



OVERBERG MARKET REPORT

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GLOBAL

Gielie Fourie

Warren Buffett's 2022 Letter to Berkshire Hathaway's shareholders.

INTRODUCTION: Since 1965 Warren Buffett (91) has been sending "Annual Letters" to Berkshire Hathaway's (Berkshire's) shareholders. Buffett has never written a book - but his Annual Letters are a treasure chest of investment wisdom. Buffett treats all shareholders equally and he likes to keep things simple. Each shareholder receives a copy of his Annual Letter. Despite being one of the biggest companies in the world, this year's Annual Letter is only 12 pages long. No discussions are granted to analysts, not even to large institutions. Whenever possible, important communications are released on Saturday mornings, when financial markets are closed. The reason for this is to maximise the time for shareholders and the media to absorb the news before markets open on Monday mornings.

TOP HOLDINGS: Berkshire is a diversified holding company whose subsidiaries engage in insurance, freight rail transportation, energy generation and distribution, services, manufacturing, retailing, and other activities. At 31 Dec 2021 the top 15 holdings were valued at \$331 billion (bn). The cost price was \$78 bn, representing a "book" profit of \$253 bn, or 324%. The 15 holdings, all of them are listed companies, include familiar names like American Express, Apple (the biggest holding), Bank of America, The Coca Cola Company, General Motors, Mitsubishi Corporation, Moody's Corporation (the ratings agency) and Verizon Communications. Its biggest and most profitable investment is GEICO, a car insurance company. GEICO is a wholly owned subsidiary of Berkshire - it is not a listed company. Warren Buffett: "GEICO, (bought in 1967), has grown Berkshire's total (cash) float from \$19 million when we entered the insurance business, to \$147 billion. So far, this float has cost us less than nothing."

PERFORMANCE: These 15 holdings are the real drivers of Berkshire. This is what Charlie Munger (98), Buffett's long-time business partner, has to say about the top 15 holdings: "If you took our top fifteen decisions out, we'd have a pretty average record. It wasn't hyperactivity, but a hell of a lot of patience. You stuck to your principles and when opportunities came along, you pounced on them with vigour." In addition to these 15 listed companies, Berkshire owns more than 100 unlisted companies. Berkshire's share performance from 1965 to 2021, compared to the S&P 500, is remarkable. The S&P 500 has increased by 30,209%. Berkshire has grown by 3,641,613%. This is not a typing error - 3.6 million percent.

BERKSHIRE'S FOUR GIANTS: Buffett calls the four biggest holdings his four "Giants". The first Giant is GEICO, an insurance company, of which Berkshire owns 100%. The second Giant is APPLE, a listed company of which Berkshire owns 5.6%, valued at \$161 bn. Giants number three and four are interesting - they are unlisted companies, and they remind one of South Africa's struggling Transnet and Eskom. The difference is that Berkshire's Giants are very profitable. The third Giant is BNSF Railway. It is one of the largest freight railroads in North America. BNSF has 32,500 miles of track and nearly 8,000 locomotives. To put things into perspective - Transnet owns just over 1,000



locomotives. The fourth Giant is BHE. BHE has become a leading force in wind power and solar power generation and transmission throughout much of the United States. Unlike Eskom it is working and profitable.

CASH MANAGEMENT: Berkshire's balance sheet includes \$144 bn of cash. Buffett does not like this. Buffett: "I always kept at least 80% of my net worth in equities. My favoured status ... is 100% - and still is. Berkshire's current 80%-or-so position in businesses is a consequence of my failure to find entire companies or small portions thereof (that is, marketable stocks) which meet our criteria for long-term holding. Charlie and I have endured similar cash-heavy positions from time to time in the past. These periods are never pleasant; they are also never permanent. And, fortunately, we have had a mildly attractive alternative during 2020 and 2021 for deploying capital. Today, internal opportunities deliver far better returns than acquisitions." What Buffett means by this is that repurchasing Berkshire shares is one of the best investments he can make.

FINANCIALS: Full-year earnings for 2021 came in at \$90 bn, more than double 2020's total of \$43 bn. Federal income taxes paid to the Treasury last year amounted to \$3.3 bn - Berkshire pays roughly \$9 million every day to the Treasury. The balance sheet is strong. Berkshire not only owns more than \$350 bn in financial assets. The infrastructure assets (property, plant, and equipment) that it owns and operates, are valued at \$158 bn. This is more than the infrastructure owned and operated by any other American corporation.

