BERKSHIRE HATHAWAY 2011 ANNUAL MEETING NOTES

BY INGRID R. HENDERSHOT

We attended the Berkshire Hathaway annual meeting held on April 30, 2011 in Omaha along with about 40,000 other folks from around the globe who gathered once again for the Woodstock for Capitalists. Warren Buffett, Chairman of Berkshire Hathaway, and Charlie Munger, Vice-Chairman, answered questions for nearly six hours.

FIRST QUARTER RESULTS

Warren Buffett began the Berkshire Hathaway annual meeting with a discussion of the preliminary 2011 first quarter results which revealed that operating earnings declined 28% during the first quarter to $1.6 billion with net earnings down 58%, primarily due to a swing to an $82 million loss on investment and derivatives compared to a $1.4 billion gain in the prior year period. On the operating side, the railroad, utilities and energy group increased earnings 79% to $908 million, which included a full year of Burlington Northern Santa Fe's (BNSF) results compared to just a portion of last year's earnings from the period when BNSF was acquired. The railroad business is expected to have a very good year this year with the industry's competitive advantage growing by the day as oil prices increase.

The manufacturing, service and retailing group increased earnings 17% to $558 million as all businesses, with the exception of housing, have been getting better quarter by quarter since the fall of 2009. With Berkshire owning more than 70 companies, they represent a good cross-section of the U.S. economy.

On the other hand, the insurance operations suffered the second worst quarter ever for the insurance industry (behind Hurricane Katrina losses in the third quarter of 2005) with industry-wide damages estimated around $50 billion. Berkshire generally coves 3%-5% of industry damages. While the first quarter felt the brunt of extraordinary earthquakes, the worst part of the year (hurricane season) for reinsurers is still to come.

Around the globe, there were major catastrophes which hit the reinsurance industry hard especially in Asia/Pacific, including the earthquake in New Zealand, the Australian floods and cyclone Yasi, and the major earthquake and tsunami in Japan. Berkshire's estimated losses incurred from these events totaled $1.7 billion, of which approximately $700 million came from their 20% quota share of Swiss Re's business. As a result, Berkshire booked an $821 million insurance underwriting loss in the first quarter compared to a $226 million gain in the prior year period. Subsequent to quarter end, the tornados in the South will result in losses for GEICO. While GEICO doesn't insure homeowners (only acts as an agent for homeowner insurance), they will suffer losses from the estimated 25,000 cars which will put in claims as GEICO has 9% of the market share for auto insurance.

Nevertheless, GEICO had a tremendous first quarter with auto policies in force increasing 46% to 318,676. In the annual report, Buffett had written how the real value of GEICO's economic goodwill is about $14 billion even though Berkshire is carrying the goodwill on its books at only $1.4 billion due to accounting rules. With GEICO off to a strong start in the first quarter, it is easy to see why Buffett said the company's value is likely to be much higher ten and twenty years from now. GEICO is gaining market share every day with a very significant percentage of its customers having been with the company for 10 years or longer. Buffett joked that the cost of holding the annual meeting could be defrayed if just 66 shareholders would sign up with GEICO at the booth during the annual meeting, as this would increase GEICO's valued by $100,000 (since each new policyholder generates $1500 in goodwill value).

In the annual report, Buffett had written that he expected Berkshire's normalized pre-tax earning power to be around $17 billion and $12 billion after tax, assuming breakeven insurance operations. For the past eight yeas, Berkshire's insurance operations had done better than breakeven. However, in 2011, given the first quarter catastrophes, it appears that for the first time in nine years, Berkshire will have an underwriting loss. This doesn't change Buffett's expectation that over time the insurance operations will break even, and Berkshire will get the benefit of the free use of float.

Insurance investment income dipped 4% to $952 million in the first quarter, and Buffett expects that investment income will go down even more since the 12% Swiss Re investment was called, the 10% Goldman Sachs preferred stock was called subsequent to quarter end, and the 10% GE preferred stock is expected to get called later this year. As a result, Berkshire will be losing three high-yielding investments.

As of quarter end, Berkshire held $38 billion in cash, not including the $5 billion received from Goldman Sachs after the quarter closed. The cash is earning virtually nothing today, but over time Buffett expects Berkshire's investment income will grow even though it will drop this year.

In discussing first quarter results, Buffett also talked about the $337 million loss which had to be taken on part of his Wells Fargo investment due to the loss having to be classified as an other-than- temporary impairment loss. He said accounting rules required this loss to be run through the profit and loss statement even though it had already been reflected on the balance sheet. At the same time, the $3.4 billion in total unrealized gains on Wells Fargo had to be ignored in the profit and loss statement. Berkshire determines its gains and losses on a specific identification basis. Had gains and losses been determined based on average cost, Berkshire would not have been required to record an other-than-temporary impairment charge with respect to the investment in Wells Fargo. This "fuzzy" accounting is why Buffett advises investors to ignore gains and losses on investments and derivatives on a quarterly basis. It is more important to focus on the operating earnings and gains in book value and intrinsic value when evaluating Berkshire's financial results. However, Buffett cautions that news headlines will focus only on the "all deceptive figure" of net income and not what is important to understanding Berkshire's underlying business results.

QUESTONS ON DAVID SOKOL AND HIS TRADING IN LUBRIZOL STOCK

As expected, there were a number of questions on David Sokol's trading in Lubrizol stock, which Buffett called "inexplicable and inexcusable." The complete transcript of all the Sokol questions and Warren Buffett and Charlie Munger's answers has been posted on Berkshire Hathaway's website linked below:

http://www.berkshirehathaway.com/dlsokol/TranscriptSokolQuestions.pdf

IMPLICATIONS OF THE END OF QE2

With the government's quantitative easing program set to end in June, a shareholder asked what the implications would be for the stock and bond markets. Buffett noted that there is no secret about what the Federal Reserve is going to do or what the Fed's balance sheet will look like. As a result, he believes the effect of the ending of QE2 has already been discounted in the stock market. He sees no reason why having the program come to an end will have any effect on the stock market or the bond market on that date. With the government no longer buying Treasuries, a big purchaser will no longer be in the market. The market will be different, but that has already been anticipated. Charlie Munger wryly said, "I have nothing to add."

SUCCESSION PLANS

Given that many folks felt David Sokol was a leading contender to be Buffett's successor and the controversy over Sokol's trading in Lubrizol stock, a shareholder asked how Buffett could be sure there were no more Sokol's in the successor lineup. Buffett commented that the shareholder made an assumption about Sokol being the next in line, which he is not sure was warranted, but the shareholder certainly was entitled to think that Sokol was a candidate.

