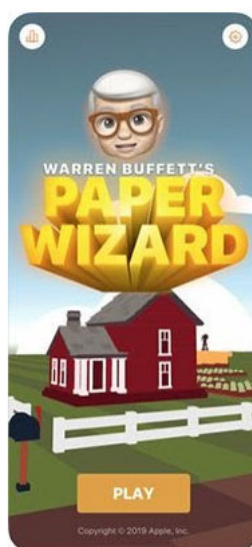


A "Berkshire, Hallelujah"



Reflections from the 2019 Annual Meeting

(BRK.A - \$314,750 - NYSE)
(BRK.B - \$209.29 - ")

Macrae Sykes
(914) 921-5398

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Sources: Omaha.com, wsj.com, economictimes.indiatimes.com, dealbreaker.com

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Berkshire Hathaway Inc. (BRK'A - \$314,750 - NYSE)

A "Berkshire, Hallelujah" - NR

<u>Year</u>	<u>B/V Per "A"</u>	<u>P/B</u>		
2021P	\$293,050	1.1x	Dividend: None	Current Return: Nil
2020P	266,140	1.2	Common Shares "A": 0.7 billion (a)	
2019E	240,900	1.3	" " "B": 1.4 " (b)	
2018A	212,503	1.5	52-Week Range "A" Shares: \$335,900 - \$279,410	

(a) One Class "A" Share can be converted into 1,500 "B" Shares. Class "A" Shares have 10,000 votes per share.

(b) Warren Buffett owns 270,644 of "A" Shares and 91,189 "B" Shares.

COMPANY OVERVIEW

Berkshire Hathaway Inc., based in Omaha, NE is a holding company for a diverse group of operating subsidiaries including insurance, freight rail transportation, utilities and energy, finance, services and retailing. The subsidiaries operate in an autonomous fashion, while investment and capital allocation decisions are managed by Warren Buffett (88) in consultation with Vice Chairman, Charlie Munger (95). As of December 31, 2018, since 1965, the firm had an annual compounded gain on book value of 18.7%.

On May 4, Berkshire Hathaway hosted its annual meeting in Omaha. The fifty-fourth event was attended by over tens of thousands of international investors and webcast to millions more. Feedback included insight on the firm's investments, operating businesses and many current issues including politics and management succession. The movie section included a short film of Warren's humorous trip to Cupertino to design a new app for the iPhone. Q&A began at 9:15am and concluded at 3:30pm with a break for lunch. Providing the multiple questions for the long session were three members of the press, three analysts and an assortment of investors and Berkshire enthusiasts including several young children. In short, the 2019 meeting reinforced the positive outlook for the company, while demonstrating the reach and scale of its unique brand among global communities.

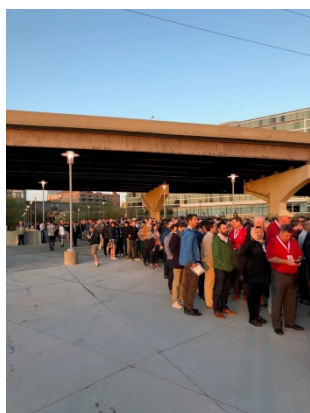
Takeaways:

- Value Investing - WB: "The people making the decision on Amazon are absolutely as much value investors as I was when I was looking around for all these things selling below working capital years ago. That has not changed." There are a lot of potential factors that go into determining an investment. Current sales, outlook for margins, tangible assets, and excess cash on the balance sheet are all a part of the calculation for buying company A vs. company B. WB: "The considerations are identical when you buy Amazon vs. a bank stock that looks cheap against book value or earnings of some sort. I don't second guess them (Todd and Ted)." CM: "Warren and I are a little older than some people and we are not that flexible. We screwed up not buying Google." WB: "We knew them when we were using them." CM: "We just sat there sucking our thumbs. Maybe Apple was atonement."
- Repurchases - During 1Q, the company repurchased \$1.7bn of shares (1,258 Class "A" Shares and ~6.5m Class "B" shares) and ultimately would like buy back a substantial amount of shares especially given the current \$100 billion+ of available cash. The duo reinforced its mission to repurchase shares when they trade a discount to intrinsic value vs. the previous guideline based on a premium to book value. Should the discount to intrinsic value reach 25-30%, the management team indicated they would buy back more pronounced levels of shares. CM: "I predict we will get a little more liberal with our repurchases."
- The insurance business – The current float is about \$124 billion, which is money that has to be paid back over time but is a good source of investing capital for the firm and will generate returns over time. WB: "We have the best property casualty business in the world." The business benefits from significant scale and no reliance on reinsurance. WB: "If you take the three largest re-insurers – all of them came close to extinction over the last thirty years. We really didn't have any worse case scenario except for Katrina." Additionally, Tony Nicely who has led GEICO has created more than \$50 billion of value with the business. CM: "It (insurance) is such an easy business. But you have to be good at it." Ajit Jain commented on underwriting unconventional risk contracts. Berkshire uses a scientific approach to get the data, and then applies a margin of safety to the agreement. "We have an absolute understanding of a worst case to cap our exposure." CM: "I don't think we help very much. Don't try this at home. This is not something you can learn."

