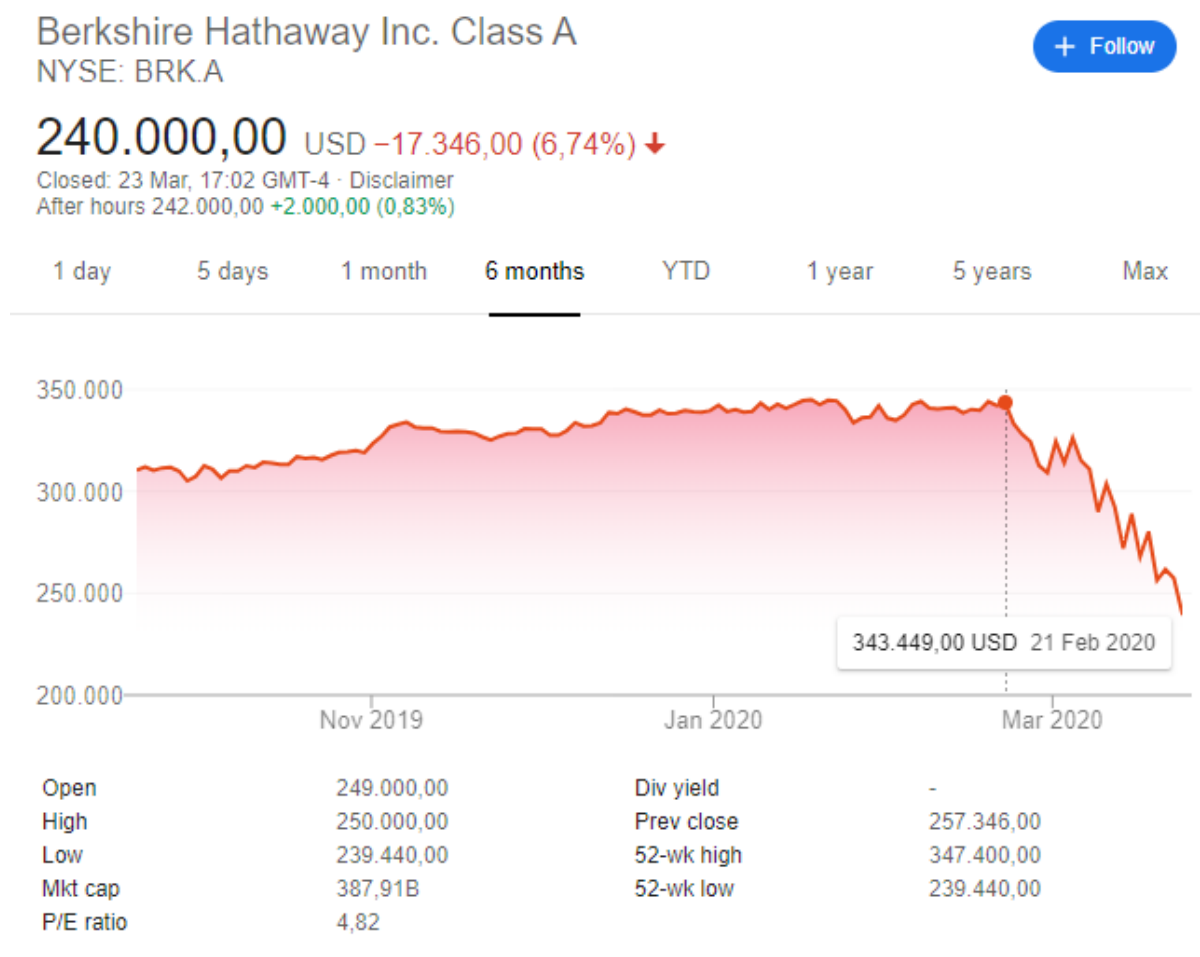


Berkshire’s expected long-term returns are back into double digits and make it an amazing, low risk, buy

Berkshire cannot trade at a single digit price earnings ratio – makes it cheap

Warren Buffett likes to tell that over the past 50 years, there have been four times Berkshire’s stock (BRK.A) (BRK.B) fell between 40% and 60%. As I am writing this, BRK is down 31% from the recent peak. Not to be added to Buffett’s story yet, but it already is a significant drop that justifies making a long-term investment analysis of BRK.



Berkshire is not a complex business to analyse. You can make it complex and discuss all the holdings in detail but that isn’t going to give an answer to the important questions to answer before investing in BRK.

The most important questions to answer before investing in BRK are:

Why is Berkshire stock down?

What are the fundamental, long-term business earnings?

What is the growth outlook?

What is the bankruptcy likelihood related to the current situation? Nil.

What the market is missing when it comes to BRK? Why the baby is thrown out with the bathwater.

