

An Analysis of Berkshire Hathaway: Our Favorite Stock and Largest Position

T2 Partners LLC

**T2 Accredited Fund, LP
Tilson Offshore Fund, Ltd.
T2 Qualified Fund, LP**

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This presentation is available at <http://www.tilsonfunds.com/BRK.pdf>

The article that accompanies this presentation is available at:

<http://seekingalpha.com/article/107153-berkshire-hathaway-credit-risk-index-puts-are-overblown-worries>

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Berkshire Hathaway: A High-Quality, Rapidly Growing 65-Cent Dollar

History

- Berkshire Hathaway today does not resemble the company that Buffett bought into during the 1960s
- Berkshire was a leading New England-based textile company, with investment appeal as a classic Ben Graham-style “net-net”
- Buffett took control of Berkshire on May 10, 1965
- At that time, Berkshire had a market value of about \$18 million and shareholder's equity of about \$22 million

The Berkshire Hathaway Empire Today

GEICO

Gen Re

FlightSafety
international

MI
MiTek

You could
save
15%
Let's get started

See's
CANDIES

BORSHEIM'S
Fine Jewelry and Gifts
A Berkshire Hathaway Company

NETJETS

THE COMPANY THAT CREATED
THE FRACTIONAL INDUSTRY

6 Largest Stakes in
Public Companies

The Coca-Cola Company

AMERICAN
EXPRESS

WELLS
FARGO



Jordan's
FURNITURE

Shaw Where Great Floors Begin

P&G



Moody's Investors Service

BNSF
RAILWAY

Garanimals

Nebraska
Furniture Mart

KIRBY

DQ

GINSU

THE BUFFALO NEWS

JM Johns Manville



Benjamin Moore Paints



The Pampered Chef
thanks for 25 years

FRUIT OF THE LOOM

McLane

Member IMC Group
ICF

Justin
BOOTS

ACME
BRICK
Since 1891

The Basics

- Stock price (11/21/08): \$90,000
 - \$2,914 for B shares
- Shares outstanding: 1.55 million
- Market cap (10/19/08): \$140 billion
- Total assets (Q3 '08): \$282 billion
- Total equity (Q3 '08): \$120 billion (\$111 billion of as of the end of October)
- Book value per share (Q3 '08): \$77,519

Recent Performance of Key Business Units

By Year:

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
<u>Insurance Group:</u>				
Premiums Earned				
GEICO	970	1,221	1,314	1,113
General Re	3	-334	523	555
Berkshire Reinsurance Group	417	-1,069	1,658	1,427
Berkshire H. Primary Group	161	235	340	279
Investment Income	<u>2,824</u>	<u>3,480</u>	<u>4,316</u>	<u>4,758</u>
Total Insurance Oper. Inc.	4,375	3,533	8,151	8,132
<u>Non-Insurance Businesses:</u>				
Finance and Financial products	584	822	1,157	1,006
McLane Company	228	217	229	232
Shaw Industries	466	485	594	436
MidAmerican/Utilities/Energy	237	523	1,476	1,774
Other businesses	<u>1,787</u>	<u>1,921</u>	<u>2,703</u>	<u>3,279</u>
Total Non-Insur. Oper. Inc.	3,302	3,968	6,159	6,727
Total Operating Income	7,677	7,501	14,310	14,859

Recent Performance of Key Business Units

By Quarter:

	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>	<u>Q4</u>	<u>Q1</u>	<u>Q2</u>	<u>Q3</u>
<u>Insurance Group:</u>	<u>2005</u>	<u>2005</u>	<u>2005</u>	<u>2005</u>	<u>2006</u>	<u>2006</u>	<u>2006</u>	<u>2006</u>	<u>2007</u>	<u>2007</u>	<u>2007</u>	<u>2007</u>	<u>2008</u>	<u>2008</u>	<u>2008</u>
Premiums Earned															
GEICO	312	358	237	314	311	288	407	308	295	325	335	158	186	298	246
General Re	19	43	-389	-7	71	106	177	169	30	230	157	138	42	102	54
Berkshire Reinsurance Group	143	140	-1,635	283	94	137	735	692	553	356	183	335	29	79	-166
Berkshire H. Primary Group	18	37	-10	190	35	43	108	154	49	63	77	90	25	81	-8
Investment Income	<u>787</u>	<u>851</u>	<u>900</u>	<u>942</u>	<u>1,018</u>	<u>1,102</u>	<u>1,103</u>	<u>1,093</u>	<u>1,078</u>	<u>1,236</u>	<u>1,217</u>	<u>1,227</u>	<u>1,089</u>	<u>1,204</u>	<u>1,074</u>
Total Insurance Oper. Inc.	1,279	1,429	-897	1,722	1,529	1,676	2,530	2,416	2,005	2,210	1,969	1,948	1,371	1,764	1,200
<u>Non-Insurance Businesses:</u>															
Finance and Financial products	199	199	207	217	251	343	282	281	242	277	273	214	241	254	163
Marmon													28	261	247
McLane Company	69	59	53	36	55	56	50	68	58	72	50	52	73	68	68
MidAmerican/Utilities/Energy	141	100	141	141	418	278	416	364	513	372	481	408	516	329	526
Shaw Industries	88	139	145	113	155	169	138	132	91	111	125	109	51	82	49
Other businesses	<u>364</u>	<u>514</u>	<u>486</u>	<u>557</u>	<u>430</u>	<u>671</u>	<u>686</u>	<u>916</u>	<u>632</u>	<u>904</u>	<u>895</u>	<u>848</u>	<u>721</u>	<u>874</u>	<u>749</u>
Total Non-Insur. Oper. Inc.	861	1,011	1,032	1,064	1,309	1,517	1,572	1,761	1,536	1,736	1,824	1,631	1,630	1,868	1,802
Total Operating Income	2,140	2,440	135	2,786	2,838	3,193	4,102	4,177	3,541	3,946	3,793	3,579	3,001	3,632	3,002

The Earnings of Berkshire's Operating Businesses Have Grown at a Very High Rate – And Growth is Accelerating

<u>Year</u>	<u>Per-Share Investments</u>	<u>CAGR</u>	<u>Per-Share Pre-Tax Earnings</u>	<u>CAGR</u>
1965	\$4		\$4	
1979	\$577	42.8%	\$18	11.1%
1993	\$13,961	25.6%	\$212	19.1%
2007	\$90,343	14.3%	\$4,093	23.5%

Berkshire is becoming less of an investment company and more of an operating business.

Note: CAGR: 1965-1979, 1979-1993, 1993-2007. EPS is pretax and net of minority interests.

Berkshire Is One of the Fastest Growing Large Companies in the World

<u>Company</u>	<u>Market Cap</u>	<u>Growth Rate*</u>
Exxon Mobil	\$413,495	22.5
General Electric	\$264,817	9.2
Wal-Mart Stores	\$234,858	10.5
Microsoft	\$229,718	20.2
Berkshire Hathaway	\$227,729	30.5
Procter & Gamble	\$211,072	16.8
Petroleo Brasileiro	\$207,595	16.0
Johnson & Johnson	\$195,587	9.4
BHP Billiton	\$186,523	49.4
Chevron	\$180,383	25.5
AT&T	\$179,324	24.1
IBM	\$161,023	8.6
Cisco	\$142,899	14.1
Pfizer	\$125,045	5.1
Coca-Cola	\$121,862	8.3
ConocoPhillips	\$119,016	30.8
Hewlett-Packard	\$118,194	23.9
Pepsico	\$114,581	11.0
GlaxoSmithKline	\$114,209	4.9
Schlumberger	\$108,815	40.0
Intel	\$108,111	14.3
Oracle	\$103,602	19.1
Genentech	\$97,405	49.1
Verizon	\$94,830	1.2
Abbott Laboratories	\$90,504	6.8

* 5-year compound annual growth rate of EBIT (earnings before interest and taxes) through Q3 07. Berkshire's figure is pre-tax EPS excluding all income from investments.

Source: Capital IQ

Valuing Berkshire

“Over the years we've...attempt[ed] to increase our marketable investments in wonderful businesses, while simultaneously trying to buy similar businesses in their entirety.” – 1995 Annual Letter

“In our last two annual reports, we furnished you a table that Charlie and I believe is central to estimating Berkshire's intrinsic value. In the updated version of that table, which follows, we trace our two key components of value. The first column lists our per-share ownership of investments (including cash and equivalents) and the second column shows our per-share earnings from Berkshire's operating businesses before taxes and purchase-accounting adjustments, but after all interest and corporate expenses. The second column excludes all dividends, interest and capital gains that we realized from the investments presented in the first column.” – 1997 Annual Letter

<u>Year</u>	<u>Investments Per Share</u>	<u>Pre-tax Earnings Per Share Excluding All Income from Investments</u>
1967	\$ 41	\$ 1.09
1977	372	12.44
1987	3,910	108.14
1997	38,043	717.82

“In effect, the columns show what Berkshire would look like were it split into two parts, with one entity holding our investments and the other operating all of our businesses and bearing all corporate costs.” – 1997 Annual Letter

Buffett's Comments on Berkshire's Valuation Lead to an Implied Multiplier of Approximately 12