Buffett added that is one of the reasons he thinks it's a good idea if his son, Howard Buffett, who would get paid nothing and have no activities in the company, becomes the chairman of Berkshire after Buffett is not around because you can make a mistake in selecting a CEO. Buffett continued, "I think the odds of us making a mistake are very, very low. And certainly the candidate that I think is the leading candidate now; I would lay a lot of money on the fact that he is straight as an arrow. But mistakes can be made. You know, the Bible says the meek shall inherit the earth, but the question is, will they stay meek?"

Buffett thinks an independent chairman, particularly one that represents a very large block of stock and has no designs himself on taking over the place, is a safety measure for the possibility, however remote, that the wrong decision is made. But the directors at Berkshire will also be thinking every bit as much about the quality of the person as a human being as they will be thinking about their managerial skills because it's vital that you have somebody at Berkshire that is running the place that really cares more about Berkshire than he does about himself in terms of advancement. Buffett thinks Berkshire has multiple candidates that fulfill that role and the idea of an independent chairman is part of the company's belt and suspenders.

CIRCLE OF COMPETENCE

A shareholder asked if Buffett and Munger were to live another 50 years, what sector would they add to their investment circle of competence. Buffett joked that he liked the part about living another 50 years. He said he would choose a sector that is large, perhaps like the technology sector. However, he warned that while the technology sector is large, it is very hard to pick winners in the sector as the degree of disparity among technology companies is very dramatic. Charlie Munger said he would likely choose the energy or technology sectors. However, he said he and Buffett are the wrong people to develop expertise now in these sectors, summing it up by bluntly stating, “If we were going to do it, it would have already happened.”

LUBRIZOL’S COMPETITIVE MOAT

When David Sokol mentioned Lubrizol to Buffett as an investment idea, Buffett said it struck him as a business he didn't know anything about initially. He said he would never understand the chemistry of petroleum additives, but that's not necessarily vital. What is important is that he understands the economic dynamics of the industry. Is there a competitive moat? Is there ease of entry into the industry? Buffett suggested to Sokol that he contact Charlie with the idea since Charlie is a lot smarter about oil than Buffett felt he was. When Buffett talked to Charlie a few days later, Charlie said he didn’t understand the business either.

What Dave passed along to Buffett after having dinner with James Hambrick, Lubrizol’s CEO, and which Buffett later confirmed in a lunch with James Hambrick in February was a good understanding of industry dynamics and how the business had developed over time and what the role of oil companies was and would be in relation to a chemical additive. The oil companies are the biggest customers. They sell base oil to Lubrizol, but they are also Lubrizol’s biggest customers. The oil companies have gotten out of the business to quite a degree, although there are two of them left in it. So this industry has consolidated over time.

Every time Buffett looks at a business, he also looks at the ease of entry of competitors into the business. When Berkshire bought See's Candy in 1972, Buffett asked himself, “If I had a hundred million dollars, and I wanted to go in and take on See's Candy could I do it? And I came to the conclusion, ‘No,’ so we bought See's Candy. If the answer had been yes, we wouldn't have done it. I asked myself that same question, can I start a soft drink company and take on Coca-Cola if I have a hundred billion dollars. Richard Branson tried it some years ago in something called Virgin Cola. The brand is supposed to be a promise. I'm not sure that's the promise you want to get if you buy a soft drink, but in any event, I felt after my conversation with Dave subject to a second conversation with
James Hambrick, but covering the same ground, that it's not impossible at all for people to enter this business but in terms of the service and the relatively low cost of what Lubrizol brings to the party, and in terms of people trying to break into a market and take them on -- and it's not a huge market, it's probably only about a $10 billion market overall, I decided there's probably a good size moat on this.”

“They've got lots and lots of patents, but more than that they have a connection with customers. They work with customers when new engines come along to develop the right kind of additive. So I felt that I had an understanding --didn't understand one thing more about chemistry than when I started, but I felt I had an understanding of the economics of the business, the same way I felt when the Iscar people talked to me. I mean, who would think you can take some Tungsten out of the ground and shine it and put it in little carbide tools and that you could have some durable competitive advantage, but I decided Iscar had some durable competitive advantage after looking at it for a while. That's the conclusion I and Charlie reached--that the Lubrizol position is the dominant --or the No. 1 company, in terms of market share and that business is sustainable and that it's a very good business over time. They are helping engines run longer and run smoother. When metal is acting on metal, the lubricants are important, and they're always going to be around, and I think Lubrizol will be the leading company for a very, very long time. And that's the conclusion I came to. And I did not have a fix on that, nor did Charlie, prior to Dave relaying to me what he had learned at that dinner, which incidentally, Lubrizol had been telling the world. They made investor presentations and all that quite extensively over the years. I simply hadn't paid any real attention to it. And when it was explained to me, I thought I understood it, and I still think I understand it. I think Lubrizol will be a very, very good addition to Berkshire, and I saw James Hambrick just yesterday and despite the turmoil around this, they are very enthused about becoming part of Berkshire, that they regard it as the ideal home."

Charlie added, "Iscar and Lubrizol, to some extent, are sisters under the skin. You've got very small markets that aren't really too attractive to anybody with any sense to enter, so if you have any more like that why, please give Warren a call."

BERKSHIRE VALUATION

A shareholder said he uses information provided in Berkshire's annual report to estimate the company's value. He takes the investments per share ($95,000 at year end) and adds it to the operating earnings discounted at a 7% rate ($90,000) to come up with an estimated value for Berkshire of $185,000 per A share.

Buffett said he provides the investments per share and pre-tax operating earnings in the annual report because he thinks they are important figures. He added that Berkshire's operating earnings are almost certain to increase over time with the investments per share currently about the same as they were at year end. Buffett's goal is to build both numbers; however, his primary goal is to increase operating earnings. He added that Berkshire's intrinsic value should be considered a range of numbers as it is "ridiculous" to come up with one specific number. He noted that intrinsic value ranges will differ even between himself and Charlie.

He said investors have received once or twice signals from him when he believes Berkshire's stock is undervalued. For example, when he announced that he was willing to buy back Berkshire stock in 2000 that was a signal. It turned out to be a self-defeating signal as the stock moved up swiftly after he announced the buyback offer. On the other hand, most of Corporate America typically buys back stock at high prices rather than low prices. Currently, Buffett doesn't think Berkshire's stock is "overpriced." He noted that a very large international company may have wanted to do a deal with Berkshire. However, the deal was too big to do without Berkshire issuing stock. Buffett didn't do the deal because Berkshire's stock is not fully priced, and it would have been a disadvantage to Berkshire's current shareholders to have issued stock.

