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Warren Buffett, Unplugged

The hands-off billionaire shuns computers, leaves his managers alone, yet has notched huge returns. He just turned 75. Can anyone fill his shoes?

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(See *Corrections & Amplifications* item [below](#).)

OMAHA, Neb. -- Warren Buffett, the billionaire investor and insurance executive, was in his office here this summer when he received a faxed letter about a company he'd never heard of.

The letter was from an adviser to Forest River Inc., an Elkhart, Ind., recreational vehicle maker. He proposed that Mr. Buffett buy the company for \$800 million.




James Bennett

Mr. Buffett liked what he saw: The company had a big market share and little debt.

The next day, Mr. Buffett offered to buy Forest River and to let its founder, Peter Liegl, continue running it. He sealed the deal, at an undisclosed price, in a 20-minute meeting one week later. As the meeting wrapped

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A TRUE SPECIALIST

- [Mr. Maguire's Unusual Job: Trading Berkshire](#)⁵

up, Mr. Buffett told Mr. Liegl not to expect to hear from him more than once a year. Says Mr. Liegl: "It was easier to sell my business than to renew my driver's license."

Mr. Buffett has relied on gut instinct for decades to run Berkshire Hathaway Inc. Watch him at work inside his \$136 billion investment behemoth, and what you see resembles no other modern financial titan. He spends most of his day alone in an office with no computer. He makes swift investment decisions, steers clear of meetings and advisers, eschews set procedures and doesn't require frequent reports from managers. Occasionally he picks up the phone, calls his broker and trades \$100 million or more of stock.

A TRUE SPECIALIST

James Maguire is a "specialist" with one of the [premiere jobs in the business](#)¹: He is responsible for trading Berkshire Hathaway.

On a recent Wednesday, he received only 13 phone calls, including one wrong number. There were no urgent confabs with his staff. He found time to work on new lyrics to "Love Me Tender" for a birthday party for his friend Bill Gates, and to demonstrate a newspaper-throwing technique

he learned while delivering papers as a boy in Omaha.

The older Mr. Buffett gets -- he turned 75 in August -- the more his minimalist approach poses thorny questions for Berkshire. How will his successor be able to take over when so much of Berkshire's DNA resides in Mr. Buffett's head? And in the wake of a recent investigation into a controversial transaction by a Berkshire subsidiary, would a different management style have helped Berkshire avoid trouble?

Mr. Buffett says he has no immediate plans to step down and does not intend to name a successor beforehand. Mr. Gates, Microsoft's chief executive and a Berkshire director, praises Mr. Buffett's hard-to-imitate management style. "It's baffling to think who else could do it," he says.

The uncertainty troubles some outsiders. In April, Fitch Ratings revised the ratings outlook on \$7.5 billion of Berkshire's high-investment-grade debt to "negative" from "stable." Fitch analyst Donald Thorpe says the credit-rating firm doesn't "believe that Mr. Buffett's talents can be easily replaced, or that Berkshire's current investment strategies would be sustainable in his absence."

Though his empire has grown, Mr. Buffett says his routine has changed little over the years. He says he spends the better part of most workdays thinking and reading. He fields a handful of phone calls, and on most days, he confers with the chiefs of a few Berkshire subsidiaries. He seldom holds meetings. "There isn't much going on here," he says of his office on a typical day.

Mr. Buffett, with a personal net worth of \$43 billion, is the nation's second-richest man, after Mr. Gates. His nearly 55-year record has brought him recognition as one of the best investors ever, earned him fierce loyalty from Berkshire shareholders and inspired legions of investors who attempt to ape his moves.





