



# SPECTRUM

## INVESTMENT ADVISORS

### Woodstock of Capitalism

Berkshire Hathaway Annual Shareholders Meeting  
Omaha, Nebraska - May, 2014

**James F. Marshall**

President

**Jonathan Marshall**

Senior Investment Analyst

For the eighth consecutive year, Jonathan and I, along with my brother Dave and his son Vince, joined up with Gary Vanden Heuvel, President of the BLC Community Bank and his son Sam and friend John Wiley, and embarked on our annual pilgrimage to Omaha.

This year's Berkshire Hathaway Shareholders Meeting had a record crowd of over 40,000 at the Century Link Center (formerly the Quest Center) in downtown Omaha. Our group looks forward to the trip each year, much like many of you would anticipate an annual fishing trip. Our trip to Omaha is deep in tradition, including watching this year's California Chrome win the Kentucky Derby at Mr. Toad's on Market Street, four blocks from the Century Link Center. Last year we had dinner at Gorat's, one of Warren Buffett's favorite restaurants in Omaha. To add something different this year, we had dinner at Warren's other favorite restaurant, Piccolo Pete's, where Alex Rodriguez from the New York Yankees was sitting at the next table. Both Gorat's and Piccolo Pete's are a reflection of Warren's life—simple, not overstated, reasonably priced and a good bargain. We had two gentlemen from Sydney Australia (who attended the meeting) take our group's picture outside of Piccolo's.

This year we had a chance to meet Howard G. Buffett (Warren's son) and his grandson, Howard W. Buffett, at a book signing. Howard and his son are authors of the new book, *40 Chances*, inferring that the average farmer plants 40 crops in their career. Growing up on a farm in Redgranite, I totally agree that each Spring, a farmer takes a chance on the weather to plant still another crop. Many of you may have seen Howard Buffett on *60 Minutes* last year, riding his John Deere combine.

Howard G. Buffett owns 4400 acres with 1500 acres of corn (grain) near Decatur, Illinois and experimental farms in Nebraska, Arizona and Africa. Howard is worth \$3 billion (not bad for a farmer). The last billion was given to him by Warren to go out into the world and teach people good farming practices in places like Africa. Howard's job is to give away that billion dollars over the next 40 years in the quest to make people self sufficient with better farming techniques. A fact in the book that we found interesting is that it takes nature 500 years to produce one inch of topsoil, so erosion control is extremely important in farming. Like his father, Howard seems like the farmer next door; friendly, engaging and a little overweight, but a lot of fun.

Berkshire Hathaway has 22 employees who work in Omaha, but oversee 300,000 employees in the 80 BH companies. What makes listening to Warren and Charlie interesting, is they have a lot of short answers that get to the point, many times, with a sense of humor. Charlie's answers are even shorter than Warren's, often stating, "I have nothing to add."

Both Warren Buffett 83, and Charlie Munger 90, seemed as spry as ever

with Warren once again kicking off the meeting with a video and a dance. After catching his breath, Warren began the meeting. After 45 minutes of a Berkshire Hathaway (BH) video featuring the managers of BH's 80 companies, Warren and Charlie began by answering alternating questions from three members of the press, including Carol Loomis and Becky Quick from CNBC, three investment analysts and members from the audience. The Q&A session lasted two and a half hours with a one hour lunch break, followed by another two and a half hour Q&A session, ending with a 30 minute Board of Director's meeting.

Prior to the Q&A, Warren mentioned that after sending out proxy's to over a million shareholders asking the question whether or not BH should pay a dividend, by a 45 to 1 margin the BH shareholders turned down the opportunity for a dividend; choosing instead to have Warren invest the profits of the company.

