'I Always Believed I Could Make Money With Money' -- Forbes 400 Member Leon Levy

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When I was a young man growing up in New York City, I could never imagine that anyone would pay me to do anything. I did not do particularly well in school, I am easily distracted, and I have always been forgetful - not the list of personality traits likely to appear in a help-wanted ad for any profession. Still, from the age of thirteen, when I invested in the stock market $200 that I had received as bar mitzvah presents, I always believed I could make money with money. This turned out to be true. --Leon Levy, "The Mind Of Wall Street"

I had the honor of interviewing Leon Levy in early December, 2002. Mr. Levy has had an illustrious career on Wall Street as founder of the very successful Oppenheimer Funds and partner of Odyssey Partners, a hedge fund that over it's 15 year history, put together one of the best and most consistent records in history. This success has made Mr. Levy a member of the *Forbes 400* for many consecutive years.

First, I will tell you that if you are reading this interview in order to learn the trading secrets from one of the masters, you will not find it here. Mr. Levy is old school. And, old school doesn't show their hand. This means they play a game of possum. They tell you nothing they don't want you to know (in fact, I edited the times he imparted to me such wisdom as "if you like a stock, you buy it, and if it goes down, you sell it.") But, Mr. Levy was kind enough to share some gems. Read into his words and you find some secrets. And the biggest secret he was willing to share was how he obtained his returns. They came from hitting home runs. Outsized gains from a few positions. Risk 25-100% on a position in order to make 10, 20 and 30 times that number. These are not trades. They are longer term holds that appreciate over the years. When you look at many of the most successful "larger" hedge funds, that is the way they play. They take a small piece of the portfolio, make many investments that they feel can explode in price and then reap the rewards when they do. It's a fairly risky way to go about investing/trading. Mr. Levy was humble enough to point out he's had many, many losers along the way. In his book "The Mind Of Wall Street," you'd think he had nothing but losing investments in his career as he spoke about them in great depth. But, even though the losing investments tend to be more colorful, I believe Mr. Levy was making a point. His point was that even the very best professionals make mistakes, sometimes big mistakes. But these mistakes can be overcome, by finding winning investments that overcome those mistakes. And how do you do that? Simple. It's risk/reward. It's getting into positions that can and will potentially lead to gains that far outweigh your initial risk. When you correctly do that you end up with returns like Leon Levy has achieved over his 50 year history on Wall Street.

As you know, there are many ways to make money on Wall Street. Leon Levy's way is certainly one of them. I hope you enjoy and learn and profit from this interview:

Larry Connors: I just finished reading your book. It's extremely well written. I congratulate you. I also congratulate you on the success you've achieved over your career.

Leon Levy: Well thank you very much, Larry. If you want the real story, it was mostly luck.

Connors: How's that?

Levy: Oh, there's luck in life, in business and everything else.

Connors: Your humbleness comes through in the book. Obviously, it's not that easy to achieve what you've done. Again, I commend you for this. Let's talk about your background before we get into your investment philosophy.

Levy: OK.

Connors: Maybe we can start right from the beginning. One of the things I noticed is that your father played a major role in your life and in your thinking. I know your book is dedicated to him and it seems that a great deal of his work found its way into your own thinking. Can you talk about that?

Levy: I certainly can. My father was interested in economics because he heard President Taft -- that's long before our time -- give a a talk at Cooper's Union, before World War I. After Taft finished talking, a fellow raised his hand and said, "Mr. President, what do you do if you can't get any job and you're a skilled mechanic and you've got three kids?" And Taft said, "God knows. I don't." Then my Dad went home and figured if the answer were in books, Taft would be likely to know it.

He was a very skilled mathematician -- that's what he studied at City College, the class of 1901. He asked, "Why do people hire other people for work?" To make a profit. "Where do these profits come from?" And he figured out a series of equations, if you will, which included all the sources of profits, and he published them in a book called *Economics As An Exact Science.* Like me, my Dad had no academic training, no degrees, nothing. So nobody paid any attention to it.