Charlie added that the shareholder was looking at the two right factors when determining Berkshire's value. He also said that Berkshire hasn't permanently lost the ability to do something interesting in terms of future deals

DEBT PROBLEMS

A shareholder asked Buffett how he could remain optimistic about the U.S. given the country's debt problems. Buffett repeated that he remains enthused about this country. Since 1776, America has enjoyed the most extraordinary economic period in the history of the world. Buffett was born in 1930. He joked that he might have stayed in the womb if someone had told him what was about to occur: a stock market crash with the Dow dropping from 381 to 42; 4,000 bank failures; 25% unemployment; the Dust Bowl and grasshoppers taking over the world. However, since 1930, the standard of living has increased sixfold in this country. We have a capitalistic system that works magnificently. Every once in awhile it gets gummed up, and we will always face problems.

Buffett recalled a talk he had with his future father-in-law, Doc Thompson, before he got married. Doc said, “Warren you are going to fail, but it won’t be your fault. The Democrats are going to take the country down the road to Communism.” In 1951, both Buffett’s father and Ben Graham warned Buffett about getting into stocks since stock prices were too high with the Dow trading over 200. Buffett said there are always negatives. This country in the past has faced a Civil War and 15 recessions, and there will always be a list of things on why this country can’t continue to prosper. However, the power of capitalism is incredible, and it will bring us out of future recessions as it has in the past. In the fall of 2008, we needed all the fiscal and monetary policy the government could provide. However, half of the recessions this country has faced occurred prior to 1900 before fiscal and monetary policies were established. The game is not over for the U.S. The rest of the world, like China, is catching up with the U.S. by tapping into our system. Over the next 100 years, we will certainly face another 15-20 lousy years, but we will still be far ahead of where we are now.

Charlie succinctly said, “The world is going to go on.” Buffett joked, “Now that is wildly optimistic for Charlie.”

BEST BUSINESS FOR INFLATIONARY ENVIRONMENT

A shareholder asked what type of business is the best for an inflationary environment. Is it companies like See’s Candy and Coca-Cola which earn high returns on tangible capital and have pricing power or companies with hard assets like utilities and railroads?

Buffett answered that the best inflation protection comes from one’s own earnings power. For example, a doctor’s services will always be in demand which will enable him or her to charge higher prices for their services.

The worst business in an inflationary environment is one that requires tons of receivables and inventories to operate the business. Normally, Buffett is not enthused by businesses which require high capital expenditures. A utility generates a bond-like return and has high capital expenditures so it won’t do as well during inflation just like bonds won’t do well in an inflationary environment.

The ideal business in an inflationary environment is a company like See’s Candy. Businesses with little capital investment needs and in a strong position to increase pricing with inflation do the best. When Berkshire first bought See’s, they were making 16 million pounds of candy and generating $25 million in volume. Today, the company’s sales top $300 million with only an incremental $30 million invested in the business since purchase. See’s now sells 75% more pounds of candy and generates more than 10 times the revenue it did when it was acquired. See’s has virtually no receivables and the inventories turn fast. The best businesses are those that are able to increase prices to offset inflation without incurring high capital expenditures.

Charlie added, “We didn’t always know this.” Buffett joked, “Sometimes we now forget this.” Charlie explained, “That is why continuous learning is important.” Buffett quipped, “I am a better investor, because I am a businessman, and a better businessman, because I am an investor.” Charlie noted that while their railroads and utilities are capital-intensive businesses, they are among the best in the world. It is not bad to be a world-class business. Buffett said that Berkshire’s $43 billion purchase of Burlington Northern Santa Fe included 22,000 miles of track, 6,000 locomotives and 13,000 bridges. The replacement value of Burlington during inflation will increase dramatically. The country will always need railroads, which is a terrific asset to own.

Buffett also mentioned a 1977 *Fortune* article he wrote, “How Inflation Swindles the Equity Investor,” which concluded with this quote from Buffett, “Stocks are probably still the best of all the poor alternatives in an era of inflation - at least they are if you buy in at appropriate prices."

DIVIDENDS

When asked if Berkshire would pay dividends, Buffett responded that Berkshire will pay a dividend once management has lost the ability to create shareholder value. As long as Berkshire is able to create more than $1 dollar of market value for every $1 they retain in the business, it makes sense for Berkshire to retain capital rather than pay it out in dividends. So far by leaving their money in Berkshire, which has retained $160 billion of shareholders’ equity, investors are better off since they could cash out for $200 billion (Berkshire’s current market capitalization). There will come a time when Berkshire can’t continue to create value. The day Berkshire declares a dividend, the stock price should go down as it will signal that Berkshire’s cash-compounding machine has come to an end.

Charlie added that if an investor wants a dividend, he sees no problem in selling a little Berkshire stock if the proceeds are used to buy jewelry at the right store.

WELLS FARGO AND U.S. BANCORP

In a response to the revenue outlook for Wells Fargo and U.S. Bancorp, two Berkshire holdings, Buffett said he consider Wells Fargo and U.S. Bancorp to both be among the best large banks in the country, if not the best. However, he acknowledged that for U.S. banking as a whole, profitability will be considerably less in the years ahead as leverage is reduced. It is a good thing for society but not for individual banks that know how to use leverage intelligently. He chuckled as he noted that, of course, all banks prior to the financial collapse thought they knew how to use leverage intelligently. Return on assets and return on equity will be less for banks going forward. However, he still thinks Wells Fargo and U.S. Bancorp have very good operations, just not as attractive as when their leverage was higher. Buffett thinks we have seen the worse of the banking crisis. He quoted Wells Fargo’s John Stumpf who said, "I don't know why the banks had to find new ways to lose money when the old ones were working so well.” Buffett said he likes his banking positions and added to the Wells Fargo position.

Charlie pointed out that Berkshire’s position in M&T Bank is headed by a sensible person, Bob Wilmers, and that it has been a wonderful investment. Buffett chimed in saying that he would recommend everyone read Wilmer’s letter to shareholders and that he also would recommend Jamie Dimon’s JP Morgan letter to shareholders for insights into the banking industry. Charlie agreed that M&T’s annual report was the best to come out of the banking industry.

GOLD

When Buffett was asked why he doesn’t invest in gold or other commodities, Buffett noted, “Gold and Berkshire A stock were once very close in price several decades ago. Gold has a way to go before catching up.” Buffett went on to explain that there are generally three categories of investments:

1) **Fixed-income investments such as bonds, cash, money market funds.**
   He then reached into his pocket to pull out his wallet, joking that we were watching an historic event, as he never likes to pull out his wallet. He held up a dollar bill and read the back which says “In God We Trust” which he says should better be stamped “In Government We Trust.” Any currency- related investment is a bet on how government will behave. If you had been in Zimbabwe, it might not have been such a good bet. However, almost all currencies have declined over time. As a class, currency-related investments don’t make much sense.