- Politics and the outlook for socialism - WB: "I don't think the country will go into socialism in 2020 or 2040 or 2060." CM: "I think we're all in favor of some kind of government social safety net in a country as prosperous as ours. . .the vast stupidity with which parts of that social safety net are managed by the government."
- Wells Fargo - They are content with the conglomerate's position in the bank stock, but continue to be critical of former Wells Fargo management who delayed disclosing the irregularities a few years ago. WB: "Wells made some big mistakes. They incentivized the wrong behavior. When you find a problem you have to address it. With Salomon – John Gutfreund did not report it fast enough. He heard about a pyromaniac and he let him have the matches. With Wells they waited a couple of years to surface the problems." Unfortunately, shareholders have paid a price for moral hazard. The government got its money back, but the shareholders got punished by paying out billions of dollars. CM: "I don't think people should go to jail for honest errors. Losing your job is enough. WB: "Paul Moser (of Salomon) went to jail for 4 months. If you are breaking laws, you should be prosecuted. If you do dumb things you shouldn't go away so rich. If a bank gets to a way where the government controls it, the leadership should lose their net worth and their spouses net worth. The FDIC was started in 1934 – new deal proposal. It has not cost the US government a penny. There is a current balance of \$100 billion and is there from all the banks that have paid in. Some banks will make big mistakes in the future."
- Kraft-Heinz - WB: "We paid too much money for Kraft. To some extent our own actions drove up prices. \$6 billion of pretax on \$7 billion of tangible assets is a wonderful business. But you can pay too much for a profitable business. The profitability has been improved over the way they were operating before." Basically retailers have gained power relative to brands. Just look at Kirkland (Costco private label) which is now doing ~\$40 billion and is bigger than Coca Cola. You can turn any good business into a bad investment by paying too much. What you can't do is turn any investment into a good one by paying too little or how Warren first started investing.
- Culture as an Asset - WB: "We do think it is a huge corporate asset. Someone can call on a Saturday morning and meet on a Sunday and have a \$10 billion commitment that is as good as set in stone." Tod and Ted are helping build on that asset. Since arriving, they have expanded the universe for transactions for the firm.
- The firm's size at over \$500 billion of market capitalization will be "a drag on performance." The firm continues to "better situated than ever,It won't be the highest compounder by a long shot against many other businesses."
- Precision Cast Parts - Expect margins to improve over time. The business is making investments to serve aviation clients better, but progress has been below what was projected a few years ago. There is \$400 million of annual purchase amortization that impacts reporting results. WB: "My expectation is that earnings of Precision will improve fairly significantly."

Exhibit 1

Berkshire Hathaway Annual Meeting – May 4, 2019



Source: Macrae Sykes

PERFORMANCE

Berkshire Hathaway continues to be among the largest public capitalizations in the United States. Since taking over Berkshire Hathaway in 1965, Mr. Buffett has generated a cumulative return of book value of 1,091,899% vs. the

155,019% change in the S&P 500 (including dividends). We would note that Berkshire's performance is after-tax, while the S&P 500 return is pre-tax.

