

Buffett Says Where to BUY – Excerpts from his 2011 newsletter.



Like most folks, Donald and Mildred Othmer blended right in with the woodwork.

In 45 years of marriage, they built the kind of quiet and unpretentious life like so many of their day...

Donald was a chemical engineering professor, while his wife was a former teacher and English major from the University of Nebraska. Outside of work, the two were as ordinary as it gets, never ones to be confused with the flashy types.

In fact the Othmers tended to be downright frugal. Friends often remarked they "lived comfortably but not ostentatiously, and rarely talked about their money." At times they even took in tenants, since they had the room to spare.

So needless to say, when both of them finally passed away in their nineties, it surprised everyone who knew them that all this time, they had been keeping company among the super-rich...

Behind the ordinary actually lay the extraordinary: The Othmers left behind a fortune worth \$800 million.

Their friends also weren't aware that an old family friend from Omaha had helped them along the way.

As it turns out, the couple from Brooklyn knew this young fellow named Warren Buffett — and in the early 1960s, they had entrusted him with \$25,000 each to invest.

The rest, I guess you could say, is history...

Over the years, they simply sat back and watched their money grow and grow and grow.

"They just rode along," Buffett said. "The investment never changed their lives."

As for that nice young upstart, I guess that's how they grow them in Omaha. Frugal as ever, Buffett still lives in the same house he bought three decades ago for \$31,500, and not long ago, drove a Lincoln Towncar with a license plate that read "THRIFTY".

But buried beneath that cuddly, down-home facade is something else entirely: a market shark if there ever was one. That's why when Warren speaks, people listen.

So every year when Berkshire Hathaway (NYSE: BRK-A) releases [Warren Buffett's Annual Letter to Shareholders](#), investors everywhere are eager to hear what the "Oracle of Omaha" has to say.

Here are a few of the highlights from this year's addition...

Warren Buffett on the housing bust:

Our businesses related to home construction, however, continue to struggle. Johns Manville, MiTek, Shaw and Acme Brick have maintained their competitive positions, but their profits are far below the levels of a few years ago.

Combined, these operations earned \$362 million pre-tax in 2010 compared to \$1.3 billion in 2006, and their employment has fallen by about 9,400. A housing recovery will probably begin within a year or so.

Warren Buffett on mortgage finance:

If home buyers throughout the country had behaved like our buyers, America would not have had the crisis that it did. Our approach was simply to get a meaningful down-payment and gear fixed monthly payments to a sensible percentage of income. This policy kept Clayton solvent and also kept buyers in their homes.

But a house can be a nightmare if the buyer's eyes are bigger than his wallet and if a lender — often protected by a government guarantee — facilitates his fantasy. Our country's social goal should not be to put families into the house of their dreams, but rather to put them into a house they can afford.

Warren Buffett on the value of dividend paying stocks:

Other companies we hold are likely to increase their dividends as well. Coca-Cola paid us \$88 million in 1995, the year after we finished purchasing the stock. Every year since, Coke has increased its dividend. In 2011, we will almost certainly receive \$376 million from Coke, up \$24 million from last year.

Within ten years, I would expect that \$376 million to double. By the end of that period, I wouldn't be surprised to see our share of Coke's annual earnings exceed 100% of what we paid for the investment. Time is the friend of the wonderful business.

Warren Buffett on Railroads:

The highlight of 2010 was our acquisition of Burlington Northern Santa Fe, a purchase that's working out even better than I expected. It now appears that owning this railroad will increase Berkshire's 'normal' earning power by nearly 40% pre-tax and by well over 30% after-tax.

Both of us are enthusiastic about BNSF's future because railroads have major cost and environmental advantages over trucking, their main competitor. Last year BNSF moved each ton of freight it carried a record 500 miles on a single gallon of diesel fuel. That's three times more fuel-efficient than trucking is, which means our railroad owns an important advantage in operating costs.

Warren Buffett on Hedge Funds:

The hedge-fund world has witnessed some terrible behavior by general partners who have received huge payouts on the upside and who then, when bad results occurred, have walked away rich, with their limited partners losing back their earlier gains.

Sometimes these same general partners thereafter quickly started another fund so that they could immediately participate in future profits without having to overcome their past losses. Investors who put money with such managers should be labeled patsies, not partners.

Warren Buffett On leverage:

Unquestionably, some people have become very rich through the use of borrowed money. However, that's also been a way to get very poor. When leverage works, it magnifies your gains. Your spouse thinks you're clever, and your neighbors get envious. But leverage is addictive. Once having profited from its wonders, very few people retreat to more conservative practices. And as we all learned in third grade — and some relearned in 2008 — any series of positive numbers, however impressive the numbers may be, evaporates when multiplied by a single zero.

Warren Buffett on the importance of credit:

Leverage, of course, can be lethal to businesses as well. Companies with large debts often assume that these obligations can be refinanced as they mature. That assumption is usually valid. Occasionally, though, either because of company-specific problems or a worldwide shortage of credit, maturities must actually be met by payment. For that, only cash will do the job.

Borrowers then learn that credit is like oxygen. When either is abundant, its presence goes unnoticed. When either is missing, that's all that is noticed. Even a short absence of credit can bring a company to its knees.

As for whether or not he is bullish or bearish, the man who built the Othmers' personal fortune still carries with him an unshakable belief in the promise of America.

"Money," Buffett calmly asserts, "will always flow toward opportunity, and there is an abundance of that in America. Now, as in 1776, 1861, 1932 and 1941, America's best days lie ahead."