CLOSING REMARKS: Buffett is a value investor. Over the past few years value investors have experienced torrid times. On the other hand, growth investors have done very well but the pendulum has swung. Year-to-date (YTD) the price of Berkshire shares is up by 17%, while several Hi-Tech growth shares are down, some by double digits: Microsoft -10%, Amazon -2%, Tencent -21% and Facebook (Meta Platforms) -35%. Berkshire's share price is trading around \$540,000.00 per share, the highest priced publicly trading stock in the US. Berkshire's Annual General Meeting (AGM) is scheduled for 1 May 2022 in Omaha. Want to attend? Then get vaccinated. Proof of Covid vaccination will be required to attend the "Woodstock for Capitalists". Expected attendance is around 40,000 people. The AGM will be live-streamed.

LOCAL

Kirk Swart

Regulation 28: "Yes", to infrastructure: "No", to Crypto. Limited Offshore Exposure Remains a concern.

What Is Regulation 28: Regulation 28 is that controversial piece of legislation in the Pensions Fund Act that sets investment parameters for pension fund investments. This includes investments in retirement annuities, provident funds, pension funds, pension preservation funds and provident preservation funds. The Pensions Fund Act has been amended many times since its adoption in 1956 to stay relevant in the everchanging retirement landscape.

Why Regulation 28: The aim of regulation 28 is not to limit the investment options available but rather to protect investors from reckless investing. Reckless investing has the potential to create a



burden on the state when investors enter retirement. The current investment limits and the recent changes are:

- A maximum of 75% may be invested in shares. (No change).
- A maximum of 25% may be invested in property. (No change).
- A maximum of 30% of assets may be invested offshore. (Lifted to 35%).
- A maximum of 10% of assets may be invested in African markets outside SA. (No change).

It is the last two limits, that limits exposure to offshore assets, which have been most controversial. Given the underperformance of the Johannesburg Stock Exchange (JSE) compared to other global markets and the exodus of companies delisting from the JSE, calls have been growing for an increase in offshore limits.

JSE Underperformance and De-listings: The underperformance of the JSE versus global indices over the last 10 years is clear. While the S&P 500 returned an average of 21% per year since Feb 2012, the JSE returned 8% over the same period. For long periods during the 10 years the JSE delivered negative returns. It is due to the recent rally in resources that the JSE managed a positive return over the 10 years. However, resources are historically cyclical which can turn negative very quickly.

The argument for increased offshore exposure becomes even stronger as the number of investable companies on the JSE steadily declines. During 2021, 25 companies delisted from the JSE and there were only 7 new listings. For 2022, 20 de-listings have been announced which will be completed before the end of the year. As de-listings escalate, the concentration risk on the JSE increases leaving Naspers, Prosus and resources as the remaining heavy weights. One might argue that to enjoy the tax advantages of a retirement product in South Africa, investments should be South African based. However, these tax advantages mean little if investors remain subject to a market that is underperforming.

Recent draft legislation on infrastructure and crypto assets: In October 2021 draft amendments introduced two new asset classes namely “crypto assets” and “infrastructure”. The draft amendments aim to prohibit pension funds from investing in crypto assets while opening the door for infrastructure investments. Crypto, given its extreme volatility, is not deemed safe enough for pension fund investing. While infrastructure investments are currently permitted under regulation 28, the draft amendments aim to define “infrastructure” as a sub-category. It is proposed that investment in infrastructure across all categories does not exceed 45% and not exceed 25% per single issuer. The draft amendments do not prescribe the investment of funds into infrastructure, they merely set the limits not to be exceeded. Infrastructure is defined as “any asset class that entails physical assets constructed for the provision of social and economic utilities or benefit to the public”. Having defined infrastructure could open the door for prescribed infrastructure allocations in future.

Do the draft amendments help: The draft amendments do very little to address the problem of investment underperformance in South Africa. Investors should be allowed to allocate a bigger part of their pensions offshore. With the ever-growing offering of global products available in South Africa, investors can optimize the offshore allowance by working with a trusted offshore portfolio manager. Today it is possible to gain access to markets all over the world from the east to the west.

Overberg Asset Management has created portfolios that specifically fit the offshore allowance gap allowed by regulation 28. These portfolios have exposure to global markets that are diversified across currencies, regions and asset classes. Do not let the lack of offshore exposure in your retirement



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portfolio negatively affect your retirement. Speak to Overberg Asset Management today to enquire about our global portfolios that will allow you to maximise your offshore allowance.



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