2) **Invest in items that don’t produce anything like gold.**
   Buffett repeated his comment on gold noting that, “If you take all of the gold in the world and put it into a cube, it would be about 67 feet on a side, and you could get a ladder and get up on top of it. You can fondle it, you can polish it, and you can stare at it. But it isn’t going to do anything. All you are doing when buying commodities, like gold, which are assets that cannot do anything, is hoping that someone else will pay you more for it down the road.” He recalled that at least when he bought silver, it had some industrial uses…joking that his investment timing was just 13 years off.

3) **Invest in assets based on what they can produce**, **such as farms or businesses**.
   This is the category of investments that appeals to Buffett and Munger. The success of the investment depends on whether it meets expectations and what the farm or business can deliver over time. In this type of investment, you don’t worry about getting a price quote every day. Instead you look at how the underlying business is performing.

While Buffett acknowledged that commodities have risen sharply recently and pointed out the doubling of cotton prices, much to the chagrin of Fruit of the Loom, he also noted that over time commodities have not been good investments. He added that he understands why rising prices can create excitement and draw in buyers, but it's not the way to create lasting wealth. He said he’d rather bet on strong businesses instead of something "that doesn't do anything."

Charlie Munger agrees:"There's something peculiar to buy an asset that will only really go up if the world goes to hell." He added that people who want to leave the country should own gold, while the rest of us will be better off owning Berkshire.

Buffett added that $100 billion of gold is being produced each year to add to that 67 foot cube. All the gold in the world is currently valued at $8 trillion. Instead you could own 1 billion acres of U.S. farmland valued at $2 trillion, ten ExxonMobils valued at $4 trillion and still stick $1-$2 trillion in your pocket as walking around money. Or Charlie grumbled, “You could have a 67 foot cube of gold that you would need to hire an army to protect.”

Buffett, concluded, "I've found the problem with investing in gold is that the only way you can make money is by having someone to pay a higher price than you. It pays no dividend or interest, so if sentiment moves - and it often does, and quickly - you're left holding the bag. Cotton, gold and silver haven't been good investments over the long term. So rather than speculating, a smarter and safer strategy to beat inflation would be to concentrate your efforts on investing in businesses that have little debt, the ability to increase prices, and a history of paying strong dividends."

ATTRACTING INVESTORS

When asked how to attract investors, Buffett joked the shareholder must be an aspiring hedge fund manager. He recounted how he started his investment business in 1956 by managing a few family and friend's accounts. He said he didn't like selling securities, and he didn't like people watching every investment decision he made. For six years, he operated his business out of his home. When Charlie came along, Buffett tried to hurry him into the investment business by telling him that law was OK as a hobby, but Charlie still joined the business slowly.

Charlie said it helps to attract investors if you conduct your life so other people trust you, and they have the right to trust you.

CONGLOMERATES

A shareholder asked Buffett to contrast Berkshire with the Go-Go conglomerates of the 1960's. Buffett acknowledged that Berkshire is a conglomerate, which permits the tax-efficient transfer of cash flows between Berkshire businesses, which is a significant plus. In the past, conglomerates were stock issuance machines. Basically, they were semi-Ponzi schemes. They would issue stock to acquire companies at lower multiples than their own. Buying companies for "free" became an unspoken conspiracy among the Go-Go conglomerates until it all collapsed. Teledyne was one conglomerate which compiled a wonderful record by issuing significant amounts of their stock when it was overpriced and then buying back significant amounts of their stock when it was underpriced. At Berkshire, Buffett is reluctant to issue stock. He does like to acquire good businesses that he can keep forever. In turn, these businesses throw off cash, which allows him to buy more good businesses.

Charlie added that in the past, the conglomerates took the view that they knew what numbers they were going to report, they just didn't know how they were going to do it.

LEGACY

When asked about legacies, and what he'd like to be known for in 100 years, Buffett quickly quipped: "Old age!" Munger adds that he thinks Buffett would want to be known as "the oldest corpse I've ever seen." This prompts Buffett to joke that Wilt Chamberlain's gravestone reads, "At last, I sleep alone."

On a more serious note, Buffett said he hopes he is remembered as a good teacher, noting that he had great teachers like his Dad, Ben Graham and Tom Murphy, former CEO of Capital Cities/ABC. Munger said he would like to be remembered for "A fortune fairly earned and wisely used."

WEAK U.S. DOLLAR

When asked about the depreciating U.S. dollar, Buffett said there is no question that the purchasing power of the dollar will decline as will most currencies. Last year, Berkshire shorted two currencies and made about $100 million doing so. He added that he is unlikely to make another big currency bet like he did a few years ago. To take advantage of a weaker dollar, Berkshire does own businesses like Coca-Cola with 80% of their earnings non-dollar earnings.

Buffett has worried about a rapid decline in the dollar, but also noted that since 1930 $1 is now worth $.06 due to a loss of purchasing power, and our country has still done well despite inflation. While Buffett hates inflation, he says the country has adapted pretty well to it.

Charlie added, "God knows where the world is headed, but it will muddle through." He pointed out that Greece's main industry is tourism. Even though Greece has a dysfunctional system, it has lasted a long time. "A great civilization has a great deal of ruin in it." Buffett chimed in that he thinks we will see a lot of inflation, but it still is better to be born in the U.S. today than at any other time.

BERKSHIRE VERSUS MUTUAL FUNDS

When asked if an investor should invest in Berkshire or mutual funds, Buffett said dollar-cost averaging into index funds over time is fine if one is not an active investor. However, Buffett said he would rather own Berkshire at the present time than index funds.

Charlie said he liked Berkshire much better than index funds, and he would be very unhappy if he had to own index funds. He advised investors to lower their expectations on stock market returns, although he acknowledged that Berkshire is a "pretty good investment." Buffett joked that Charlie's wife lowered her expectations when she married Charlie and he lived up to them.

BERKSHIRE'S COMPLIANCE REGULATIONS

(See transcript on Berkshire website.)

SLUGGISH U.S. ECONOMY VERSUS FOREIGN ECONOMIES

When asked about the sluggish U.S. economy versus foreign economies, Buffett said the U.S. government had their foot to the floor on monetary and fiscal policy. He joked that when Ben Bernanke was asked to define what an extended period would be for low interest rates, he said an extended period. Buffett said the problem is that we are taking in 15% of GDP in tax receipts and spending 25% of GDP. However, the natural resuscitative policies of capitalism will be what gets the economy going.

