

Investment Insight

BUFFETT'S BERKSHIRE IS ANYTHING BUT BRITTLE

Warren Buffett recently returned to the stage in Omaha for the Berkshire Hathaway annual meeting after a two-year hiatus. Christopher Rossbach, our chief investment officer, who has been making the yearly pilgrimage since 2014 was one of the thousands to attend. He found the legendary investor in great form and emerged with several key takeaways.

It was great to be back in Omaha, Nebraska for the first in-person Berkshire Hathaway annual meeting since 2019. I had wondered: Would it be the same and would the crowds return?

After all, every year, the Woodstock of Capitalism is attended by tens of thousands of people from all over the world. They come to hear from Warren Buffett and Charlie Munger, who have built Berkshire Hathaway into one of the most valuable companies in the world. The Stern family has been invested in Berkshire Hathaway for decades. It is an annual trip I have taken until the pandemic stopped it two years ago and it is the only 'industry convention' I attend.



Source: See's Candies



Christopher Rossbach

It is a spectacularly unique event. Nobody gets a reserved seat. The person next to you in line at 5 o'clock in the morning can be a retired teacher who has invested in Berkshire all their life, a well-known fund manager, or the CEO of a major business. Many are long-term investors like me who come to meet like-minded people from all over the world and participate in the many investment conferences and side-line discussions.

It is also the only shareholder meeting that pays for itself because shareholders get nothing for free. The shareholder's pass on a lanyard entitles you to discounts to buy products from the many companies Berkshire owns, whether it be Brooks shoes, Fruit of the Loom t-shirts, See's Candies or Geico car insurance. Buffett and Munger munch their way through a box of See's Peanut Brittle as they sit on stage answering questions for hours, so it must be good for your investments.

1. Berkshire Hathaway and its businesses continue to thrive

The crowds did indeed return. Some 40,000 people came this year and the auditorium was packed. Buffett at 91 and Charlie Munger at 98 were in great form. Berkshire, its companies and its business model are thriving. Much of this success is because Buffett and Munger keep on adapting what they do to the opportunities and circumstances they encounter while staying true to their principles of long-term, fundamental investing.

They do it at their own pace and admit that they have missed opportunities because they still have lots of businesses in their box labelled ‘too hard’. But Berkshire has generated huge value for shareholders by continually generating cash to reinvest and by buying big positions in stocks or even entire businesses like Allegheny, the insurance company it bought earlier this year in a USD \$12 billion deal.



That transaction was part of the USD \$51 billion of Berkshire's cash pile that Buffett has deployed so far this year. He has been using the recent fall back in stocks to buy and it is striking that Buffett has put so much money to work this year given that he hesitated in March 2020 at the height of the uncertainty about the pandemic. He and his Berkshire colleagues

Ted Wechsler and Todd Combs recognise the opportunities for long-term value thrown up by the current market turmoil.

Other investments so far this year have included lifting their stake in oil producer Occidental Petroleum to over 15%, and as he told the annual meeting, a personal decision to increase Berkshire's position in gaming company Activision Blizzard after the Microsoft deal to 9.5% or more. It is remarkable that at his age, Buffett cannot resist a risk arbitrage play, telling shareholders that “occasionally I'll see an arbitrage deal and do it”.

2. Berkshire is buying

It is just as striking how little discussion there was during the annual meeting about macroeconomics. Charlie Munger has famously said that “micro is what we do, macro is what we put up with”. Buffett made a couple of comments about inflation but the closest he came to saying what to do about it was when a young person in the audience asked a broad question about how to find opportunities in the current environment. The response was that “companies will be fine if they are the best at what they do.”

Buffett does not time markets. He bases his decisions on fundamentals and value. Talking to some of the Berkshire managers in the huge exhibition hall reminded me that he does not need economists or investment analysts to tell him what is going on. He knows the strength of the US economy because he can see how well the businesses which Berkshire owns are actually doing and if he has a question, he can ask one of his managers.

Buffett's decision to deploy significant amounts of capital in March, despite the challenges, is based on what he sees. It is not just a significant vote of confidence in the prospects for Berkshire Hathaway and its businesses, but also the strength and resilience of the US economy, and its markets. And he remains sanguine about inflation telling the shareholders that “inflation swindles the bond investor, too. It swindles the person who keeps their cash under the mattress. It swindles almost everybody.”

It certainly reaffirmed the long-held view we have that investment decisions should be formed from the bottom up. You should look at what companies are doing, why they do it well, what opportunities they have and how much value they can create over the long-term. You should not worry or be swayed by macroeconomic conditions and short-term market concerns.

Buffett's confidence to keep investing in the best companies is similar to our view that in an inflationary environment quality companies have the ability to grow because of the markets they are operating in or through strategic competitive advantages built over time. If a company can show that it has the pricing power to offset inflation and the resources and innovation to grow volumes, it will be well-positioned for what comes next. The fact that government bonds have had their worst year for two decades highlights the danger of being invested in anything other than equities at this juncture.

3. Berkshire's succession plans reassure

The succession at Berkshire is fully underway. Berkshire is a conglomerate that employs 370,000 people. Its business and culture allow it to allocate capital which its companies generate flexibly and opportunistically. Buffett has said many times that Berkshire is much bigger than Charlie and himself, and that the culture they have imbued will prevail because it is strong and ingrained in the managers of the business.

The changes to the management over the past couple of years, as well as the board changes last year, showed us the shape of what Berkshire will look like when Buffett leaves.

Asked by a shareholder, he hinted that his successor as CEO, Greg Abel, currently vice-chair of Berkshire's non-insurance business and chair of Berkshire Energy Holdings, the business he has led since 2000, will face "more restrictions" on the approval process than he currently does and that there would be a greater need for governance and approvals.

There is a lot of evidence that Buffett is not just saying all of this. Weston M. Hicks, the CEO of Allegheny since 2004, did not agree to sell his company to Berkshire with the expectation that Buffett will be around forever to guarantee Allegheny's independence.

It provides reassurance that the people in charge of potential targets agree that Berkshire's approach to buying businesses and being a patient long-term owner is a business model that goes beyond Buffett and Munger.

At the annual meeting I got a real sense of how Buffett is preparing Berkshire for the inevitable succession. The board changes made last year, appointing Chris Davies, an experienced fund manager and third-generation Berkshire shareholder who is a generation younger than Buffett, Munger and several others on the board, as well as Susan Buffett, Warren's daughter, are not just about ensuring the continuity of the values and the legacy and but also about how to implement them without Buffett and Munger at the helm.

As I put it to **Eric Platt**, correspondent at the *Financial Times* for an article he wrote about the annual meeting, "they are putting the people and processes in place to ensure the governance works [and] that when the succession takes place Berkshire retains the nimbleness it needs to make the investments it does."

4. No substitute for a first hand perspective

In Omaha, it is not just from hearing Buffett and Munger first hand that you get a sense of perspective. Talking to many investors and business leaders at the meeting and fringe events, I was struck by the strength of the economic recovery and the demand for goods and services.

The pandemic, the Russia/Ukraine conflict and other issues have been highly disruptive but it was clear how much of what is going on is about bottlenecks and supply shortages. They are serious, but their impacts on the global economy and on companies will get resolved as companies adapt, supply increases and global supply chains are realigned.

China's travel restrictions prevented many thousands and Munger's biggest fans from attending. It was still great to see so many people back in Omaha coming together from all walks of life to share in the spirit of Berkshire and what it represents.

See you next year in Omaha!

Christopher Rossbach
May 2022

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