Table 1 **Berkshire Hathaway Performance**
1965-2018

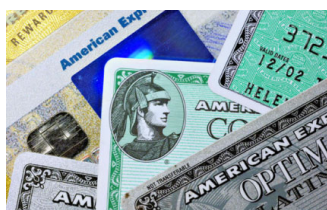
Year	Annual Percentage Change				Year	Annual Percentage Change			
	in Per-Share Book Value of Berkshire	in Per-Share Market Value of Berkshire	in S&P 500 with Dividends Included	Relative Results		in Per-Share Book Value of Berkshire	in Per-Share Market Value of Berkshire	in S&P 500 with Dividends Included	Relative Results
1965	23.8%	49.5%	10.0%	39.5%	1992	20.3	29.8	7.6	22.2
1966	20.3	(3.4)	(11.7)	8.3	1993	14.3	38.9	10.1	28.8
1967	11.0	13.3	30.9	(17.6)	1994	13.9	25.0	1.3	23.7
1968	19.0	77.8	11.0	66.8	1995	43.1	57.4	37.6	19.8
1969	16.2	19.4	(8.4)	27.8	1996	31.8	6.2	23.0	(16.8)
1970	12.0	(4.6)	3.9	(8.5)	1997	34.1	34.9	33.4	1.5
1971	16.4	80.5	14.6	65.9	1998	48.3	52.2	28.6	23.6
1972	21.7	8.1	18.9	(10.8)	1999	0.5	(19.9)	21.0	(40.9)
1973	4.7	(2.5)	(14.8)	12.3	2000	6.5	26.6	(9.1)	35.7
1974	5.5	(48.7)	(26.4)	(22.3)	2001	(6.2)	6.5	(11.9)	18.4
1975	21.9	2.5	37.2	(34.7)	2002	10.0	(3.8)	(22.1)	18.3
1976	59.3	129.3	23.6	105.7	2003	21.0	15.8	28.7	(12.9)
1977	31.9	46.8	(7.4)	54.2	2004	10.5	4.3	10.9	(6.6)
1978	24.0	14.5	6.4	8.1	2005	6.4	0.8	4.9	(4.1)
1979	35.7	102.5	18.2	84.3	2006	18.4	24.1	15.8	8.3
1980	19.3	32.8	32.3	0.5	2007	11.0	28.7	5.5	23.2
1981	31.4	31.8	(5.0)	36.8	2008	(9.6)	(31.8)	(37.0)	5.2
1982	40.0	38.4	21.4	17.0	2009	19.8	2.7	26.5	(23.8)
1983	32.3	69.0	22.4	46.6	2010	13.0	21.4	15.1	6.3
1984	13.6	(2.7)	6.1	(8.8)	2011	4.6	(4.7)	2.1	(6.8)
1985	48.2	93.7	31.6	62.1	2012	14.4	16.8	16.0	0.8
1986	26.1	14.2	18.6	(4.4)	2013	18.2	32.7	32.4	0.3
1987	19.5	4.6	5.1	(0.5)	2014	8.3	27.0	13.7	13.3
1988	20.1	59.3	16.6	42.7	2015	6.4	(12.5)	1.4	(13.9)
1989	44.4	84.6	31.7	52.9	2016	10.7	23.4	12.0	11.4
1990	7.4	(23.1)	(3.1)	(20.0)	2017	23.0	21.9	21.8	0.1
1991	39.6	35.6	30.5	5.1	2018	0.4	2.8	(4.4)	7.2
						18.7%	20.5%	9.7%	
						1091899%	2472627%	155019%	

Source: Company data.

Exhibit 2



Source: Geiconow.com.



Source: AmericanExpress



Source: Coca Cola Co

VALUATION AND REPURCHASE LEVELS

In the past Mr. Buffett often referred to Berkshire's change in book value as a proxy for evaluating the progress against the S&P 500 Index. Since 2009, price-to-book (GAAP) value has fluctuated between 1.1x and 1.6x. At the end of March 2019, book value per Class A Share was \$225,553 or approximately 1.4x the current price.