When the real estate market comes back after working off the crazy excess oversupply, we will see a big improvement in employment. It won't be just a pickup in construction jobs, but also indirect jobs like workers at Shaw Carpets (which now has thousands fewer workers) and workers at furniture marts. Buffett thinks the real estate market will be coming back perhaps by the end of this year as households are now forming faster than the number of new homes.

The pace of the recovery is picking up and has come back quite a bit since the recession. This can be seen in the weekly number of railroad car loadings which peaked at 219,000, dropped to 151,000 during the depths of the recession and currently are running at about 190,000. Certain Berkshire companies are setting records, including TTI, a distributor of electronic components, and Iscar, which provides tools for basic industry.

Charlie added that we are not learning enough from the wretched excesses of the financial industry. All financial collapses are due to asinine and greedy behavior. We need to use an ax on the financial industry. Our tax system should discourage trading. Securities should trade with the frequency of real estate rather than on algorithms with one computer system front-running another computer system. Charlie hates the idea that 25% of the best minds in this country are going into finance. “The lack of contrition in the finance industry makes Dave Sokol look like a hero.” Charlie stormily concluded with a discussion of the problems with our tax code, “A hedge-fund operator having a lower tax rate than taxi cab driver is demented!”

TEN YEAR BET

Prior to the lunch break, Buffett put up a chart which showed that he is still on the losing end of his 10 year bet with hedge funds that S&P 500 index funds could beat five selected hedge fund in performance. This is a $1 million bet with the proceeds going to charity. Since 2008, the S&P 500 is down 8.18% while the Hedge funds are down 4.24%, although the index funds are gaining ground.

Year	S&P	Hedge Funds
2008	-36.97%	-23.9%
2009	26.62	15.92
2010	15.08	8.46

RON OLSON COMMENTS

After lunch, Ron Olson, director and attorney for Berkshire, made some clarifying remarks regarding the Sokol trades. See the transcript on Berkshire’s website.

BYD

A shareholder asked if BYD, the Chinese battery and auto company, was still attractive given recent product delays. Buffett turned over the question to Charlie, whom he called the expert on BYD. Charlie said BYD’s price was higher than when Berkshire purchased its 10% stake in the company, so the company is not as attractive on a valuation basis today. Any company moving as fast as BYD will have delays and glitches. BYD tried to double their sales every year, and it worked for the first five years. Grinning from ear to ear, Buffett said, “I have nothing to add.”

COMMODITIES

When asked about trading oil, Buffett said in the 1990’s he took a position in oil at $10 a barrel. With oil, we are dealing with a finite resource. In exploring new frontiers for oil, we have stuck a lot of straws in the earth. Some day, oil will sell for a lot more than it does today. We have 500,000 producing oil wells in the U.S. Traditionally, Burlington Northern Santa Fe has hedged a certain amount of their oil needs. Buffett suggested that they didn’t need the hedges. If they know where oil prices are going, they don’t need to bother with running a railroad. They could just open a hedge fund. Buffett concluded by saying that an intelligent person can make more money over time on investing in productive businesses than on speculating on commodities. He added he has no edge on commodities.

Charlie simply added, “We like to keep life easy.”

LESSONS FROM THE LAST YEAR

When asked what they had learned in the last year, Charlie said he had read the book, "In The Plex: How Google Thinks, Works, and Shapes Our Lives." He found the book very interesting and likes engineering cultures. He said he doubted he would make any use of the book, but he enjoyed learning about Google. He stated, "We are here to go to bed wiser."

Buffett joked that he learned that he will have Charlie write the company's next press release. Charlie responded, "I approved that damn press release without any objection. Shareholders are going to be in terrible trouble if they expect me to correct your errors."

TOO BIG TO FAIL

When asked if taxpayers will still have to bail out a company too big to fail, Buffett said there are institutions around the world that the government would still need to bail out if they failed. In Europe, there are countries too big too fail.

Freddie Mac and Fannie Mae still haven't paid back their government loans. He said Freddie Mac and Fannie Mae are "too big to figure out."

However, Buffett said "hats off" to Chrysler for paying back its loans. He said he was skeptical of the government giving loans to the auto companies, but the government made the right decision to save the auto companies.

Buffett said incentive practices should be put in place so the propensity is for companies not to become too big to fail. If a company needs to be bailed out, the CEO and his spouse should be left dead broke. The Board of Directors should be forced to give back five years of their fees. We should also reduce the leverage in the financial system, otherwise in 10 years we will once again have too big to fail institutions.

Charlie said past panics and depressions always started on Wall Street due to great waves of speculation and bad behavior. This last mess should have caused something like the 1930's when new regulations were put into place to prevent future problems. Charlie said he confidently expects a new mess or two in the future and thinks it "is really stupid for a country to allow this." He said the finance and economics fields tend to attract people who should have gone into snake charming.

THE WASHINGTON POST AND COSTCO

Buffett was asked about his resignation from The Washington Post's board of directors and whether that meant he might sell some of his Post shares.

He said he will not sell any of The Washington Post stock he owns and that he is just a phone call away from Don Graham, if he ever wants any advice. At age 80, Buffett said he preferred to spend more time on Berkshire than traveling for board meetings. He added that his enthusiasm for The Washington Post and its management is the same as always, and that he is now available to the Post a lot cheaper than before.

Charlie, who sits on Costco's board of directors, says he admires Costco so that is why he is staying on their board, but added that "serving on a bunch of boards is for the birds."

Charlie said that Costco is the best in the world in its category with extremely ethical people. Costco takes all their cost advantages and pass them on to their customers. This has created ferocious customer loyalty. Costco has one store in Korea that is generating $400 million in revenue. Costco has the right management, personnel, ethics and diligence, which is quite rare to find. It is more normal to find businesses like GM, which once was the most successful business, and then later wiped out their shareholders. It would be good for business schools to teach the history of GM to students so they could learn how heavily unionized businesses and tough competitors can wipe out a business. However, no business school is yearning for graphs on the history of businesses. Harvard once taught that way, but quit when it trampled on other disciplines being taught. IBM would also make an interesting case study.

After Charlie's Costco discussion, Buffett joked that he and Charlie were recently on a plane which was hijacked. The hijackers gave each of them one last request before they said they would shoot them. Charlie said, "Let me give my speech on the virtues of Costco once again complete with illustrations and graphs." The hijackers then turned to Buffett to find out what his last request was, and Buffett said, "Just shoot me first."