That's also my background. I never studied business. Although I taught business at City College, and that's a story in itself... I used to work with my father and I helped collect securities. And whatever I learned in business, he taught me. I taught at City College for a while and then I got a job as a trainee at a firm that no longer exists and probably no one remembers, called Hirsch and Co. Then I met some salesmen at Hirsch and Co. called Max Oppenheimer and two other German fellows. They were refugees from Mr. Hitler and they started their own firm and they asked me to join them as a partner.

To give you an idea of the importance of this firm, I was head of research. But if Goldman Sachs printed a report, say, on the Rio Grande railroad, I'd call up and ask for a copy, saying I would send over my messenger. I was 26. Then I'd put on my raincoat and go over to Goldman Sachs and I'd say, "I'm Mr. Levy's messenger. Do you have a copy of the report?"

Connors: (Laughs)

Levy: That's completely integrated operations. In the beginning, I wrote all the research reports. I was a financial journalist at the time -- I wrote for *Barron's* and *Financial World* and so forth -- but I was Oppenheimer's research department. I was head of research and chief bottle washer and all that sort of thing.

Connors: And the rest is history.

Levy: Yes. And the rest is history. I did start the Oppenheimer funds, and by the way, I just resigned as the head today. I felt 45 years is probably long enough.

Connors: I'm sure we'll read about in the papers tomorrow.

Levy: Or Monday, I think they intend to release it. It was all on very, very friendly terms.

Connors: Congratulations. Let's move onto your investment philosophy. One of the things you wrote is: "Most people believe that markets are driven primarily by economic factors and that psychology plays a minor role. I take the position that markets are driven by both psychological and economic factors."

Levy: I do believe that.

Connors: Can you discuss a little bit about what your belief is of psychology, and the role that psychology plays in the markets?

Levy: Sure. Assume a news event takes place. For example, we get into a war with Iraq. Is that good for the market or bad for the market? I can't *give* you an answer right now. We have to wait and see how the market starts to react. And then once we see, we get some feeling, and we'll have more of an idea as to whether it's a positive for the market or a negative. But most events can go either way. I noticed before World War II, every time there was a war scare, the stock market would go way down. When we finally got into the war -- not when *we* got in -- but the war started in September 1939, the market zoomed up. I don't know how you could have figured *that* out. It was a psychological event. People sold before the war on the war scares but when the war started, they bought.

Connors: And...

Levy: And I think there are many news events that are rather like that. It depends on the public's interpretation of the same event. It can be different at different times.

Connors: How do you take advantage of that?

Levy: Well, you can only take advantage once you have a feeling that this is what's going to happen and then you sell the stocks you want to sell, or buy the stocks you wish to buy. *But you have to act with the psychology.*

Connors: Let's use the example of the war with Iraq. Do you go in there with a premonition that, for argument's sake, it's going to be bullish because in previous events we've gone to war and markets have taken off as we've gone into war?

Levy: Yes, you have an intuition.

Connors: And you see that just the opposite is happening. We go to war and in fact it's not selling off. Does that change everything for you or do you become more aggressive at that point to the short side?

Levy: Well, I think it depends on the event, the mood of the market and other things which are going on at the same time. I don't think that you *can* tell. But you can have a gut feeling or an intuition.

Connors: If the market reacts opposite to that intuition, what happens?

Levy: You're wrong. But again the market will tell you fairly early how it's going to react and then you take it from there.

Connors: And how do you react? How have you reacted in the past when you're wrong? Are you out immediately?

Levy: Well, sometimes you run immediately, and it depends on the whole circumstance, the economy, how you see these things affecting economic practice and you have to make the best judgment you can make. The odds are not 100, or 90 or 80, but they're something over 50, maybe, if you have a lot of experience. No two experiences are ever the same and this is where your discretion comes into play.