### Why is Berkshire stock down?

BRK is mostly exposed to the US economy and with large parts of it in lockdown, BRK's business will get hit. However, we must look at what BRK owns and how it will get hit. Headlines like [the below one](#) might lead people to sell the stock, but there is much more to BRK than stock prices.

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## Warren Buffett's Berkshire Hathaway may have racked up \$80 billion in coronavirus losses on its 10 biggest investments

Theron Mohamed  
© Mar. 23, 2020, 01:54 PM

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- Warren Buffett's Berkshire Hathaway may have racked up over \$80 billion in losses across its 10 largest equity holdings as coronavirus hammered the stock market.
- Berkshire's stakes in Apple, Coca-Cola, Delta, and other household names fell in value by an average of 43% between February 20 and midday on

#### MARKET VIEW

Your Personalized Market Center

Porsche	37.64	-27.34	-42.07%
BHC	13.27	-0.39	-2.86%
Xinyi Glass	0.94	-0.03	-3.11%
Sodexo	56.94	-0.22	-0.38%
Amer-yhtymä	42.00	-2.90	-6.46%

#### Best Savings Accounts & Rates — March 2020

<b>TotalDirectBank</b> <small>MONEY MARKET ACCOUNT Member FDIC</small>	APY <b>1.85%</b> <small>Mar 23, 2020</small>
MIN. BALANCE	<b>\$2,500</b>
EST. EARNINGS	<b>\$463</b> <small>Over 1 Year</small>

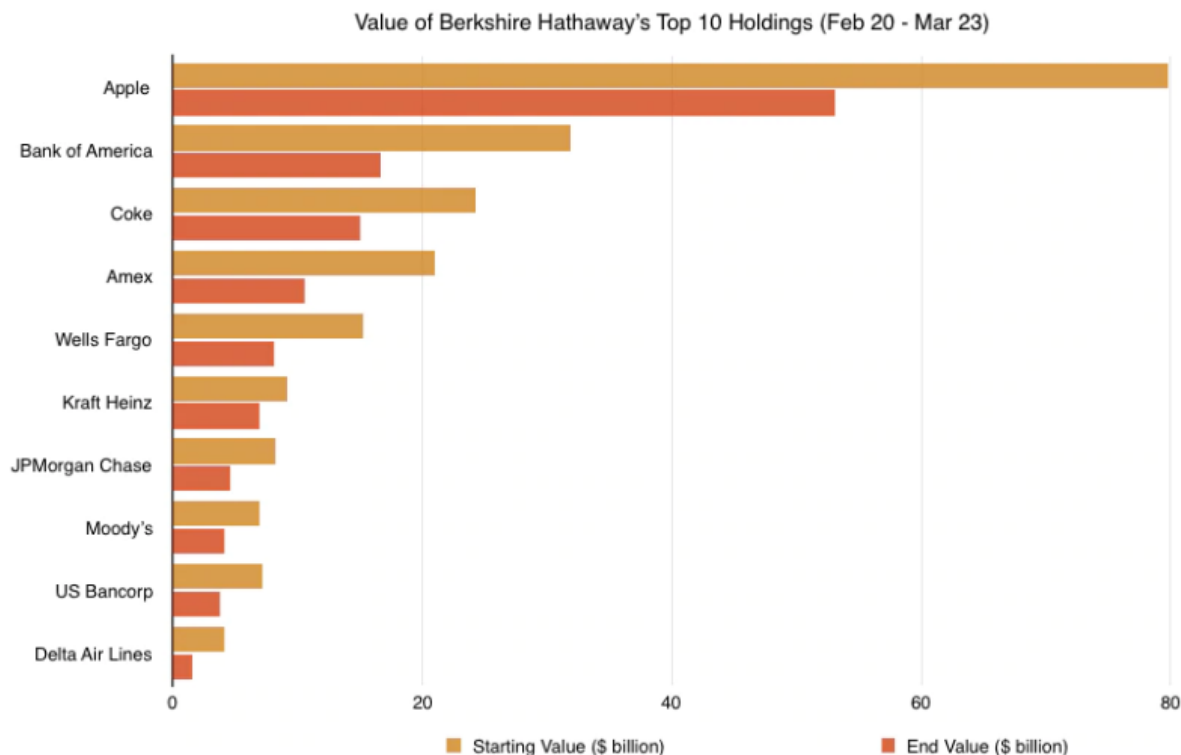
BRK's stock market portfolio at 2019 yearend was \$248 billion.

**Investments**

Below we list our fifteen common stock investments that at yearend had the largest market value. We exclude our Kraft Heinz holding – 325,442,152 shares – because Berkshire is part of a control group and therefore must account for this investment on the “equity” method. On its balance sheet, Berkshire carries the Kraft Heinz holding at a GAAP figure of \$13.8 billion, an amount that represents Berkshire’s share of the audited net worth of Kraft Heinz at December 31, 2019. Please note, though, that the market value of our shares on that date was only \$10.5 billion.