For many years, Berkshire had a common share repurchase plan based on buying shares at prices no higher than a 20% premium to book value. On July 17, 2018, Berkshire's Board of Directors changed the program. Now Warren Buffett

and Charlie Munger are authorized to repurchase shares when they believe shares are trading at a discount to intrinsic value, “conservatively determined.” Since the change, the company has repurchased 2,475 Class A Shares for \$750 million and 11.3 million Class B Shares for \$2.3 billion. (Table 2)

Exhibit 3 **Berkshire Class A Price-To-Book Ratio**
2008 – May 2019



Table 2 **Berkshire Repurchase History (2018 – 1Q 2019)**

	<u>Date</u>	<u>Class A</u>	<u>Price</u>	<u>Total</u>	<u>Class B</u>	<u>Price</u>	<u>Total</u>
1Q19	Mar-19	965	\$304,175	\$293,529,020	5,924,418	\$200.63	\$1,188,615,983
	Feb-19	293	302,622	88,668,293	595,412	201.73	120,112,463
4Q18	Dec-18	790	295,954	233,803,652			
	Oct-18	202	310,763	62,774,084	589,955	205.09	120,993,871
3Q18	Aug-18	225	312,807	70,381,517	4,139,192	207.09	857,185,271
		<u>2,475</u>	<u>\$302,690</u>	<u>\$749,156,565</u>	<u>11,248,977</u>	<u>\$203.30</u>	<u>\$2,286,907,588</u>
		Class A Price	\$314,750		Class B Price	\$209.29	

Source: Company data.

CONCLUSION

Another year and more interesting progress from the investment team of Warren and Charlie. Last year, Mr. Buffett talked about his legacy and his desire to be remembered for his teaching. The 2019 annual meeting provided both typical reinforcement of historic values and insight on the firm’s unique corporate evolution (Apple app and investing in Amazon).

Is anyone tired of questions about management succession? Mr. Buffett is so good at assuaging shareholder concerns, yet investors seem so hung up on the topic. The good news beyond the inevitable is that the corporate bench is seasoned and has a terrific history of execution. Vice Chairmen, Greg Abel (56) and Ajit Jain (67) have had

distinguished and long tenured careers at the firm (Ajit since 1986, Greg since 1992). During the meeting Q&A, Warren credited Ajit for generating over \$50 billion of gains for Berkshire or the equivalent market capitalization of Deere & Company, the 110th largest firm in the S&P 500 Index. Todd Combs (48) and Ted Weschler (57) continue to assume more of the investment capital and have also added through their own networks an increased pipeline of potential transactions for the conglomerate. During last year's meeting, Warren had stated that both had outperformed his own investments for the firm during their tenures.

As part of the video series, Tim Cook and Warren teamed up for an entertaining short film about tech innovation. As part of the script Warren shows up at the Apple campus and demands to drive innovation. Among the products he humorously designs are a Mrs. See's chocolate computer (the consumer eats it while she works) and an iPad that dispenses Dairy Queen ice cream. During this episode he also pokes fun of his Cupertino friends by working furiously on multiple white boards, while consuming large amounts of caffeinated soda. The short was one of the more popular aspects of the movie series given the applause and reaction to co-partner Tim Cook as they reveal the "tangible innovation" or Warren's new app "Paper Wizard." The game provides entertainment to individual players as they throw newspapers at residential and other properties while collecting points for accuracy and consistency. More important though on messaging, the film and its unique app provide more data points about Berkshire's evolution and appreciation for consumer/technology firms such as Apple. Although it helps when you own approximately \$50 billion of a company, Warren's engagement is a golden endorsement and further solidifies investor interest in the giant firm.

Value investing. One of the questions from the audience asked about how the firm could buy Amazon given Berkshire's focus on value stocks (sometimes synonymous with investing in low price to book companies). Warren replied that "the people (Todd or Ted) making the decision on Amazon are absolutely as much value investors as I was when I was looking around for all these things selling below working capital years ago. That has not changed." He explained that there are a lot of considerations when buying an investment including and not limited to the level of tangible assets, company sales, margins and cash and debt on the balance sheet. In the past, firm members have spoken highly about Jeff Bezos and his "miracle work" at Amazon.