INVESTING IN BERKSHIRE FROM AUSTRALIA

A shareholder from Australia wanted to know if Buffett thought that the value in Berkshire's stock could offset currency losses. Buffett said that part of his $100 million currency gain last year came from the Australia dollar, but he said he couldn't tell the shareholder what the relative change in the Aussie dollar to the U.S. dollar will be over their investment time horizon. He said every day at Berkshire they focus on increasing the intrinsic value and the earnings power of Berkshire. He said their interests are 100% aligned with shareholder interests. He also cautioned that they can't do remotely as well as in the past given the larger size of Berkshire's assets.

Charlie added that Australia has fabulous mines which are benefiting from Asia's boom. He said that Berkshire will do well compared to other U.S. companies.

ACQUIRING COMPANIES VERSUS INVESTING IN EQUITIES

When asked whether he will spend more time focusing on large acquisitions than on investing in equities, Buffett said he prefers large acquisitions. However, he spends more time on the equity portfolio since large acquisitions only occasionally come along. He said he hopes to get lucky in adding significant companies to Berkshire through more acquisitions. Many of the existing companies at Berkshire do bolt-on acquisitions. Most of these companies will earn materially more money in 5-10 years

Charlie added that Berkshire will always have a fair amount of marketable securities because of the insurance business, but said Berkshire will do less well with its larger asset base. Buffett said Berkshire now needs to put billions of dollars to work, and it is impossible to have a big edge, but he continues to think Berkshire will have a small edge. Charlie said it more fun to have people call looking for a permanent partner via an acquisition than it is shuffling little bits of paper around through equity investing.

VALUING THE INSURANCE BUSINESS

When Buffett was asked if he is too conservative on valuing Berkshire's insurance business by not including any underwriting profit, he said it is conservative to assume break even underwriting results for the insurance business. However, every few years, there will be an underwriting loss like this year may have. He acknowledged that it might not be inappropriate to include some normalized underwriting profit to the $17 billion normalized pre-tax earnings.

Charlie said he wouldn't trade any other insurance company for Berkshire's insurance companies.

Buffett agreed and said GEICO has a marvelous business; Ajit Jain has built a business from scratch which is capable of providing huge amount of insurance; Tad Montross has a terrific operation at Gen Re; and all of Berkshire's smaller insurance businesses are also first class.

Charlie warned that the property and casualty insurance industry has the "temptation to be stupid" like the banking industry.

STOCK SPLIT FOR THE A SHARES

When asked if Berkshire would consider splitting the A shares, Buffett said they already split the B shares, and there was no disadvantage to owning the B shares except voting rights. He said don't count on Berkshire splitting the A shares.

Charlie grumbled, "May you live until the A shares split."

AJIT JAIN AS POSSIBLE SUCCESSOR

When asked if Ajit Jain might be the possible successor for Buffet, Buffett said Ajit Jain is not a publicity hound. Buffett said he can't think of any decision Ajit made that Buffett could have made better. He said Ajit is as rational a thinker as Charlie Munger is. Ajit loves what he does and is very creative. Ajit moved Berkshire into new reinsurance areas. Ajit's mind works like a machine day after day. Buffett said his best deal ever was hiring Ajit.

Charlie said that the secret of success in a field is finding something which you are very interested in like Ajit found in insurance. He said every Thanksgiving, Ajit flies to London because they don't have a Thanksgiving holiday, and he can continue to work. Buffett joked, "We do give him Christmas off."

Buffett said they are not exaggerating on how valuable Ajit is to Berkshire. Ajit could monetize himself for $100's of millions of dollars by going to work elsewhere. He is smart and always thinks for himself. He is a remarkable human being. He always thanks Buffett for his bonus, even though Buffett feels he has left off a zero on the amount when he writes the check. Buffett concluded that we are very lucky that Ajit has fun at Berkshire.

WORST BUSINESS AT BERKSHIRE

When asked what the worst business at Berkshire is, Buffett said it would be smaller businesses without the potential to get big. He said retailing businesses, like Dexter, might be the worst.

Despite the success of the Nebraska Furniture Mart, the retailing businesses at Berkshire haven't created lots of earnings power for the company. Charlie agreed that retailers haven't been Berkshire's best businesses.

GOODWILL AND RETUN ON TANGIBLE CAPITAL

Buffett said that the goodwill Berkshire pays for a business should not be judged as to how attractive the business is. Instead one should look at the return on the tangible capital the business earns. In terms of judging how Berkshire deploys capital, one does need to look at goodwill, since that is what Berkshire paid. Amortization of goodwill makes no sense, but write-offs of goodwill make sense when appropriate.

For example, Buffett said that Berkshire is paying $9 billion for Lubrizol which is earning $1 billion in pre-tax earnings, so that is what investors should judge Berkshire on in terms of capital deployment. However, Lubrizol's business should be judged on the $1 billion it is earning pre-tax on $2.5 billion of its equity. One can buy a good business, but if you pay too high a price for the business, it may not be a good investment.

Charlie added that it is difficult to find decent operating businesses selling for low prices, but if you can earn $6 billion in earnings on $60 billion of float that is not all bad.

RAISING CHILDREN

Answering a question on raising children, Buffett said that if you are rich, bringing up kids to think they have privileges is a big mistake. He said Charlie raised 8 kids with good results. However, if one raises kids to think that they will have others wait on them, you won't get good results. Buffett didn't want to give his own kids an idea that they were rich when they were growing up.

Charlie added that when you are wealthy, it is difficult to raise children to think that they will have to dig ditches in the hot sun for 60 hours a week. He muttered, "Just lose your fight as gracefully as you can. If you were a proctologist, you might also not like your day."

SUCCESSOR

Buffett said the next Berkshire CEO will make a lot of money. His base salary will likely be supplemented with an option system with the option strike price set to what the business is worth at the time. Berkshire's present compensation system won't be a factor for the successor. It is important to get the right person with the right values who can interact with the other managers and knows how to allocate capital. There are several managers at Berkshire who already make eight figures, and they earn it.

Charlie added that he hopes it will be a long time in the future before the successor question arises, but that Buffett's spot will be occupied by the right person who doesn't grab all they can.

RENEWABLE ENERGY AND CLEAN WATER

In response to a question on renewable energy, Buffett said it was an important subject but not one that impacts his investment strategy. He looks at earnings streams 5-10 years down the road when making his investment decisions. There are a number of societal issues that don't impact his investment decisions, such as clean water.

Charlie said that if we have enough energy, we will have enough clean water, noting that Israel gets half of their water from seawater. Charlie is a great believer in conserving carbons. He said those who think "Drill, drill, drill" is the answer are "all nuts."

