

## A BUFFET OF KNOWLEDGE FROM BUFFETT

by [Steve Brown](#)

Over the weekend, if you are a shoe collector, the Nike Galaxy Air Foamposite Ones were all the rage. If you wanted a pair of these shoes, you had wait in incredibly long lines, riot or pay \$1,200 at eBay. If you are a collector of business knowledge, however, things were a little easier. You were still giddy with anticipation, as Berkshire's much-loved annual shareholder letter was released. While we question anyone who makes a Netjets investment on top of a losing US Air investment, what do we know - we are just \$40B shy of the man's \$40B net worth. You don't judge a person by their worst trade and you don't get to be in the top 3 of the Richest People in the World by making bad financial decisions. You can call Buffett over-hyped and one of the first to take advantage of the U.S. Gov't during the crisis (Goldman Sachs investment), but he stands alone as one of the smartest investors the world has produced. This is why we closely review every word of his annual shareholder letter. An analysis of Berkshire Hathaway and its wisdom is helpful on many different levels - investments, sales, risk management, M&A, diversification, benchmarking, you name it and Buffett is one of the best. This year, he doesn't disappoint, as he gives insight into cash flow value, governance, lending and philosophy. We capture a few of our favorite tidbits of knowledge below: - "The primary job of a Board of Directors is to see that the right people are running the business and to be sure the next generation of leaders is identified." - "Our [Charles and I] primary focus is on building operating earnings." Note nothing in the letter about building asset size, operating margin, or market share. In fact, he writes a tidbit that is worth the whole read: "Ignore our net income figure. Regulation requires that we report it to you." When it comes to analyzing a business, net income with its onetime gains and accounting adjustments, is a poor stand in for cash flow. Warren nails it with his IBM analysis on page 7. - Warren made a "major unforced error" in calculating "gain/loss probabilities," when he made an investment in Energy Future Holdings, which was really just a bet on natural gas prices. Note his framework in dealing with probabilities, as well as a quick admission and accountability for the mistake. - While Berkshire has been wrong on housing's bounce-back for the past 18 months, he is still very bullish on the sector. - A lesson in cost control and leading by example - "At Berkshire's World Headquarters' our rent is \$270,212. Moreover, the home office investment in furniture, art, Coke dispenser, lunch room, high-tech equipment - you name it - totals \$301,363. As long as Charlie and I treat your money as if it were our own, Berkshire's managers are likely to be careful with it as well." - Hitting home for bankers - Warren loves "float." Like a non- interest bearing deposit, the money from insurance premiums sitting around amortizing until claims are paid out, is "like a deposit" with a "fee for holding" that can be invested "for our own benefit." - Warren understands the importance of branding as he likes to buy companies [Coke, See's, etc.) when they are "commodities and sell when they are brands (sic)" As regulatory pressure subsides, banks will again pay a dividend, making them a great value. - "Charlie and I favor repurchases when two conditions are met: first, a company has ample funds to take care of the operational and liquidity needs of its business; second, its stock is selling at a material discount to the company's intrinsic value, conservatively calculated." This should be required reading for anyone running a bank. Buffett's latest investment philosophy, combined with his homespun humor and his never-ending effort to promote his products, is a monument to business intelligence.

Read the entire letter and be sure to check out his 4 disciplines of insurance investing that could pertain to loan underwriting. Particularly, his comment that many businesses can't price risk as they

"simply can't turn their back on business that their competitors are eagerly writing. That old line, "The other guy is doing it so we must as well," spells trouble in any business."

#### **Related Links:**

[Berkshire Hathaway Annual Shareholder Letter](#)

## **BANK NEWS**

### **Closed (11 YTD)**

Regulators closed: 1) Central Bank of Georgia (\$279mm, GA) and sold it to Ameris Bank (\$3.0B, GA). Ameris gets 5 branches, all deposits and entered into a loss share on \$193mm of assets. 2) Home Savings of America (\$434.1mm, MN) was closed and a buyer was not found, so the institution will be liquidated. The last time the FDIC paid out deposits immediately to account holders was late 2010, when they couldn't find a buyer willing to assume the deposits of First Arizona Savings Bank.

### **Social Media**

An article in the Philadelphia Business Journal indicates Sun Bancorp (\$3.2B, NJ) has 574 Twitter followers, Susquehanna (\$14.3B, PA) has 1,217; Fulton (\$9.0B, PA) has 174 and Beneficial (\$4.7B, PA) has 1,033.

### **Switch Kits**

A survey by the ICBA found about half of community banks have a switch kit to move customers to their bank and about half still do not.

### **BofA**

In an effort to cut costs, the Bank announced that they will stop pension contributions starting July 1 and will instead utilize 401(k) plan contributions with a 2% to 3% employer match. The move is similar to what Wells did back in 2009, as about 70% of Fortune 100 companies have made the switch, according to Towers Watson.

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