Connecting the dots a little more, one could surmise that Berkshire already has a strong knowledge of the cloud opportunity (which Amazon is ranked #1) given the previous investments in IBM and Oracle, and being closely tied to Microsoft (#2) because of founder and Berkshire board member, Bill Gates. Additionally, Apple has disclosed that it uses AWS (Amazon Web Services) for its iCloud storage. Berkshire's own retail company investments provide more feedback on Amazon's platform success, while the health care joint venture with Amazon closes the network further. Lastly, like Apple, the size of Amazon's market cap is attractive because it allows for a significant amount of capital to be put to work and avoids reporting issues related to closely held companies which Warren discussed with respect to ownership of Wells Fargo. So perhaps the investment is not that surprising. CM: "Warren and I are a little older than some people and we are not that flexible. We screwed up not buying Google." WB: "We knew them (Google) when we were using them." CM: "We just sat there sucking our thumbs. Maybe Apple was atonement."

During the quarter, the company repurchased \$1.7 billion of shares (1,258 Class A Shares and ~6.5m Class B shares) and ended with \$110.5 billion in cash and short-term investments on the balance sheet. Several questions were asked about the topic of repurchases. The feedback was consistent:

- 1) Will continue to repurchase shares when the price trades below intrinsic value (for both Warren and Charlie it is not an exact number, but a band of estimates).
- 2) Should the price get to a 25-30% discount the firm would be more aggressive in its approach. Currently the firm's cash position represents almost 20% of the market capitalization.
- 3) Will generally favor open market transactions of the B shares given the superior liquidity vs. the A shares; however, may also consider transactions with major Class A holders, but also using a discount approach.

At over \$500 billion of market capitalization, the serial compounding that occurred earlier in Warren's career is no longer possible (20.5% annual CAGR since 1965), yet management still remains confident in its ability to maintain its culture of disciplined and unique approach to capital allocation. At the turn of the meeting, Warren had negotiated a commitment of \$10 billion for 8% preferred shares in Occidental plus 80 million warrants at \$62.50 (\$5 billion of additional capital) as the firm was actively pursuing an acquisition of Anadarko Petroleum. The financing is contingent

on a completed deal and the preferred cannot be redeemed for ten years, providing Berkshire a long-term opportunity to benefit from \$800 million a year in dividends and equity upside from the warrants. Additionally, there is a \$50 million signing fee, not bad for Buffett's one-hour of negotiating time.

The new 20-year headquarters lease with Kiewit comes with the caveat of expanding the corporate footprint by 100% to two floors of office space versus the current one floor. We believe the Chairman probably incurred the greater expense to increase productivity at the 26 person corporate headquarters and felt he could absorb it in a year when Berkshire was benefiting from \$10 billion+ in gains from the Apple position. CM (from The Daily Journal Meeting 2019) "One of the reasons that Berkshire has been so successful is there is practically nobody at headquarters. We have almost no corporate bureaucracy. Having no bureaucracy is a huge advantage."

CM: "One of the reason we have so many questions is that we are peculiar. I think you are going to have to endure us." At next year's meeting Warren will be approaching his 90th birthday, and well before he will have to decide on the next corporate lease at age 108. In the interim, we think investors should continue to follow the developments from Omaha. CM: (from The Daily Journal Meeting 2019) "If you actually figured out how many decisions were made in the history of the Daily Journal Corporation or the history of Berkshire Hathaway it wasn't very many per year. They were meaningful. It's a game of being there all the time and recognizing the rare opportunity when it comes and recognizing that a normal human life does not have very many."

Other Companies Mentioned:

Alphabet	(GOOG – NASDAQ)
Amazon	(AMZN – NASDAQ)
American Express	(AXP – NYSE)
Apple	(AAPL – NASDAQ)
Coca-Cola	(KO – NYSE)
Deere & Co.	(DE – NYSE)
Kraft-Heinz Company	(KHC – NYSE)
Microsoft	(MSFT – NASDAQ)
Wells Fargo Corporation	(WFC – NYSE)

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Macrae Sykes (914) 921-5398

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ONE CORPORATE CENTER RYE, NY 10580 G.research, LLC TEL (914) 921-5130 FAX (914) 921-5098

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A **Buy** rated stock is one that in our view is trading at a meaningful discount to our estimated PMV. We could expect a more modest private market value to increase at an accelerated pace, the discount of the public stock price to PMV to narrow through the emergence of a catalyst, or some combination of the two to occur.

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A **Sell** is a stock that may be trading at or above our estimated PMV. There may be little upside to the value, or limited opportunity to realize the value. Economic or sector risk could also be increasing.

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