in the Berkshire crowd, is that rather than taking, you want to give. And so rather than turn, I mean, I've ad-libbed quite a bit through this conversation. I haven't just asked questions, but you actually threw the spotlight back on me. So, I'm trying to throw the spotlight onto you by saying how can people get in touch with you. And you're like, you sort of mumbled your email and you said, “I'm available on Twitter.”

Michael McCloskey: (01:46:55)

It makes me uncomfortable. <laugh>

Guy Spier: (01:46:58)

Well, so it it's this fascinating thing because it's a beautiful quality and it's, you know, as a friend of yours, you know, you certainly should put your email into more documents, let people get in touch with you. It's not crafts marketing. It's just allowing people who want to engage with you to engage with you. But there's this idea of, and I expressed this idea at ValueX, so everybody we talk to is on our team and if we can make them successful, we'll end up being successful. And what you want to be is you want to get into a team where everybody's helping each other. It's often far easier to help somebody else get successful than it is to help yourself. So, you want to get into situations where you're helping the people who'll become your friends, if they're not already your friends. And then they will also help you, which is kind of what you did by turning the spotlight on me. So, I just wanted to thank you for it, for doing it. I also wanted everybody who's paying attention to this, who's eavesdropping in, to see how naturally Michael did that. And I just find constantly, I miss opportunities to do that in my life. And every time I do it, it never diminishes me. It usually doesn't cost me anything and creates an enormous amount of fun.

Guy Spier: (01:48:17)

Very brief story on that front. I'm at an event that is on the outskirts of the World Economic Forum. And there's a guy at my table where we're asked to discuss something at the table and then one of the people at the table has to report to the room. And there was some very powerful people in the room, people you would want to have hear your voice. And there were two or three or four middle aged people, and then there was a young man who can't have been more than 21, 22. And I thought, wouldn't it be fun – because we'd be jostling between ourselves as the older men who was going to report to the room – why not give the opportunity to the young man? And he was up for it. And so, I pushed for that, and he did it. Four or five years later, I met the guy in an event, and he reminded me of that. And he told me that it was a huge impact on him. His voice was heard in this room, there were conversations that happened subsequently. And so, when you turn the spotlight on somebody else in an environment where people want the spotlight on themselves, you know, the benefits can come, you know, years down the road. So, it's just interesting. Thank you for doing it.

Guy Spier: (01:49:28)

Answer to the actual question that you asked is that, so I did put myself out there. I didn't realize that actually in a certain way, by doing that, I was saying goodbye to anonymity. And you know, it's a bit like your one virginity, you know, songs of innocence and songs of experience. So, when you're innocent, you want the experience. And when you have the experience, you mourn your loss of innocence. And so, I gave away the innocence of being anonymous and I benefited enormously as a result. But people know the person who wrote the book, they don't know the person I am today, which is like almost 10 years down from writing the book. So, there is a basis for writing kind of like a follow up. There are two possible reasons why I would not do it. One is that by far and away it is the most painfully difficult thing that I've done. And painfully difficult, not because the writing was hard, although that was also hard, but because I realized that in order to deliver value to the reader, I needed to dig deep into myself. And I dug deep into myself. Digging deep into yourself is really painful. And I asked myself, do I really want to do that again?

Guy Spier: (01:50:46)

And I think that another question that I have is that I really do believe this and, you know, call out to, he was not my editor for the book, but Myles Thompson is the producing, managing editor of

Columbia University Press, who has deep knowledge of writers and the craft of writing and the business of writing. And he was the guy who was the editor for Victor Niederhoffer's book, *The Education of a Speculator*, which provided the inspiration for my book. And he said, “Look, there are one book people, and there are...”, so he said, I said to him, I don't think I'll write another book. And he said, “Yeah, you're probably very right to do that, because you're a one book guy.” And so, you know, the perspective is, every individual on the planet, including you, Michael, has one book in them. And that book is kind of like the memoir of the life story, telling it your way, telling it how you experience the world. And if you have this perspective that every human being is unique, then they have a unique story to tell, a story that's worthy of telling, a story that is worthy of reporting, even if it's just for their wife and children, if not for a broader audience.