EASY LUBRIZOL QUESTION

When asked if Lubrizol's board breached its fiduciary duty to its shareholders by not running an auction of the company, Charlie responded, "No, the board of directors did not breach their fiduciary duty because we don't participate in auctions." Buffett added, "They got a very certain deal, and they got a very significant price in my view. If they said, 'we want to conduct an auction,' we'd say good luck and would have moved onto something else." Charlie snorted, "Anybody else have an easy question?"

CAPITAL ALLOCATION

In judging Berkshire's capital allocation skills, Buffett said the real test is whether Berkshire's earnings progress at a rate higher than the capital retained. Does Berkshire's market value increase at a rate greater than retained earnings? Buffett said, "If we keep shareholder money, we need to earn a better than average return on that money, which we so far have done."

Charlie added that Berkshire keeps beating the market. It won't be at the rate as in the past, but Berkshire should continue to do so.

HIGH YIELD INVESTMENTS

A shareholder asked why Buffett had negotiated different yields on a variety of high-yield investments. With the Goldman Sachs and GE investments, Berkshire received 10% yields plus warrants, while the Swiss Re deal earned a 12% yield.

Buffett explained that every deal was done at a different time and under different market conditions. As a result, opportunity costs were different. He said Berkshire could have done better if they had struck their deal with Goldman and GE five months later. He bluntly said, "I was early." He said the Swiss Re deal didn't compare to the Dow deal done one and a half years earlier. He had to consider what was available at the time. He said past deals don't make any difference when negotiating new deals. He said it is a big mistake to compare a current deal with the best deal ever made. The goal is not to do the best deal ever, but to do the best deal available at the time.

Charlie agreed that you make different deals based on opportunity costs at the time.

SPEED READING

When asked what advice he would give children on taking speed reading classes, Buffett said he reads five newspapers a day along with 10-K's and 10-Q's, but he said he is not a fast reader. He said he is not sure how effective speed reading is but thought it would be a huge advantage to read fast. Buffett added that there is nothing more pleasurable than reading and that perhaps learning speed reading when he was younger would have been helpful. Buffett then retells an old Woody Allen joke about speed-reading. When Allen tells someone he read “War and Peace” in about 20 minutes, the person is stunned. “What’s it about?” the other person asks. “Russia,” Allen responds.

Charlie grunted, “Speed is overestimated. What the hell difference does it make how fast one can read?”

DEBT CEILING

When asked what would happen if Congress doesn’t raise the debt ceiling, Buffett said, “It will be the most asinine act Congress ever did.” He then recounted the story about how Indiana once passed a law to change the mathematical function, Pi, to three figures so it would be easier for kids to learn. Buffett said the only thing stupider than that would be for Congress not to raise the debt ceiling. He explained that even having a debt ceiling is a mistake as the economy of 1911 is different than the economy of 2011. It is a waste of time debating the debt ceiling, as a growing country has a growing debt capacity. He went on to say that Congress will raise the debt ceiling. The U.S. will not have a debt crisis as long as they issue notes in their own currency. Instead of worrying about a debt crisis, the real worry should be about the printing press and inflation. Japan has high debt/GDP with no debt crisis due to issuing their notes in their own currency. On the other hand, European countries may face a debt crisis, since they are forced to pay in a currency they don’t control.

Charlie said that with regard to the debate over the debt ceiling, “Both parties are competing to see who can be the most stupid! And they keep trumping one another.”

MIDAMERICAN’S NUCLEAR LIABILITY

When asked if MidAmerican’s bond-like return is worth the risk of a potential mega-catastrophe from its nuclear operations, Buffett said that nuclear power is an important part of dealing with the energy problem. France receives a high percentage of their power from nuclear operations. Currently, 20% of U.S. electric power comes from nuclear power. Buffett thinks it is safe, however, he doesn’t think new nuclear operations will go anywhere fast given what happened in Japan.

Charlie said that you can’t be so risk-averse that something which is remotely possible prevents useful solutions. You need a reasonable amount of courage in running companies. Buffett added that toxic waste is carried on railroads, but that he doesn’t think Berkshire has any risk that would threaten Berkshire whether it be leverage, derivatives or nuclear power plants. Charlie agreed saying that new nuclear plants are much safer than the old ones, while Buffett chimed in that more people have lost their lives in coal mines than from nuclear power. Charlie concluded by wryly stating, “If a tsunami gets to Iowa, it will be a hell of a tsunami.”

REINSTATING CHARITALBE CONTRIBUTION PROGRAM

When asked if Berkshire would reinstate its charitable contribution program, Buffett said that shareholders loved that program for 20 years. He said it was a tax-efficient way to let shareholders give away money to charity. Nobody in Corporate America copied Berkshire’s plan, as CEO’s prefer to direct company charitable contributions instead of allowing shareholders to do so. While Berkshire always had a backlash on where some of their charitable contributions were directed, Berkshire ended the program when a campaign developed to boycott Pampered Chef's representatives. This program was hurting a lot of innocent people and threatening their livelihood, so Berkshire reluctantly stopped the charitable program.

Charlie added that he didn't want Berkshire, through its charitable program, to always have to deal with various social issues of the time. He said that a lot of Berkshire stock is given away to charity every year.

ESTIMATING GROWTH OF LONG-TERM CASH FLOWS

When asked how to estimate long-term cash flows, Buffett said growth is part of the investment equation, but one should focus on profitable growth. He spoke of Coca-Cola growing for the past 125 years and now being in 200 countries. Buffett said he likes to see high returns on incremental capital, but that he doesn't rule out low-growth companies if they can be acquired at a reasonable price.

Charlie said business schools teach students to make projections well into the future, but growth projections do more harm than good. "There is enormous false precision when making long-term projections."

Buffett recounted the story of when they acquired Scott Fetzer. Even though they struck the deal on their own, Fetzer's broker received a $2 million fee. The broker, feeling a bit guilty, offered to provide them with the book he prepared on all of his growth projections for Fetzer. Charlie retorted, "I'll pay you $2 million if you don't show me the book!" Buffett chimed in that he never saw projections from an investment banker that didn't show everything going up. He warned, "Don't ask the barber if you need a haircut."

13-F

When asked if a shareholder could determine what securities Buffett personally owned from reviewing the company's 13-F, Buffett turned over the question to Berkshire's CFO, who does the SEC filing. He explained that the securities which have Buffett's name by them are for Berkshire's profit-sharing plans which Buffett manages. Buffett added that he personally owns very few securities. Most of his personal money is in government bonds, which he said are not good investments right now. However, he focuses his attention on investing Berkshire's investments not his own.

CHINA

Buffett said he will invest in foreign companies such as those in China, however, he acknowledged that he knows less about their tax laws, customs and government policies than he does about domestic companies. He said he did buy PetroChina a few years ago because it appeared extraordinarily cheap, so the uncertainty was already built into the valuation. Besides, PetroChina's annual report disclosed that the company would pay out 45% of their earnings in dividends, which they did. Buffett said he is more comfortable investing in China than in Russia.