Mr. Buffett calculates that since 1951, he has generated an average annual return of about 31%. The average return for the Standard & Poor's 500 over that period is 11% a year. A \$1,000 investment in Berkshire in 1965 would be worth about \$5.5 million today. Over the past decade, Berkshire shares have tripled in price, returning twice as much, in percentage terms, as the S&P 500. Berkshire's Class A shares closed yesterday at \$90,500. In recent years, the company's growth has slowed, as Mr. Buffett has become wary of deploying cash reserves due to market conditions. ([See related article.](#)²)

Berkshire Hathaway, of which he owns about 31%, is a large and complex business. It has substantial stakes in **Coca-Cola Co.**, **Wells Fargo Co.** and **American Express Co.** And it boasts 42 subsidiaries in businesses ranging from insurance to ice cream to bricks.

Mr. Buffett believes that managers of these companies ought to be left to run their businesses without interference from him, and without having to hew to any unifying corporate strategies or goals. "We delegate to the point of abdication," Mr. Buffett says in Berkshire's Owner's Manual, a six-page manifesto posted on the company's Web site.

This approach sets him apart from other chief executives. Former **General Electric Co.** Chief Executive Jack Welch, for example, decentralized management but closely monitored his managers, who had to meet strict goals. **Microsoft Corp.** requires that its offices and businesses around the globe coordinate their efforts so the company's products fit together.

Even the job of investing Berkshire's \$45 billion stock-investment portfolio -- bigger than all but eight of the 7,063 U.S. stock mutual funds tracked by Lipper Inc. -- is far less systematic than it is at most investment firms. Berkshire has no investment committee or asset-allocation guidelines, and Mr. Buffett does not meet with analysts or advisers.

Despite its size, Berkshire has no public-relations, human-relations, investor-relations or legal departments. It holds no quarterly earnings calls for investors and analysts, and gives no guidance on future earnings. Its headquarters is staffed by just 17 employees.

Berkshire's audit department is a one-woman show: Rebecca Amick, 53. A lone employee, 44-year-old Mark Millard, executes the trades Mr. Buffett directs for Berkshire's \$25 billion bond portfolio and for its \$16.5 billion in foreign-exchange investments.

Marc Hamburg, the 56-year-old chief financial officer, oversees financial reports produced by Berkshire's 42 units and regulatory reporting to the Securities and Exchange Commission. He also writes news releases, which, until a few weeks ago, he sent to the media via fax machine. Mr. Hamburg has a finance staff of

seven, far fewer than the dozens of workers most big companies assign to each aspect of his job. When financial reports for the SEC are due at the end of each quarter, Mr. Hamburg explains, "people work very hard."

Mr. Buffett tells the chiefs of his business units not to produce any special reports for him. When Berkshire was acquiring wholesale food distributor McLane Co. in May 2003, for example, he told Chief Executive Grady Rosier that whatever reports he was producing for its then-owner, Wal-Mart Stores Inc., would be fine for Berkshire. Mr. Rosier says Mr. Buffett has never pushed for more detailed information. "Warren just doesn't call," he says.

Mr. Rosier called Mr. Buffett recently to discuss two company jets. "Warren, I have two Learjets, a 1981 and a 1982," he says he told Mr. Buffett. "They are nearly 25 years old now, and I am thinking about getting a new airplane. Is that an issue?"

AN OWNER'S MANUAL

Excerpts from Warren Buffett's "An Owner's Manual":

Charlie [Munger] and I are the managing partners of Berkshire. But we subcontract all of the heavy lifting in this business to the managers of our subsidiaries. In fact, we delegate almost to the point of abdication: Though Berkshire has about 180,000 employees, only 17 of these are at headquarters.

Charlie and I mainly attend to capital allocation and the care and feeding of our key managers. Most of these managers are happiest when they are left alone to run their businesses, and that is customarily just how we leave them. That puts them in charge of all operating decisions and of dispatching the excess cash they generate to headquarters.

Most of our managers are independently wealthy, and it's therefore up to us to create a climate that encourages them to choose working with Berkshire over golfing or fishing. This leaves us needing to treat them fairly and in the manner that we would wish to be treated if our positions were reversed.