As in the past, with two boxes of See's Candy (a BH company), peanut brittle, two cans of Cherry Coke (BH owns 8% of Coke) and two glasses of water, Warren and Charlie, without rehearsing, asked for the first question please. Charlie's first yawn was at 3:25 p.m. - 6 hours later. Not bad for a guy that's 90. The following are answers, by Warren and Charlie, to a few of our favorite questions:

**You stated that your goal is to outperform the S&P 500 Index, but you haven't lately. Your comments.**

**WB:** It's obvious that if the market has had five strong years in a row we will not beat the S&P 500. We generally underperform in the up years and outperform in the down years, but in any long-term business cycle, we will outperform. There is no question that our size is an anchor on performance.

**CM:** In the last couple of years, the value of BH went up \$60 billion. If this is a failure, I want more of it. (laughter from the audience).

**Why don't you sell some of your poor performing businesses?**

**WB:** We keep our businesses because we make a promise, so that our managers and the managers of future businesses we buy, know they can count on us. If we don't, the word gets out on us. *Seldom does Warren buy a company to purge it and fire all of its employees.* We have only sold a few businesses since 1949, one of them being the original Berkshire Hathaway textile business. *WB says a "brand is a promise".*

**CM:** We behave the way we do because we love doing it.

**WB:** You can tell Charlie doesn't get paid by the number of words he says (laugh).

**What would you suggest in selecting and compensating directors?**

**WB:** Most compensation committees don't look for directors that are Doberman pinschers, but rather directors who are cocker spaniels, preferably with their tails wagging. Selecting a director who is somewhere in between may be the right thing to do.

**CM:** Directors who act like Doberman pinschers and say no to everything lose the respect of the group, where the group begins not to pay any attention to them over time. If you say no, you need to pick your spots and pick your battles, and not say no to everything. Warren calls me, the abominable no man.

### **What was your latest acquisition and why?**

**WB:** Our latest acquisition is AltaLink, an operator of 280 electric substations and about 7500 miles of transmission lines in Alberta, Canada, which owns half the grid and serves 85% of the population in the area. Our latest stock purchase was Exxon, of which we now own 41 million shares. Most of the Exxon stock was purchased in the third quarter, 2013.

*Warren feels very positive about the energy business, including fracking, illustrated by buying the Burlington Northern Sante Fe (BNSF) Railway in 2010, which runs right through the Bakken Region in North Dakota. Warren asked the manager of BNSF, Matt Rose, to stand up and comment about BNSF's business. Matt says that the Bakken (ND) oil came a lot faster than expected and that BNSF will spend \$5 billion this year to increase capacity and improve the safety of the railroad system.*

### **Why do you have so much cash on your balance sheet?**

**WB:** Berkshire Hathaway will always have at least \$20 billion in cash in any market. Berkshire currently has \$48.9 billion in cash, which could be used to buy securities as well as to acquire whole companies. We never want to depend on the kindness of strangers. Cash or credit is a lot like oxygen, you don't notice it until it's gone. Everyone of our companies have more cash than they need. Berkshire's strong financial position means we can't be pressured into buying or selling something. We might do some dumb things, but it won't be because we were forced into it.

**CM:** We don't use sweep accounts. Sweep accounts aren't pleasant. They create an undesirable tone on a company.

*In 2003, BH owned \$30 billion worth of stock in 10 companies. Today, 15 companies account for almost \$100 billion in BH owned stock, which include: American Express, Coca-Cola, Moody's, Wells Fargo, DirecTV, Exxon, Goldman Sachs, IBM, Munich Re, Phillips 66, Procter & Gamble, Sanofi, Tesco, US Bank and Walmart. In addition, BH owns \$20 billion of stock in 30 other companies. The above list is not a recommendation by Spectrum (Omaha World-Herald 5/3/14).*

### **What is your philosophy on managing people?**

**WB:** We give our managers a lot of freedom. We don't have an HR department at BH (with 22 employees). By the standards of the rest of the world, we over trust. Berkshire Hathaway creates a culture of trust by hiring the right people.

