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Berkshire Hathaway Annual Shareholders Meeting
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For the twelfth consecutive year, I, along with Jonathan, my brother David and Scott Schwartz, joined Gary Vanden Heuvel, President of BLC Community Bank, his sons, Sam and Casey, and Casey's friend Scott Lorge, for our annual pilgrimage to Omaha. This year's event marked the 52nd Anniversary of the Berkshire Hathaway (BH) shareholder meeting, with **Warren Buffett** (86) and **Charlie Munger** (93) on stage. Fifty-two years ago, Warren started with $105,000 of family money. Today, BH is worth $620 billion, up from $552 billion in 2015, making it the fifth largest company in market value in the United States. In 12 years of attending, we still find Warren and Charlie as informative, witty and entertaining as ever. Warren and Charlie both grew up in Omaha, less than two miles from the CenturyLink Center, the site of the BH annual meeting.

Even though the doors opened at 7 a.m. and the session didn't start until 8:30 a.m., some attendees arrived at 10:30 p.m., the night before, in order to get a good seat. During the wait, the song *New York*, by Alicia Keys, was once again played, with the word "Berkshire" used in place of "New York". The song was followed by a 45 minute video highlighting BH, which owns close to 90 companies; 50 of those managers were in attendance. After a Coke ad, the video featured clips from a recent HBO documentary entitled, *Becoming Warren Buffett,* featuring unpaid celebrity cameos. One memorable part of the documentary is Warren singing his own version of *My Way*, with Paul Anka, who wrote the song for Frank Sinatra. Warren sings, "I pray each day for Charlie Munger. Who needs the gym? When next to him, I feel younger!" Another part of the documentary, which made the audience laugh and cheer, was when Warren ordered breakfast from a McDonald's drive-through, basing how much he spent on his order on the previous day's price of BH. Warren's life is complex, but also simple. He lives and works in Omaha, on the same street, 20 blocks apart, with the McDonald's in between.

Each year, close to the end of the video, a clip of Warren's 1991 testimony before Congress, when politicians were investigating a bond trading scandal at Salomon Brothers, is played. Warren was called in to sort out Salomon after the scandal broke. In that testimony he states, **"The spirit of compliance is more important than the words of compliance. Lose money for the firm, and I will be understanding; lose a shred of reputation for the firm, and I will be ruthless. I welcome your questions."** Even though the majority of the meeting was broadcast on the Internet for the second year in a row, there were still 40,000 people in attendance, which matches the record set at the 50th Anniversary meeting. What's so remarkable is that Warren and Charlie would spend their time, the first Saturday of every May, answering five hours of unrehearsed questions. You would think businessmen of their standing would rather go golfing or fishing.

Charlie needed help sitting in his chair again, but once he was seated, he was ready to go. Warren kicked off the meeting by saying, "That's Charlie. I'm Warren. You can tell us apart because he can hear and I can see. That's why we work together so well."

The following are answers to a few of our favorite questions, with 18 questions coming from members of the media, including Becky Quick from CNBC and Carol Loomis, former editor-at-large at *Fortune* magazine and editor of Warren's annual BH shareholder letter. In addition, 18 questions came from investment analysts and 18 from the audience, in alternating fashion. What is most remarkable about the annual meeting is the way Warren and Charlie respond to complex, technical questions with eloquent and witty words of wisdom that even novice investors can understand.

The first question was about Wells Fargo, which is Berkshire's largest equity holding, and the sales practice scandal.

How do you satisfy yourself that BH isn't subject to the same risks as Wells Fargo with its highly decentralized structure and the very substantial autonomy given to senior leadership of the operating companies?
WB: We certainly operate on a more decentralized plan than any company that's remotely our size and we count very heavily on principles of behavior, rather than loads of rules. That's one reason that at every annual meeting you see our Salomon Brothers video clip and that's why I write very few communiques to our managers. I send them a letter once every two years that says that we have all the money we need, we'd like to have more, but it's not a necessity, but we don't have one ounce of reputation to lose and that our reputation at Berkshire is in their hands. **Charlie and I believe that if you establish the right sort of culture, and that culture to some extent self-selects who you obtain as directors and as managers, that you will get better results.** There's nothing wrong with incentive systems, but you have to be very careful what you incentivize, you can't incentivize bad behavior. If so, you had better have a system for recognizing it.

Warren criticized Wells Fargo's previous management for failing to take action immediately upon learning that its employees were signing up customers for accounts they didn't want. Of the bank's ousted CEO, John Stumpf, Warren said, "The moment the CEO heard about it, he had to act. He didn't."