"That is your decision," Mr. Rosier recalls Mr. Buffett replying. "That is your company to run." Says Mr. Rosier: "Wal-Mart left us alone, too. But not like this."

Over the years, not all of Berkshire's investments have been winners, of course. In 1998, Mr. Buffett bought NetJets Inc., a fractional-use aircraft leasing company, for \$725 million of cash and stock after a 20-minute meeting with its founder. Despite fast revenue growth, the company posted losses in each of the past three years -- including a pretax loss of \$41 million in 2003 -- amid tough competition in Europe. Dexter Shoes, a Maine shoemaker purchased by Berkshire for \$420 million in stock, stumbled for eight years. It was absorbed in late 2001 by another Berkshire unit, which took a \$219 million write-off.

On occasion, problems of such severity arise that Mr. Buffett abandons his hands-off approach. Trouble surfaced several years ago at General Re, Berkshire's reinsurance unit, due to bad underwriting policies and a complex derivatives business. Mr. Buffett moved to reduce the

company's exposure to derivatives, financial instruments that are tied to the value of stocks, bonds or other securities. He later called them "financial weapons of mass destruction."

Earlier this year, regulators began investigating a transaction General Re did in 2000 with **American International Group** Inc. They are examining whether AIG manipulated its books to mislead investors, and whether executives at the Berkshire unit knew the transaction was improper. Mr. Buffett has told investigators he didn't know details about the questionable transaction. Investigators have not accused him of any wrongdoing.

On that recent Wednesday morning, at just before 9, Mr. Buffett pulled his slate-colored Lincoln Town Car with vanity license plate "THRIFTY" into a parking garage in downtown Omaha. Mr. Buffett, exhibiting no apparent signs of reduced vigor, walked swiftly toward Berkshire headquarters, which occupies a single

floor of a nondescript office building. Recently, on the advice of his doctor, he adopted a three-day-a-week workout regimen with a personal trainer. "I always feel good," says Mr. Buffett, whose diet is heavy on hamburgers and soft drinks.

He chatted briefly with his assistant, then hurried into his modest-size office and shut the door. There is no computer in there, nor is there a stock-quote machine or stock-data terminal. He keeps a muted television set tuned to CNBC, the financial-news network. Although he occasionally carries a cellphone on the road, he does not use one in Omaha. He keeps no calculator on his desk, preferring to do most calculations in his head. "I deplore false precision in math," he says, explaining that he does not need exact numbers for most investment decisions. On the cabinet behind his desk are two black phones with direct lines to his brokers on Wall Street.

He had barely settled into his seat when one of them rang. It was John Freund, his longtime broker from **Citigroup** Inc.'s investment-banking unit. Mr. Freund briefed Mr. Buffett on a stock position he had been building for Berkshire. "If we bought a couple million, that would be fine," Mr. Buffett said, giving Mr. Freund a parameter for how many shares he wanted to buy that day. (Mr. Buffett declines to identify the stock.)

By the end of the day, Mr. Buffett had bought \$140 million of the stock for Berkshire's investment portfolio -- equal to the entire asset value of many mutual funds.

Even with such heavy trading, Mr. Buffett's desk isn't littered with stock research. "I don't use analysts or fortune tellers," he says. "If I had to pick one, I don't know which it would be."

Mr. Freund says that when Mr. Buffett is buying stock, he pays little attention to some factors that shape other investors' decisions, such as the economic climate. "He doesn't wait to see what the Fed is doing" to make a trade, Mr. Freund says. Mr. Buffett also can move more quickly than his other clients, he says. "There is no investment committee," the broker explains. "That allows him to make immediate decisions."

Mr. Buffett gives Mr. Freund wide latitude to execute transactions. In 2003, for example, Mr. Buffett was buying shares of Chinese oil company **PetroChina** Co. Mr. Freund would often call Mr. Buffett at about 9 p. m. Omaha time, when the Hong Kong market was open, an hour at which Mr. Buffett is typically relaxing at home in a sweat suit, playing bridge online. He interrupted his games to place orders.

