Notes from the 2018 Berkshire Hathaway Annual Meeting

"You're killing me, Daphne."– Warren Buffet's response to an eight-year old girl's excellent question at the Berkshire Hathaway Annual Meeting in Omaha, Nebraska

Comments by Henry Asher

While Saturday's meeting is still fresh in my mind, I wanted to share some impressions that may be different from some of the coverage in the press. For the record, the reports I have read in the New York Times, Wall Street Journal, Bloomberg and on Morningstar's site are uniformly accurate and extremely well-written. My comments reflect the different role that Northstar plays, since we are responsible for committing so much capital to Berkshire's shares on behalf of our clients.

Having just returned from Portugal, Linda held the fort in New York, watching the livestream from the comfort of our office. Our Omaha attendees were:

- Henry Asher (eighth meeting)
- Bobby Asher (first time)
- Joshua Garcia (second meeting)
- Jeff Dziegielewski (first time)
- Diana Asher (first time attendee who has graciously listened to my Omaha sagas for twenty years)

Some Observations:

- While still clearly brilliant and sharp, Warren Buffett has ceded operational oversight to Greg Abel and Ajit Jain. This means that each operating company reports directly to someone other than Buffett himself. This should smooth the way to a more seamless transition once Buffett is unable to act as Berkshire's Chairman. Since he is almost 88 years old, this is an extraordinarily prudent path for the company to take.

- Buffett's historical perspective was wonderfully illustrated by contrasting the headlines from 1942 with his actions. On a summer day in 1942, eleven-year-old Buffett bought his first shares of stock despite headlines about America's losses in the Pacific. Japanese forces were seizing island after island, and this strange kid in Omaha was finding bargains in preferred stocks. The lesson for today is obvious, but still difficult for many of us to accept: As investors, this time really isn't different.

- The core businesses in which Berkshire invests are prospering. This is reflective of the economy. But the risks are clear, and we should not be complacent about possible trade wars or expanding healthcare costs. Buffett pointed out the rise in healthcare compared to GDP from 11% to 18% over the past fifty years. While they have hopes for success in their healthcare joint venture with Amazon and JP Morgan Chase, the outcome is far from assured. As Charlie Munger pointed out, "If it were easy, it would already have been done."

- Charlie Munger is no fan of Bitcoin and compared the whole enterprise to people who would get jealous "If they found out that their neighbors were getting rich trading turds." He's an unfiltered ninety-four-year-old, what can I say?

- Some risks are real, but cannot be quantified in advance. One such area is cyber security. Any attempts to pin a number on it would be misleading, since they would only offer a false sense of accuracy.

- **Important note:** For many years, the holy grail of Berkshire analysts has been the "intrinsic value" calculation for the company. At most other meetings, Buffett has only offered vague platitudes about the subjectivity of such analysis. This time was different. He pointed to the first quarter results and noted that they were straightforward and could be used as a base. And so, if that is the case, the company can expect something like $22,000,000,000 in operating earnings this year. If you assume that $170 Billion of stocks (Coke, Wells Fargo and Apple among them) will add value, you come up with a number somewhere around $35 Billion of total expected earnings. On that basis, Berkshire's shares would appear to be undervalued by approximately 15-20% using current market multiples. This should not excite most normal people, but for me it was a cheap and wonderful thrill.

Comments by Jeff Dziegielewski

Important Themes:

1) People will be living better 10, 20, and 50 years from now. Warren Buffett is bullish on the human race, as "there will be more selection by merit rather than by gender, race, or inheritance."
    a. This is important for long-term investors. Aside from nuclear warfare (in which case, we would have much bigger problems), the world will continue to improve. Great leaders and technology will prevail, ultimately making living easier and allowing the economy to grow and prosper. This holds true in the US, along with other countries across the globe.

2) "Subzero" cost structure and bureaucracy: The conglomerate model has come under pressure as of late, specifically focused on the corporate culture at GE. Berkshire differs in that it operates in a decentralized structure; and, while the company employs about 377,000 people, there are only 26 employees at headquarters. "It isn't just the cost reduction. It's the efficiency gained if you eliminate bureaucracy. I think bureaucracy is like cancer. So we're very anti-bureaucracy." (Charlie Munger 05/05/2018). We try to adopt a similar mind-set at Northstar.