What attributes do you look for when you invest in a business?
WB: We sort of know it when we see it and it would tend to be a business that for one reason or another, we can look out 10 or 20 years and determine that the durable competitive advantage that it had at the present would last over that period and it would have a trusted manager that would not only fit into the Berkshire culture, but that was eager to join the Berkshire culture. Then it would be a matter of price. When we buy a business, essentially we're laying out a lot of money now, based on what we think that business will deliver over time and the higher the certainty with which we make that prediction, the better we feel about it.

If you go back to our early years, it wasn't the first outstanding business we bought, but it was kind of a watershed event, which was a relatively small company, See's Candy. We made a judgement about See's Candy, that it would be special and probably not in the year 2017, but we certainly thought it would be special in 1982 and even 10 years later, fortunately, we were right on it. We're looking for more See's Candies, only a lot bigger and not capital intensive, but they're hard to find.

WB: There's nothing like the pain of being in a lousy business (*BH owned Dexter Shoes and closed it five years later*) to make you appreciate a good one. What you learn is what to avoid. If you have a wonderful business, even if it's a small one like See's Candy, you basically have an economic castle, and in capitalism, people are going to try and take away that castle from you. So you want a moat around it, protecting it, then you want a knight in the castle that's pretty darn good at warding off marauders, but there are going to be marauders and they'll never go away. Charlie?

CM: I have nothing to add.

WB: If you keep that up, we might need to cut your salary. (Laughter)

Tell us why you sold 1/3 of your shares in IBM yesterday?
WB: We bought IBM six years ago and sold a third of it yesterday. Investing in IBM has been disappointing, but our worst mistake in tech was not investing in Google. Berkshire's subsidiary, Geico, was paying $10 or $11 to Google every time someone clicked on an ad.

Unlike most investors, when Warren sells a stock, he doesn't just reinvest in another stock, but rather will sit on cash and do his homework and research before reinvesting.

Why didn't you buy Amazon?
WB: Stupidity! Jeff Bezos has been the CEO, almost simultaneously, of two businesses starting from scratch and we missed it entirely. We never owned a share of Amazon. I was too dumb to realize what was going to happen. I admired Jeff, but I did not think he'd succeed on the scale that he has, and I didn't even think of the possibility that he'd do the things with the cloud services. I never even considered buying Amazon. I always thought it was too expensive. My biggest regret isn't that we did not invest in Amazon, it is that we did not invest in Google.

How has the investment business changed?
WB: Four of the top five US companies (Apple, Google (Alphabet), Microsoft, Amazon) are not capital intensive. That is a different world than what existed in the past. Our nation, for 200 years, was built on capital intensive companies, railroads, energy industry and the auto industry.

CM: The railroad industry was a very poor investment for years and now has gotten good with only seven railroads left in the country. It's part of why we bought Burlington Northern Santa Fe Railway.

WB: The five largest companies in the S&P 500 together have a market cap of $2.5 trillion, which represents 10% of the entire market. Most of them are low capital intensive companies.

CM: Chemical companies at one time were wonderful investments. Today they are commoditized, making them tough businesses to run.

WB: The US was built on tangible assets. Today, it's a different world with lower capital intensive businesses, which is likely to continue.

So why wouldn't Warren go just go out and buy Amazon and Google today? He doesn't chase returns. ***He would rather quietly build cash and then wait and wait and wait. He compares investing to baseball. You don't have to swing at everything, you just wait for the fat pitch.*** *Warren liquidated his entire holdings of marketable securities in 1968-69 and all but a few in the late 80s, and started buying bonds in 1999, just before the 2000-2001 correction. After the market corrected in the late 60s, Warren waited for three years before investing in another stock, waiting for the fat pitch.*

Warren hired Todd Combs and Ted Weschler, who each invest in about 10-12 companies independent of Warren. Todd and Ted have been accumulating shares of Apple and BH has doubled its stake in the first quarter, 2017. BH now owns 2.5% of Apple. Apple recently disclosed that they now have over $250 billion in a cash/bond reserve. If Apple's reserve fund were a mutual fund, it would be the largest bond fund in the world (Bloomberg 5/4/17).

Today, due to his size, Warren doesn't exit the market in a big way, but rather quietly builds cash. The chart at the top illustrates BH's buildup of cash for the past eight years, from $30 billion to over $90 billion. In his annual letter to shareholders Warren wrote, "Every decade or so, dark clouds will fill the economic skies, and they will briefly rain gold. When downpours of that sort occur, it's imperative that we rush outdoors carrying washtubs, not teaspoons." A good example of this is in 2009, when no one else would lend GE and Goldman Sachs money, Warren cleaned up by lending to both at a higher interest rate, plus warrants, which provided the ability to purchase more stock at a set price. Warren's cash build up is something to monitor as we approach the end of this decade.

CM: If things go to hell in a handbasket, and then get better later, we will do better than others. We are good at navigating through that kind of stuff, due in part to our cash position.