One night, when a 200-million-share block of PetroChina came on the market, Mr. Freund phoned Mr. Buffett to gauge his interest. "Let's bid," he recalls Mr. Buffett saying. Later that night, a Hong Kong broker called back to tell Mr. Freund he had bought the shares on Mr. Buffett's behalf. Mr. Freund rolled over and went back to sleep without bothering to wake Mr. Buffett with details of the trade, as some other clients would want. Mr. Buffett built a position that eventually totaled \$488 million, according to a regulatory filing.

Mr. Buffett deliberately keeps the outside world at bay, believing it is the best way for him to remain "rational" as an investor. If he is interested in investing in a company, he studies the financials himself. "I've created a good environment," he says. "All I have to do is think and not be influenced by others."

Last year, Mr. Buffett says, he began buying Korean stocks for his personal brokerage account, investing a total of \$100 million in roughly 20 Korean companies. He says that the investments were too small to be

appropriate for the Berkshire portfolio. "These were not Berkshire-size remotely," he says.

He picked the stocks, which he declines to name, by leafing through a reference book compiled in Korea and provided by Citigroup to some clients. The book devotes a single page to each listed company. "You look for solid-looking companies at very low multiples of earnings, and sometimes with the added bonus of lots of excess cash," he said. After the shares rose in price, he unloaded some of them, though he still calls them cheap.

This year, Mr. Buffett's name surfaced in published reports about potential investors in **Dow Jones & Co.**, the publisher of this newspaper. Mr. Buffett, whose company holds an 18.1% stake in **Washington Post Co.**, declines to comment, as does a spokeswoman for Dow Jones. The Bancroft family, which holds a controlling stake, has said the company is not for sale.

Mr. Buffett, an Omaha native, learned about investing under the tutelage of the classic "value" investor Benjamin Graham, who preached buying beaten-down stocks with good underlying value. He became a broker in 1951 at Buffett-Falk & Co., his father's stock-brokerage firm in Omaha, before going to work for Mr. Graham in New York three years later. In 1965, Mr. Buffett bought control of Berkshire, a foundering New Bedford, Mass., fabric mill. He soon purchased National Indemnity Cos., an Omaha insurer, which gave Berkshire \$20 million of assets.

Buffett's Tips for Individual Investors

1. "Look at stocks as parts of businesses. Ask yourself, 'How would I feel if the Stock Exchange was closing tomorrow for the next three years?' If I am happy owning the stock under that circumstance, I am happy with the business. That frame of mind is important to investing."
2. "The market is there to serve you and not to instruct you. It is not telling you whether you are right or wrong. The business results will determine that. I stole that one from [famed value investor] Ben Graham."
3. "You can't precisely know what a stock is worth, so leave yourself a margin of safety. Only go into things where you could be wrong to some extent and come out OK."
4. "Borrowed money is the most common way that smart guys go broke."
5. "The stock doesn't know you own it. You have feelings about it, but it has no feelings about you. The stock doesn't know what you paid. People shouldn't get emotionally involved with their stocks."



Patrick Harbron

In the ensuing decades, Mr. Buffett added several large insurance companies, including General Re and Geico, a national auto-insurance company. He also bought an eclectic mix of manufacturing and retail

companies, from paint company Benjamin Moore & Co. to underwear maker Fruit of the Loom Inc.

After speaking with Mr. Freund that day, Mr. Buffett received calls from the chiefs of three Berkshire units. None of the conversations were lengthy. He spent most of the time listening, not advising. "A few of the [Berkshire] CEOs think if they talk to you, you'll tell them what to do," Mr. Buffett says. A prerequisite to a Berkshire purchase of any company is trusting that company's managers to make decisions, he says.