**CM:** A culture of measuring too much of a company's operations does more harm than good.

### **Is investing in the US more attractive than investing internationally?**

**WB:** Berkshire Hathaway has not had a lot of recognition in foreign countries, unlike the US. Our best international investment so far has been Iscar, a manufacturing company in Israel. The founder of Iscar wrote a letter a few years ago addressed to me stating he wanted to sell to BH. In the letter he said if we cannot sell to BH, we are not selling, which illustrates the strength of our culture and brand. Our best bet by far is to buy a business from a founder with a good business model, who also has passion and loves their business. BH has very few international investments and would rather invest in major US Global brands, who do business worldwide.

**CM:** We could not have done BH in any other country and be this successful. What a great country.

**WB:** We like to buy wonderful businesses from people who care about their company and still want to continue to run their company after they sell to Berkshire Hathaway.

### **If you were 23 years old and wanted to go into a non-tech business, what business would it be?**

**WB:** I would go into the investment business because it is not a capital intensive business, nor does it take a lot of capital to get started.

### **You have a reputation for being frugal. Why don't you play more, work less and enjoy your life?**

**WB:** There is a point in consumption where you have an inverse correlation. If I owned 6-8 houses, it would not make me happier. I was blessed

with great parents and also blessed with an occupation that I love. I tap dance to work every day.

*Warren Buffett still lives in the same house he bought in 1958, and Charlie Munger still lives in the same house he bought in 1960.*

**CM:** I look out in the audience and see a lot of understated people. We collect you people.

### **What about a succession plan at Berkshire Hathaway?**

**WB:** Long term, my son, Howard, will become Chairman of the Board whose main job will be to protect and act as a guardian to the Berkshire Hathaway culture. I have four to five candidates in mind that could some day take my position, but for now I would rather have them keep running their own companies.

*Two of the likely candidates are managers from his top five companies who both stood up and answered questions from the audience during the meeting. Matt Rose from BNSF Railroad and Greg Abel from Mid American Energy. They both answered questions from the audience at last year's meeting. Could be a telling sign on Warren Buffett's succession plan.*

**CM:** The momentum is in place. The ethos (culture/values) will be in place for a long time at BH. I would not sell your Berkshire Hathaway stock.

### **America has made a huge mistake by letting our public schools go to hell. Can you comment on that?**

**CM:** Warren let me take this one. What's wrong is not our grade schools or our high schools, it's our universities and what they're teaching. Long-term, it's not the schools, it's the behavior of the parents that matter most. Parents need to lead and love by example.

**WB:** The earlier financial literacy can be taught in our schools, the better. Many people spend their lifetimes digging themselves out of financial holes. Both Charlie and I learned financial literacy from our parents in early grade school.

### **Can Berkshire Hathaway get too big?**

**WB:** In 20 years BH will be worth \$1.2 trillion. Someday we will have more cash than we know what to do with. At that time, we will deploy more cash to repurchase shares.

**CM:** It's not a tragedy to succeed so much that returns go down.

The renaissance in energy (fracking) that Warren talks about, should give our country a durable competitive advantage for years. An example of the potential of our nation's renaissance in energy is a new 3000 acre energy complex in Lake Charles, Louisiana. SASOL, a former South African state oil company, is embarking on the single largest foreign investment project in US history. SASOL plans to spend \$21 billion in developing a natural gas plant. In total, 66 industrial projects, worth \$90 billion, will be breaking ground in Louisiana in the next five years. It's viewed by the *Wall Street Journal* as the Qatar on the Bayou (5/28/14). This potential development stems from the positive impact on the local and national economies because of the energy boom in our country. For those of you who want to learn more about the impact of fracking, we suggest the book *The Frackers*, by Gregory Zuckerman.

Warren and Charlie talk about being in acquisition mode and trying to find more whole companies to buy. They are not purposely building cash, anticipating the next correction in our economy. They both appear bullish on the market, realizing that we will continue to have cyclical market corrections every 4-6 years, but they do not appear to see anything devastating ahead.

All in all, a very positive outlook on our country. When the question was asked, **When was it the best time for a child to be born in this country?** Warren's answer was, today, where our young children have a great future and wonderful opportunities ahead of them in this country, as long as they have the right parents.

Once again, we enjoyed our trip and have already made reservations for next year's meeting. We appreciate your business.