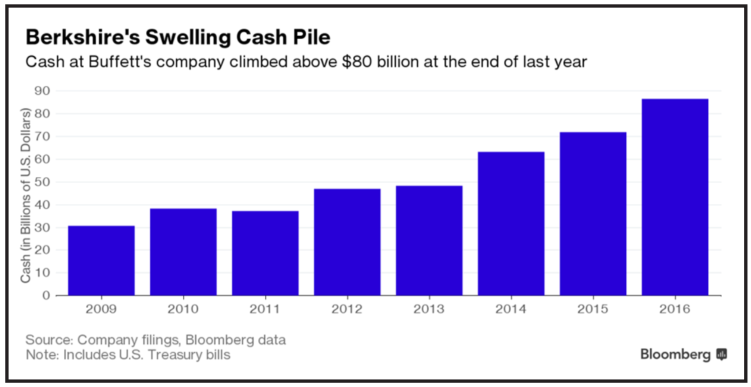
WB: When markets go haywire we will have enough cash to survive.

What do you follow as the most important factor in investing?
WB: Interest rates. The most important number to follow vs. all other indicators is interest rates.

Warren pays close attention to the yield on the S&P 500 vs. the yield on the 10-year treasury. For example, in 1999 when the yield on the 10-year treasury exceeded 6.2% vs. the yield on the S&P 500 at 1.1%, he bought treasury bonds vs. stocks.

When you are gone, why do you advise your wife to buy the S&P 500 Index?

WB: There will be less worry investing in the S&P 500 Index vs. owning any one single company. The important thing is for her not to worry the rest of her life. However, if I died tonight, I think the BH stock would go up tomorrow.



CM: The Mungers are different. I want them to hold the BH stock vs. the S&P 500 Index. The S&P 500 Index is very hard to beat, but I am just more comfortable owning BH stock. If you want to protect your heirs from the stupidity of others, you may have a good system, but I am not much interested in that subject. (Laughter)

Buffet introduced and thanked index fund king, Jack Bogle, founder of the Vanguard Group in 1974, who celebrated his 88th birthday the Monday after the meeting. Bogle created the first index fund that allows investors to passively invest in the stock market by tracking a lower cost market index.

In this year's annual report, Warren made a bet 10 years ago that Ted Seides, a hedge fund manager, couldn't beat the return of the S&P 500 Index. Ted picked five hedge funds, that generally charge 2% annual fees per year, plus 20% of the profits. Could the hedge fund managers beat the S&P 500 Index over 10 years? After 10 years, ending in 2016, the average return of the five hedge fund managers was 2.2% compounded annually vs. the return of the S&P 500 Index at 7.1% compounded annually. As much as Warren likes the S&P 500 Index, he still prefers active managers, like BH's Todd Combs and Ted Weschler. He believes that hedge funds charge too much in fees.

At Spectrum, our business model is to combine active management with index funds. For example, index funds generally do well in the large and mid cap space, but active managers generally do better than index funds in the bond market, small cap and international space (Morningstar).

How smart do you have to be to be a good investor?
WB: There is nothing more agonizing than seeing your neighbor, who you know has a lower IQ, getting richer than you are.

CM: I think we have one big advantage. A lot of other people are trying to be brilliant, and we're just trying to stay rational. Trying to be brilliant is very dangerous, particularly when gambling. Fear can spread like you wouldn't believe, until you have experienced it a few times.

Warren says if you have an IQ of 150, sell 30 points to someone else. The difference between a good investor and a mediocre investor, is not their IQ, but their ability to control their emotions.

What are your thoughts on the sugar content in Coca-Cola products?
WB: I drink five, 12 ounce cans everyday. It has about 1.2 ounces of sugar in it. I think the choice is mine. Maybe sugar is harmful, but I think Coca-Cola has been a very positive factor in this country and the world. I really don't want anyone telling me I can't drink it. I think there's something in longevity of feeling happy about your life.

How much should BH pay for your successor?
I actually would hope that we have somebody that's already very rich, which they should be if they've been working a long time, and is not motivated by whether they have 10 times as much money than they and their families can need or a 100 times as much. If the board hires a compensation consultant after I go, I will come back—mad.

Charlie, what do you dream about?
CM: A life properly lived is just learn, learn, learn all of the time. Sometimes, when I am especially wishful, I think **'oh to be 90 again'.**

As we have said before, attending the Berkshire Hathaway Shareholder Meeting is an unforgettable experience. We wanted to share with you our thoughts on the meeting and have already made reservations for next year's annual meeting, the first Saturday in May. Some people describe it as getting an MBA in a day. Warren and Charlie are wonderful teachers. It truly is the Woodstock of Capitalism.