Around midday, a call came in from David Sokol, chief executive of Berkshire's MidAmerican Energy subsidiary. Mr. Buffett put his hands behind his head and cradled the phone against his shoulder, nodding when Mr. Sokol told him that MidAmerican had received a government approval for its pending acquisition of utility PacificCorp. for \$5.1 billion in cash, plus \$4.3 billion of assumed debt. Mr. Buffett, sipping a Coke from a Styrofoam cup, soon ended the conversation.

Mr. Buffett tends to stick to investments for the long haul, even when the going gets bumpy. Mr. Sokol recalls bracing for an August 2004 meeting at which he planned to break the news to Mr. Buffett that the Iowa utility needed to write off about \$360 million for a soured zinc project. Mr. Sokol says he was stunned by Mr. Buffett's response: "David, we all make mistakes." Their meeting lasted only 10 minutes.

"I would have fired me if I was him," Mr. Sokol says.

"If you don't make mistakes, you can't make decisions," Mr. Buffett says. "You can't dwell on them." Mr. Buffett notes that he has made "a lot bigger mistakes" himself than Mr. Sokol did.

That afternoon, Mr. Buffett phoned Ajit Jain, who runs the reinsurance business of National Indemnity. Hurricane Wilma was gaining force in the Gulf of Mexico. During the five-minute talk with Mr. Jain, conversation turned to Mr. Buffett's decision last year to slash Berkshire's exposure to "super cats," or catastrophic events. "If this year's hurricanes had happened last year, or two to three years ago [before Mr. Buffett cut the exposure], what percentage more would our losses have been?" Mr. Buffett asked Mr. Jain.

"One-hundred percent, worst case," Mr. Jain replied. Despite the reduced exposure, Berkshire has since reported net income of \$586 million in the third quarter, down 48% from the year-earlier period, due in part to about \$3 billion of hurricane-related losses.

Judgment calls such as Mr. Buffett's move to reduce hurricane exposure make his succession a difficult issue for Berkshire. Mr. Jain, 54, is believed to be one of the three candidates Mr. Buffett has recommended to the board to succeed him. In all likelihood, Mr. Buffett has said, his job will be split into three pieces: a CEO in charge of operations, a chief of investments and a chairman. Mr. Buffett declines to identify his candidate for the critical CEO position.

Succession has been a big topic of conversation of late at board meetings, directors say. "We delayed it until late and then devoted a lot of time to it," says Charles Munger, Berkshire's 81-year-old vice chairman and Mr. Buffett's closest associate.

"The chance of getting another Warren is zero," says Mr. Munger. Nevertheless, he brushes off concerns that Berkshire will suffer for it. He says it is likely Berkshire will continue to be run in a decentralized fashion "with enormous discretion in the subsidiary units and a hatred of bureaucracy." The three candidates

recommended by Mr. Buffett present Berkshire with "a number of good options," he says.

Mr. Buffett has allowed about \$40 billion of cash to accumulate at Berkshire because he hasn't found many attractive investments over the last couple of years. Some investors doubt that shareholders would stay patient if anyone other than Mr. Buffett had such a large cash horde, "especially when it is competing with so much hedge-fund money and mergers-and-acquisition activity these days," says Thomas Vandeventer, a portfolio manager at Citigroup Asset Management, which holds some Berkshire shares. Cash doesn't generate income, and some investors want their money fully invested.

It's unlikely that any successor would choose investments or acquisitions quite like Mr. Buffett does. He says he knows an attractive acquisition candidate when he sees it. "If I don't know it in five to 10 minutes," Mr. Buffett says, "then I'm not going to know it in 10 weeks."

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Corrections & Amplifications:

A conversation during late September between investor and insurance executive Warren Buffett and Ajit Jain, a manager of a Berkshire Hathaway Inc. subsidiary, happened on a day when Hurricane Rita was gaining force in the Gulf of Mexico. This article incorrectly identifies the storm as Hurricane Wilma. In addition, Bill Gates is chairman of Microsoft Corp. This article incorrectly identifies him as chief executive of Microsoft.

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