Guy Spier: (01:51:54)

And I'm beyond convinced that I am a one book person. So, I think that what I might do is write a kind of second edition, where sort of like many of the original chapters are there and then there's three or four sort of subsequent chapter chapters added in. What is actually painful for me about your question is that something that I would really fancy myself as being, but I don't think it's the case is, you know, I mean, I really admire people who've written multiple great books. So, you know, I really admire William Green. You know, William Green hasn't got a spot on us when it comes to mathematics, he can't do jack squat there. But writing, my experiences with William, he's not a genius. Obviously, I'm plugging his book, *Richer, Wiser, Happier*. So, when you're somebody like William Green, I mean, at the Berkshire meeting, I was very lucky to witness a meeting between William Green and Lilu, and they had this wonderful conversation that I was a part of. But there are conversations that happen between authors and their subjects or writers and subjects, that are just kind of like, you know, the unexamined life is not worth living. The perspective of a true writer is just an extraordinary perspective. So not entirely sure that I would've liked to have been George Orwell, but there's an aspect of his life that is just incredible.

Guy Spier: (01:53:31)

And so, there's a guy called Paul Graham who writes essays that you can read online. He's a venture capitalist. And he writes these incredibly concise, sort of like, there's not an extra word in place and they're amazing essays. And they really, every one of them teaches. And I kind of, it really pains me that I think I'm not saying it's impossible, but the more I live, the more I realize that it's unlikely that I will leave behind a body of essays the way Paul Graham has left behind. But that's just not my skill, you know, and you have to accept different people have different skills. At the end of the day, Warren's work of art is Berkshire Hathaway and the Buffett letters, but he hasn't written any novels. He hasn't written any textbooks. He hasn't written any well, he has effectively written essays. The long story is I'm pretty sure that I am, I did call myself author, when I do a bio, I call myself author, but it's the author of one book. And I think it would be presumptuous of me to call myself quote a writer, much as I would love to really be a writer. So, very long answer to a really lovely question that I appreciate you asking, have I answered it well enough for you?

Michael McCloskey: (01:54:45)

You've answered very well, and I'd say you don't give yourself enough credit because you are a writer, you're a teacher. It's an amazing book and it's intensely personal, and I understand why it would be such a burden to write and, you know, how difficult it would be to do another one. And you talk about the anonymity or, you know, I saw it. I saw it in your reception in Omaha that, you know, people fly deep trying to get at you and you're always on. And as an introvert, I mean, I was like, “oh my God, why would I want to put myself in that position?” So, if I ever decide to write a book, I'll make sure it's near my deathbed. So, I'll just leave it for posterity. But you're writing in a different way, when you think of what you're doing with ValueX in the community that you're fostering. And you said something to me once, that wouldn't it be amazing to look back in 10 or 20 or 30 years at this group, and then just see how everyone's done. And so, to me that's your painting. To go back to what Warren has done, you know, in addition to your book, that's kind of, you know, maybe ValueX wouldn't have happened if it weren't for the book, but this community that you're continually building and people that you're helping, I mean, maybe that's your painting, Guy.

Guy Spier: (01:56:05)

Maybe.

Michael McCloskey: (01:56:06)

And so, you've done incredible things and I'm eternally grateful for having fallen into your orbit, because you've taught me a lot.

Guy Spier: (01:56:14)

Well, that's very kind. You realize Michael, it's just long term greedy. <laugh>

Michael McCloskey: (01:56:20)

<laugh> I don't think you have an agenda. You're not Machiavellian.

Guy Spier: (01:56:23)

<laugh> You know, I think I said it, I don't know if you're in the talk, brief talk. So, you know, I am, it's not a necessary outcome for my life, but I ask myself, you know, would it be nice to be, you know, oligarch, Warren Buffett, Bill Gates style wealthy? Of course, it would be fabulous if any one of us, if let's say speaking for myself, if I were to get there. But how miserable and lonely to get there on your own. I don't know much about Sumner Redstone, but if I understand correctly, he didn't have many friends. And we know the story that Warren's told that, you know, all these people went to the guy's funeral because they wanted to make sure he was really dead. But, you know, consider another way round is that, and I really do, you know, I don't ever want to own a mega yacht, but how cool would it be if I had a number of friends who owned a mega yacht and not friends, not fast friends that I made because I met them at some fancy event and I was trying to get invited on their boat. But what if we got 20 years' time and 10 longstanding members of ValueX are so fabulously wealthy that they have incredible lives. And because their friends at ValueX go back all these years, and we've had all these amazing conversations at bars, ski slopes, and what have you, those are their real friends.