Connors: You mentioned you had given some money to a hedge fund manager who proceeded to lose, I think it was 98% of its value, and you mentioned one of the stocks that he was buying in the hundreds that found its way down to $2.

Levy: Yes. Right.

Connors: And he was still rationalizing his decision to be in the stock. This is a gentleman who obviously meant well but along the way, price ultimately dictated... it overruled his belief system. Do you claim at the same time that price will ultimately overrule your belief system?

Levy: Well, I think price and the action of a security is one of the elements that goes into the decision making. Now we have to say that this fellow is a little bit of a fool. And I know because he used to work for us and he seemed to be a perfectly sensible, fine fellow. But he obviously had a problem. He couldn't adjust to different conditions and I think a trader has to have the ability -- or an investor I should say -- has to have the ability to adjust to being wrong. In other words, you can't be too stubborn. You must have a certain degree of flexibility as to what's going on.

Connors: Yes, I fully agree. Your performance with your fund -- especially the hedge fund -- is extraordinary. Did you find that the performance was straight line, or...

Levy: No, we had ups and downs. Every day was another day... but it wasn't a straight line.

Connors: Obviously more ups than downs...

Levy: Well, the record speaks for itself, so apparently yes. I mean in my life -- and I was in the markets for 50 years -- the ups were better than the downs

Connors: Were the ups from hitting home runs or a lot of singles?

Levy: Well, my nature -- and now we get back to the personal psychology -- I like to be a long term investor. Maybe it comes from laziness. I don't have to make too many decisions. But I like long-term concepts anyhow.

Connors: So for you, your performance came from hitting home runs?

Levy: I would say I made more home runs than most other fellows who were in the markets. And I traded less.

Connors: The home runs were more than enough to overcome the losing trades.

Levy: Correct.

Connors: If you were to give advice to people who were just starting out today, what would you tell them? The markets have obviously changed over the last 45 years and you've had an influence in the change of the marketplace...

Levy: The markets have changed, but I don't think psychology changes that much.

Connors: Please explain that.

Levy: I think that people are still motivated by fear and avarice. And sometimes they are more fearful and other times they are more greedy.

Connors: And if you were to give advice to somebody who was just starting out today, would you tell them to learn the psychology of the markets first?

Levy: Well I would tell them that's terribly important and they ignore that to their own detriment.

Connors: Did instinct play a role in your success?

Levy: Oh yes, there is instinct. But then what is instinct? It's really all of your *past experiences put together* and somehow -- we don't exactly know how the mind works but you make some decisions based on everything that's happened before.

Connors: Another question... you talked about getting out of a position. You say, "If I found myself in a position worrying about a stock and I have learned from bitter experience and decide to sell, not to sell a small part but to sell, for example, a third or a half." How does that come about? Do you basically make a commitment to walk away from your decision?

Levy: What you're saying is I'm beginning to question the decision. And it takes so much energy to change one's mind that if you're going to change your mind, you may as well do it for a *meaningful amount.* I mean, we're never sure of anything in the market. I don't know if anybody could buy a security and be certain it's going to go up or do what it's supposed to do. So, you then say that if I decide to take a position, then change a position I have thought a great deal about, I want to be sure I make a major change. It's like treating it with a BandAid to sell just a little bit... you might think you've done something, but you haven't. So if you're going to do something, you might as well do something that's going to have some meaning.

Connors: Great advice. Let's talk about your market outlook. You've been pretty bearish for the past few years.

Levy: Right.

Connors: What would make you change your mind?

Levy: Well you know my family are economists. They run the Jerome Levy Forecasting Center up on Mount Kisco which is run by my nephew, David Levy. His work is probably more analytical and less psychological but if he sees corporate profits trending upward, and I should add he doesn't see that now, he sees them going down... I would be inclined to become more optimistic as far as economics is concerned.

Connors: So, what would make you change your mind about the market? Would it be psychology combined with those corporate profits? Do you want to see those corporate profits rising and money pouring again into the marketplace from investors?