<i>Shares*</i>	<i>Company</i>	<i>Percentage of Company Owned</i>	<i>12/31/19</i>	
			<i>Cost**</i>	<i>Market</i>
			<i>(in millions)</i>	
151,610,700	American Express Company .....	18.7	\$ 1,287	\$ 18,874
250,866,566	Apple Inc. ....	5.7	35,287	73,667
947,760,000	Bank of America Corp. ....	10.7	12,560	33,380
81,488,751	The Bank of New York Mellon Corp. ....	9.0	3,696	4,101
5,426,609	Charter Communications, Inc. ....	2.6	944	2,632
400,000,000	The Coca-Cola Company .....	9.3	1,299	22,140
70,910,456	Delta Air Lines, Inc. ....	11.0	3,125	4,147
12,435,814	The Goldman Sachs Group, Inc. ....	3.5	890	2,859
60,059,932	JPMorgan Chase & Co. ....	1.9	6,556	8,372
24,669,778	Moody’s Corporation .....	13.1	248	5,857
46,692,713	Southwest Airlines Co. ....	9.0	1,940	2,520
21,938,642	United Continental Holdings Inc. ....	8.7	1,195	1,933
149,497,786	U.S. Bancorp .....	9.7	5,709	8,864
10,239,160	Visa Inc. ....	0.6	349	1,924
345,688,918	Wells Fargo & Company .....	8.4	7,040	18,598
	Others*** .....		<u>28,215</u>	<u>38,159</u>
	Total Equity Investments Carried at Market .....		<u>\$110,340</u>	<u>\$248,027</u>

Given the market’s rout, many of those are down and yes, the value of those stocks is down \$80 billion.



However, the same value was also up \$57 billion in 2019 and therefore, one should not focus on the stock prices of BRK's holdings, but on the actual long-term value those offer through real business earnings.

### Berkshire stock and its earnings

Investing in BRK is not about stock prices, it is about earnings. Berkshire's share in earnings from just the top 10 stock market portfolio positions in 2019 was \$8.3 billion.

<u>Company</u>	<u>Yearend Ownership</u>	<u>Berkshire's Share (in millions)</u>	
		<u>Dividends(1)</u>	<u>Retained Earnings(2)</u>
American Express	18.7%	\$ 261	\$ 998
Apple	5.7%	773	2,519
Bank of America	10.7%	682	2,167
Bank of New York Mellon	9.0%	101	288
Coca-Cola	9.3%	640	194
Delta Airlines	11.0%	114	416
J.P. Morgan Chase	1.9%	216	476
Moody's	13.1%	55	137
U.S. Bancorp	9.7%	251	407
Wells Fargo	8.4%	705	730
<b>Total</b>		<u><u>\$3,798</u></u>	<u><u>\$8,332</u></u>

(1) Based on current annual rate.

(2) Based on 2019 earnings minus common and preferred dividends paid.

Source: [2019 Annual Report Berkshire Hathaway](#)

On top of the stock market earnings we have the earnings from businesses that are not listed as BRK owns 100% of them. BRK's insurance, railroad, utilities and other businesses earned an additional \$23.3 billion in 2019. We do not include the \$57 billion stock market portfolio gains or losses because that is just accounting and something long-term investors don't really care about. Last year's accounting gain of \$57 billion will likely be an \$80 billion loss this year if things remains as those are at the time of writing.

#### Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

##### Results of Operations

Net earnings attributable to Berkshire Hathaway shareholders for each of the past three years are disaggregated in the table that follows. Amounts are after deducting income taxes and exclude earnings attributable to noncontrolling interests (in millions).

	2019	2018	2017
Insurance – underwriting	\$ 325	\$ 1,566	\$ (2,219)
Insurance – investment income	5,530	4,554	3,887
Railroad	5,481	5,219	3,959
Utilities and energy	2,840	2,621	2,033
Manufacturing, service and retailing	9,372	9,364	7,282
Investment and derivative gains/losses	57,445	(17,737)	1,377
Other	424	(1,566)	(485)
Tax Cuts and Jobs Act of 2017	—	—	29,106
Net earnings attributable to Berkshire Hathaway shareholders	\$ 81,417	\$ 4,021	\$ 44,940

In total, BRK's earnings have been at \$8.3 billion from BRK's share in the earnings of the businesses held in the stock market portfolio and \$23.3 from the owned businesses for a total of \$31.6 billion. Thus, we can conclude that in a good year for the economy, BRK will make more than \$30 billion.

Given the situation now, likely economic slowdown, it is a certainty that BRK's earnings will not come even close to \$30 billion in 2020. However, that might be the case again in 2021 or 2022 and certainly beyond.