3) Focus on businesses: For much of the meeting, Buffett and Munger spoke about the individual businesses that make up Berkshire, and the mangers that run them. The companies owned by Berkshire continue to produce and perform, and we left the meeting as confident as ever that the operating procedures that got the company to where it is today will carry-on. They invest in excellent businesses with large moats and motivated leaders, and they intend to allow those companies to operate without major interference.

Investment Notes:

1) "The one thing we know is we think long-term bonds are a terrible investment at current rates or anything close to current rates. So basically, all our money that is waiting to be placed is in Treasury bills that I think have an average maturity of four months, or something like that, at most." (Comments by Warren Buffett 05/05/2018)

2) $10,000 in the US Market (assuming an S&P Index Fund had been available then) in 1942 is worth $51,000,000 today; meanwhile, $10,000 in gold is worth about $400,000 today. (Comments by Warren Buffett 05/05/18)

Comments by Joshua Garcia

1) I thought one of the more profound statements to come from the meeting was when Charlie Munger shared the rumination that he and Buffett have always been united by the fact that they are both curious to see the world as it really is. A lot of successful paths can be boiled down to having this pursuit laid at its foundation. And, in many ways, the services we provide at Northstar aim to do just that. By understanding that our focus starts with people (client goals and needs) then process (asset-allocation, effective education and communication) rather than products ("Pleasantville Never Lose a Dime Fund A"); studying behavioral psychology in order to better understand how human nature can work against us, causing us to react in ways that are detrimental to our own self-interest; or seeing through the sensationalism of the media while at the same time understanding that its core function was and continues to be to provide a basis of factual information that we can use to better understand and judge the world around us; our clients trust us to understand who they are in their environment and, with this in mind, to help them make good, well-informed decisions so they can someday stand on the mountaintop, fulfilled at having successfully navigated the valley below.

2) The second idea was the reiteration that being a constant learner in this world is one of the best ways (outside of nepotism and luck, of course) to attain success and remain successful. When it comes to understanding our large, constantly-changing world, the work is never done.

> "If you're going to live a long time, you have to keep learning—what you formerly knew is never enough. So, if you don't learn to constantly revise your earlier conclusions, and get better ones, you are—I always use the same metaphor—you're like a one-legged man in an ass-kicking contest." Charlie Munger, 5/5/18, Berkshire Hathaway Annual Shareholder Meeting.

Comments by Bobby Asher

The key lesson reiterated to me was that the most simple questions led to the most impactful answers. Here are two questions to Buffett and Munger asked by children:

1) "How will tariffs affect trade?"
2) "Why have your most recent investments strayed from the capital efficient philosophy?" (referring to buying businesses).

Warren Buffett's answers:

1) "The benefits of trade are basically not visible. No one thinks about benefits day by day .... The negatives, and there are negatives, are very apparent and very painful."
2) "You're killing me, Daphne," Buffett responded. Buffett went on to reiterate that spending more for a reliable wonderful business is more important than choosing to buy simply based on capital needs.

While these questions may not have been produced by the kids, it speaks to the importance of communication with untrained ears and bringing the conversations to the core of the issues.
Our job at Northstar is (in many cases) to channel the answers to a complex question to the core of the client need. The Lubrizol manager who I spoke with in the expo area set an excellent example of this practice, answering very politely and patiently, as I humbly asked the question "what is a polymer?"

Now I understand what a polymer is and why Lubrizol is (pun not intended) a "sticky business to own."

Also, I took away the conclusion that "networking" as a term, should be in the same bucket as "sales" and "selling." The goal in each case falls under the umbrella of "building relationships and connections."

The lasting impression that the Lubrizol "manager" (whom at any other organization would be called "executive") made on me is the quintessential example of how to build a relationship with shareholders correctly. He had also run marathons (he saw the Boston shirt) and probably knows more about shoes than Jim Webber, the CEO of Brooks Shoes, yet another Berkshire-owned company.

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