Levy: **Well I like to see corporate profits rising and everybody very negative**. You would have to think that's positive because then everybody can change and become positive. But if everybody *began* by being positive as they were a few years ago, well, there's no room -- if all the money that's going to be invested, speculated in the market, is committed, then you have to be pretty negative.

Connors: Are we getting anywhere near levels of pessimism in your mind, where they should be at these levels?

Levy: No.

Connors: You believe that some of the better opportunities are in some of the smaller nations. I believe you favor Russia and a couple of other countries.

Levy: Well, that's a long-term view and that has to be intuitive as much as anything else, but I think that countries which have much cheaper labor markets and highly intelligent people who speak English -- like India or China or Russia -- are probably... and Russia certainly... are going to be good places to invest.

Connors: How do you go about creating a portfolio knowing how much risk you should be taking in any position?

Levy: Well, what I did in Russia -- and I don't think any one person's strategy necessarily applies to everybody -- but in Russia, I knew a portfolio manager who ran a fund and I thought it was he was very straight and very able and knew his field very well, so I took a major position in Russia through him.

Connors: Are you more aggressive managing other's money than you are managing your own?

Levy: Well I like to treat all money as though it was my own money because I think everybody cares as much about... you care about $1,000 as much as I do. I do think you have to refer to what you would do yourself. I never liked the idea of buying a stock that I wouldn't buy for myself.

Connors: Is there some point if your position starts moving against you, let's say you're 20% down, or 30% down, that you say, "Uncle. No more. I need to get out of this."

Levy: Well, if that happened, let's say I owned something. Let's even say Russia, since we started talking about Russia. And I would figure if it went down 20%, gee, there may be something out there that I don't know. There's always something you *don't* know. And I would probably start lightening up.

Connors: So price will dictate your action.

Levy: Yes, but with one caveat. If it's caused by some event that I think is silly. In other words, it might be a reason why people get very discouraged about Russia and I think that reason has no merit whatsoever. I'd probably want to buy more.

Connors: So you really are taking each position and taking all the pieces together and making decisions along the way. There's nothing mechanical about the approach.

Levy: I think you put it very well.

Connors: I'm glad we were able to get to that point. Many successful traders and investors use a fixed formula for going about making their decisions. For you, your fixed formula is a combination of psychology and corporate profits. And then from there you use your experience to guide you on the proper way to proceed with the position.

Levy: Yes, exactly.

Connors: I greatly appreciate your time, Mr. Levy.

Levy: Thank you very much. It's been a pleasure talking with you and I appreciate it.

Connors: Thank you. I wish you the best of luck.

My thoughts:

First, as I mentioned in the introduction, he's old school. He's sly as a fox. And he's not going to show his hand beyond what he wants to. But, he was kind enough to share a handful of things with me which will ultimately impact my own viewpoint of the markets and my own trading. Some of these are:

1) His unparalleled performance has come from hitting home runs. He risks X to make many times X. He claims he's just lazy and just doesn't want to do the work to get out of a position (I could see him smiling through the phone as he was telling me this.) The bottom line is, he does substantial homework before making a decision and if his analysis is correct, he makes many times what he originally risks. If not, he aggressively gets out and looks for other opportunities.

2) The early major move from a historic event many times is the beginning of a much larger move. This information will be key if and when we go to war with Iraq.

3) Psychology of the markets has played a key role in his success. In his words, not applying it to your own investment decision-making process would be a detriment to your performance.

4) Rising corporate profits combined with bearish sentiment will lead the next bull market and likely every bull market in the future. On the opposite side, declining corporate profits combined with bullish sentiment precedes bear markets. You only have to think back to Intel missing their numbers in the summer of 2000 to fully appreciate this.

5) Even the best are many times wrong. But, what they do very well is walk away. They don't let stocks drop 98% on them.

6) Leon Levy has parlayed a stake of $200 into a net worth which makes him amongst the wealthiest people in the country. He is the epitome of someone who has learned how to correctly "make money with money."