This means that at current levels, BRK's market capitalization of \$387 billion, implies a long-term return of 8.1% when we divide the \$31.6 billion in earnings with the market capitalization.

8.1% is not bad, but wait, it actually gets better.

#### Berkshire's \$124 billion cash pile

Over the past 10 years many have been accusing Buffett that he has too much cash, how he is missing out on many opportunities and how he is doing a disservice to his shareholders. However, if you listen carefully to what Buffett and Munger have been saying over time, you'll know that they target investment returns that can compound into eternity and are at least at 8% at the moment they make the investment.

So, firstly, we have to deduct the \$100 billion from the market capitalization. I will not deduct the complete \$124 billion because Warren always mentions how he needs approximately \$24 billion for potential insurance calamities.

By deducting \$100 billion from the market capitalization, BRK shareholders are buying a business making \$31.6 billion for \$287 billion for a return of 11.1%.

It is also very likely is that Buffett will like the above returns very much and do lots of buybacks at current levels that further increase shareholders returns as it is certain the current stock price is below Buffett's intrinsic value estimation. As he was ready to buy back shares months ago when the price was much higher, he must be even happier now.

### Short Subjects

In past reports, we've discussed both the sense and nonsense of stock repurchases. Our thinking, boiled down: Berkshire will buy back its stock only if a) Charlie and I believe that it is selling for less than it is worth and b) the company, upon completing the repurchase, is left with ample cash.

Calculations of intrinsic value are far from precise. Consequently, neither of us feels any urgency to buy an *estimated* \$1 of value for a very real 95 cents. In 2019, the Berkshire price/value equation was *modestly* favorable at times, and we spent \$5 billion in repurchasing about 1% of the company.

Over time, we want Berkshire's share count to go *down*. If the price-to-value discount (as we estimate it) widens, we will likely become more aggressive in purchasing shares. We will not, however, prop the stock at any level.

Shareholders having at least \$20 million in value of A or B shares and an inclination to sell shares to Berkshire may wish to have their broker contact Berkshire's Mark Millard at 402-346-1400. We request that you phone Mark between 8:00-8:30 a.m. or 3:00-3:30 p.m. Central Time, calling only if you are ready to sell.

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Further, he might be buying also other things that will deliver good returns long-term.

So, by buying BRK, you will likely own a business that will have a price to earnings ratio below 10 in the coming years when the economy stabilizes. You have a cash cushion that is likely being deployed for good returns and you have infinite compounding growth. A set of features you can hardly find anywhere else. Given all the above, BRK is one of the best no risk long-term investments that offer a good return at these levels. See how that fits your investing requirements and whether BRK is the vehicle that will lead you to your financial goals.

### Berkshire is a financial fortress

Investing in BRK means investing in a financial fortress where the fortress is not a cost but it actually makes money. Safety and never running out of cash, as said below in the 2018 letter to shareholders, is what has been Buffett's credo since ever and what makes BRK a no risk investment even in situations like the current ones.



In our fourth grove, Berkshire held \$112 billion at yearend in U.S. Treasury bills and other cash equivalents, and another \$20 billion in miscellaneous fixed-income instruments. We consider a portion of that stash to be untouchable, having pledged to always hold at least \$20 billion in cash equivalents to guard against external calamities. We have also promised to avoid *any* activities that could threaten our maintaining that buffer.

Berkshire will forever remain a financial fortress. In managing, I will make expensive mistakes of commission and will also miss many opportunities, some of which should have been obvious to me. At times, our stock will tumble as investors flee from equities. But I will never risk getting caught short of cash.

In the years ahead, we hope to move much of our excess liquidity into businesses that Berkshire will permanently own. The immediate prospects for that, however, are not good: Prices are sky-high for businesses possessing decent long-term prospects.

That disappointing reality means that 2019 will likely see us again expanding our holdings of marketable equities. We continue, nevertheless, to hope for an elephant-sized acquisition. Even at our ages of 88 and 95 – *I'm the young one* – that prospect is what causes my heart and Charlie's to beat faster. (Just writing about the possibility of a huge purchase has caused my pulse rate to soar.)

My expectation of more stock purchases is *not* a market call. Charlie and I have no idea as to how stocks will behave next week or next year. Predictions of that sort have *never* been a part of our activities. Our thinking, rather, is focused on calculating whether a portion of an attractive business is worth more than its market price.

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Source: [2018 Annual report](#)

If the FED's unlimited QE leads to inflation, BRK will be positioned even better as most of BRK's businesses have pricing power. The insurance part will get hurt in such a situation but other insurers would get hurt more which means BRK would gain market share long-term.

On the risk of things going bad due to the current economic situation. If there is one company that is structured to weather anything, that is Berkshire. Therefore, I don't think investors should be worried about the going concern.

So, whatever happens, it is always a win, win, win situation for BRK and Buffett.