Charlie added that Buffett loves to look at new companies in different parts of the world. He said there is one private company in China that is making $3 billion after taxes that they looked at. However, one has to be careful in evaluating things not seen before. Charlie told a joke about a professor going out West one summer. He came back and told his students that Indians always walk in single file. When asked how the professor knew that, he said, “Because I saw one Indian while I was there, and he did.”

CASH

When a shareholder asked Buffett where he holds Berkshire’s massive $38 billion cash stash, he said all the choices for short-term money are currently lousy. Berkshire does not own any commercial paper or money market funds. Basically, all Berkshire’s cash is in U.S. Treasuries. Berkshire is getting paid virtually nothing on the cash which is irritating. However, it serves as a parking place, and Buffett knows he will get his money back. In Sept. 2008, he was able to complete the $6.5 billion Wrigley deal which had been previously negotiated because Berkshire had the money liquid.

Charlie said he has seen people struggle to get 10 basis points more on short-term money. However, cash allows one to do opportunistic deals. He recounted how Berkshire was able to acquire a pipeline over a weekend because they had the ready cash available.

Buffett added that the ability to come up with cash easily when the rest of the world is petrified allows Berkshire to do good deals. For example, he joked, if Bernanke were to run off to South America with Paris Hilton, Berkshire would still be able to get deals done.

WESCO MEETINGS

In response to a question about Wesco shareholder meetings which will no longer occur after the remaining shares of Wesco are acquired by Berkshire, Charlie said he plans to hold annual “Afternoon Meetings with Charlie” which are only for hard-core addicts.

WIND POWER

In response to a question on wind power, Buffett said wind power was terrific but only when the wind blows, which it does about 35% of the time in Iowa where MidAmerican has its wind power operations. However, you can’t count on wind power for your base load of power. Wind power economics only make sense right now if companies receive a government subsidy in the form of tax credits. The central part of the country is the best for wind power, and Berkshire is number one in providing wind power. Since Berkshire pays a lot of taxes (20% of all corporate taxes in the U.S), the tax credits it receives on its wind power projects are valuable so Berkshire will continue to build wind power operations in Iowa. The wind power Berkshire generates also has helped keep Iowa’s electric rates unchanged for a decade.

NETJETS

When a shareholder asked if NetJets was destined for bankruptcy absent Berkshire’s support, Buffett said Berkshire never had an intent to bankrupt the company. However, Buffett did acknowledge that NetJets would have gone bankrupt if it had been an independent company. Buffett said in the past they had two insurance companies that would have gone bankrupt but Berkshire agreed to make them whole.

HIGH YOUTH UNEMPLOYMENT

Given high youth unemployment, a shareholder asked what advice Buffett would give youths about starting their own businesses. Buffett recommended that they take a Dale Carnegie course as communication skills are the most important skill to improve. If they are lucky, they will find what they are passionate about and start a career in that area.

Charlie added that economics is a tough subject, and he wouldn't urge students to hurry into economics. He would suggest students master the easy stuff first.

REINSURANCE

When asked about whether Berkshire should limit the reinsurance it agreed to take on for Swiss Re, Buffett said he wouldn't change the direct risk Berkshire is willing to bear in reinsurance. Currently, Berkshire is well below their capacity for reinsurance and would love to add more reinsurance to the books but only at attractive rates. . With normalized earnings power of $17 billion, Berkshire is unlike any other insurance company in the world. The insurance industry just went through the worst quarter since Katrina. Buffett added that Berkshire didn't succeed in the reinsurance business in their first 15 years in the business, not until Ajit Jain came along.

Charlie added that the reinsurance business looks easier than it is. The industry needs to factor in worst-case events. The investment bankers who sell reinsurance products are the same ones that sold derivative products that blew up.

TODD COMBS

When asked how Berkshire came to hire Todd Combs as an investment manager, Charlie said it was "very complicated." Todd sent Charlie a letter, and Charlie agreed to have a meal with him. Charlie said Todd has been thinking about financial stocks for a long time, which will be useful for Berkshire. Buffett added that Todd's results over five years were good. He also noted that Berkshire will likely have more than one investment manager over time.

JOHNSON & JOHNSON

When asked what Buffett thought about Johnson & Johnson (one of Berkshire's investments) using stock to acquire Synthes, Buffett said he hadn't talked to anyone at JNJ about the deal, but he would have liked the deal better if it was done using all cash. When a company trades away its existing business for another business, one would draw the inference that the company is not valuing its own business as you might think they should.

Charlie reminded Buffett that he knows more about chocolate and pizza (Kraft's deal that Buffett criticized) than he does about medical devices.

ACQUISITION APPETITE

With cash potentially reaching $60 billion by year end, Buffett was asked about his acquisition appetite. Buffett said his acquisition appetite is always there. However, he won't borrow a lot of money to do an acquisition, and he won't issue many Berkshire shares. He also won't sell an existing business to buy another business. Cash will build over time, and Buffett is willing to sell portfolio securities to fund an acquisition. He said he is looking at a couple of deals right now in the $9 billion range, but they are still just a gleam in his eye. He said Berkshire can't really do a big elephant deal right now given that he just committed $9 billion to do the Lubrizol deal. Berkshire has never really taken a risk in deals because it doesn't need to.

Charlie added that Berkshire is very reluctant to issue shares. In fact, he said Berkshire hates to issue shares as they would be divesting parts of a wonderful business they already own.

RESIDENTIAL REAL ESTATE MARKET

When asked about the residential real estate market, Buffett said the immediate real estate market situation is terrible. He sees it at Berkshire's real estate related businesses like Shaw, Mitek, Johns Manville, and Acme Brick. There has been no bounce at all in those businesses. But that hasn't stopped Berkshire from investing further in the real estate business, noting that they recently bought the largest brick company in Alabama. We will once again build houses which will equal future household growth. Over the long term, Berkshire will make significant money when we get a normalized housing market. While there is still no movement in the real estate industry, Buffett expects things to improve by year end or next year.

Charlie added that real estate is a very cyclical business, noting there is no one else right now bidding on brick companies in Alabama. Many people don't like cyclical businesses, but at Berkshire they don't mind lumpy business results as long as they are good businesses.

Buffett added that See's Candy loses money eight months out of the year, but Berkshire never worries that Christmas won't come. With cyclical businesses, Berkshire looks at the business over the next 20 years. They recognize over that period there will be 3-4 bad years. If they can buy the cyclical business cheap enough, they will do OK over time.