TIM UNDERWOOD

Monthly Report – February 2023

Probably the most famous investor is Warren Buffett who together with his partner Charlie Munger have managed the company Berkshire Hathaway for over 50 years. Their performance has far exceeded the US stock market as measured by the S&P500 and a whole industry has developed trying to analyse how they can be so successful. The company is based in Omaha in the mid West USA, rather than Wall Street, but the two billionaires are quite open about their business. Each quarter they release data on their investments and each year a shareholder letter is sent out, the latest was just published in February.

They openly admit that they are not stock pickers, but buyers of businesses. Some businesses are wholly owned and there they have control, but tend to put good managers in place and let them run the business. Other investments are in public companies where they have little influence and the recent data shows the following holdings:

Apple Inc	40%
Bank of America	11%
Chevron	10%
Coke Cola	9%

So just 4 companies make up 70% of the portfolio with an amazingly large allocation to Apple Inc. It is generally recommended for investors to have a wide diversification of investments so this is unusual but also because I have read that one of Mr Buffet's rules for selling an investment is when it gets too big, within a portfolio to maintain diversification. (The other two rules are when an industry is suffering a major set back so even the best companies will struggle and secondly when he can see a better investment for the capital. Note no mention of the buying price, profit or loss when deciding to sell). Their criteria for investing, or buying a business as they put it, is when the intrinsic value of the company is more than the capital value.

Intrinsic value is the future cash flows that can be expected in the years ahead discounted back to present value at an appropriate discount rate. If that is higher than the current capital value as measured by all the shares outstanding, times the share price, then the company is interesting for them. Simple!

One of the comments in the letter that caught my eye was the Coke Cola holding. They built this up years ago and since 1994 receive millions in dividend cheques. Back in 1994 it was $75 million but by 2022 it has grown to $704 million in dividends each year! Of course the initial investment price has to be attractive and hence their intrinsic value calculation, but once attractive it does show the power of compounding and having investments which have the free cash flow to pay dividends.

Tim 7 March 2023

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