Guy Spier: (01:57:55)

And so, how do you get to there? And in a certain way, that's I guess part of my life, it's not my mission, but it's a goal for me to do my very best, when I look back on my life 20, 30 years from now to know that I had a really good shot at that. And so, you know, it is a kind of a long term greedy. But it's, so what I found with when I analyze decisions or actions that Warren Buffett has taken, that there's a kind of a stacking of logic. It makes sense on multiple different levels and in multiple different perspectives. And I sometimes wonder if maybe that's one of his decision heuristics, that he does something not when there's one reason for it to make sense, but when there's three or four reasons for it to make sense. So, it's a nice time at ValueX. I'll get to learn about investing. I get to hang out with a great group of people, and I also get to build these possible future outcomes. Those are kind of multiple ways in which that stacks up. But thanks for saying it. So, I'll turn the last question on you <laugh>, so do you think that you will ever write a book?

Michael McCloskey: (01:59:09)

I don't know. First, I have to convince myself that I have something intelligent to say and worth sharing. You know, I'm a bit impish and I have so many stories from our investment banking days, and I tell them to my daughter when she's an adult, and some of the students. I don't know. I don't have any dying need to do it, but maybe someday, I'm not sure yet. I'm not sure where my journey will take me and whether or not there'll be a time in my life to do it. I'm not going to do it now, because I'm busy with my business and I've had many other sidetracks and projects in my life, but for now I'm focused on building the company. But I don't know. I'd say I never say never, because I like to write. So, I don't know.

Guy Spier: (01:59:53)

So, I'll share this with you, and this is going to be my closing thought, and then you can have a closing thought and then we'll shut this down, because we could be here a long time. So, I don’t know where, so it's in around David Perell, there's another guy, Tiago Forte, who's got a whole bunch of intellectual content around what he calls building a second brain. And the idea that, so whole bunch of thinking in that, which I don't, I feel like I need to be respectful of various people's times, so I don't want to go into it. But one of the key things that I've learned is that as I go around, collecting notes, learning about different things, I need to be a bit like a squirrel who puts away, hides away nuts in that I have to take care of my future self and my future self wants to come across certain things. So, something that I will do is I'll rip out one page or I'll rip out the balance sheet, income statement, cash flow statement of an annual report that I'm reading and put it in a pile to be read in six months. I know I'm going to come back to it in six months’ time.

Guy Spier: (02:01:05)

And so, I was talking to somebody who's having a particularly difficult time recently. And one of the things I told them to do is just write something about your experience for your future self, because your future self will want to know how you felt and will want to see a record of how you were during this period. And if you don't write it, you'll never be able to recreate it. So, my kind of exhortation to you is, in creating the richest possible future, what you might want to do is without the intent of setting the goal of writing a book, but to create optionality for your future self, you know, write an occasional diary of thoughts as they come out, which aren't well enough focused to turn into some, into a Visa research report or an investor letter, because your future self may well be able to raid that material for the book that you might write. So, there's my exhortation to you and closing thought.

Michael McCloskey: (02:02:05)

Thank you for the suggestion.

Guy Spier: (02:02:06)

Yeah. So, I'm now going to say thank you so much for following my mind in the various places that it goes. It has been a real delight to talk to you. I really enjoy the fact that I've managed to corner this introvert, who doesn't like talking very much and here we are, we got him live. So, thank you for doing it. <laugh> You know, it doesn't come easily to you, so I really appreciate it.

Michael McCloskey: (02:02:31)

No, it doesn't. Well, and I appreciate everything that you've done for me. I think I said when we were in Dubai that, you know, my life is better for having met you and the group of people around you, and what you've created and dragging me out of my cave. So, Guy, you're just a terrific person, and thank you for everything. And if I can ever help you, you know, I'm sure people clamoring to help you because you're so generous.

Guy Spier: (02:02:58)

Well, that's very kind. Well, you helped me just by being yourself. Because it goes both ways, and very genuinely, there are all sorts of aspects of my mind and my existence in the world that's reinforced by being around you. And so, you know, just by being yourself and I think that I've, I want to just leave the last word to your wonderful daughter. So, she made a huge impression on me. Self-confident, intelligent, interested, not fazed by all those people in the room, proud of her father, but also an independent personality. There was a lot of very, very positive stuff going on there. So, I just wanted to, it was something that I learned at the meeting. And it brings me to the very end of War and Peace with Leo Tolstoy, where he is gone through this huge ranging history of the Napoleonic wars and these different families and changes and then the sweep of history. But at the end of the day, what he writes about is the happiness of the home and family life with the wife that loves you. And so, in a certain way, none of that counts if you don't have the strong family relations that you clearly do.

Michael McCloskey: (02:04:06)

Life is good.

Guy Spier: (02:04:08)

<laugh> Thank you, Michael.

Michael McCloskey: (02:04:09)

Thank you, Guy.