<u>Year</u>	<u>Investments</u> <u>Per Share</u>	<u>Pre-tax EPS</u>		<u>Intrinsic</u> <u>Value</u>	<u>Implied</u> <u>Multiplier</u>
		<u>Excluding All</u> <u>Income From</u> <u>Investments</u>	<u>Year-End</u> <u>Stock</u> <u>Price</u>		
1996	\$28,500	\$421	\$34,100	\$34,100	13
1997	\$38,043	\$718	\$46,000	\$46,000	11
1998	\$47,647	\$474	\$70,000	\$54,000	13
1999	\$47,339	-\$458	\$56,100	\$60,000	

- 1996 Annual Letter: "Today's price/value relationship is both much different from what it was a year ago and, as Charlie and I see it, more appropriate."
- 1997 Annual Letter: "Berkshire's intrinsic value grew at nearly the same pace as book value" (book +34.1%)
- 1998 Annual Letter: "Though Berkshire's intrinsic value grew very substantially in 1998, the gain fell well short of the 48.3% recorded for book value." (Assume a 15-20% increase in intrinsic value.)
- 1999 Annual Letter: "A repurchase of, say, 2% of a company's shares at a 25% discount from per-share intrinsic value...We will not repurchase shares unless we believe Berkshire stock is selling well below intrinsic value, conservatively calculated...Recently, when the A shares fell below \$45,000, we considered making repurchases."

Applying the 12 Multiple: 2001 – November 2008

<u>Year End</u>	<u>Investments Per Share</u>	<u>Pre-tax EPS Excluding All Income From Investments¹</u>	<u>Intrinsic Value Per Share</u>	<u>Subsequent Year Stock Price Range</u>
2001	\$47,460	-\$1,289	\$64,000	\$59,600-\$78,500
2002	\$52,507	\$1,479	\$70,000	\$60,600-\$84,700
2003	\$62,273	\$2,912	\$97,000	\$81,000-\$95,700
2004	\$66,967	\$3,003	\$103,000	\$78,800-\$92,000
2005	\$74,129	\$3,600	\$117,300	\$85,700-\$114,200
2006	\$80,636	\$5,200-\$5,400 ²	\$143,000-\$144,400	\$107,200-\$151,650
2007	\$90,343	\$5,500-\$5,700 ³	\$156,300-\$158,700	\$84,000-\$147,000
11/19/08	\$76,000 ⁴	\$5,000 ⁵	\$136,000	?

1. Unlike the table on page 4 of the 2007 Annual Report, we include earnings from Berkshire's insurance businesses.
2. Actual result was \$6,492, but we reduce this to assume the 2nd-worst year ever for super-cat losses.
3. Actual result was \$6,270 but we reduce the pre-tax, pre-investment-income margins of the insurance businesses by 400 basis points (from 14% to 10%) to reflect Buffett's guidance in the Annual Report.
4. Investments per share was \$86,000 as of Q3, but we estimate a \$10,000/share impact due to market declines in October and the first few weeks of November.
5. We have trimmed our estimate of normalized earnings to reflect the weak economy.

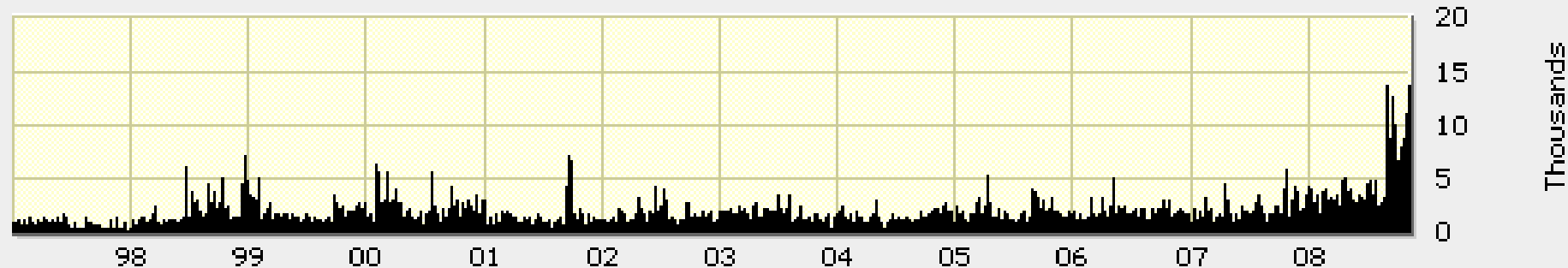
Berkshire Is Approximately 35% Below Intrinsic Value, By Far the Most Undervalued It's Been in the Past 12 Years

BRKA Weekly



Volume

©BigCharts.com



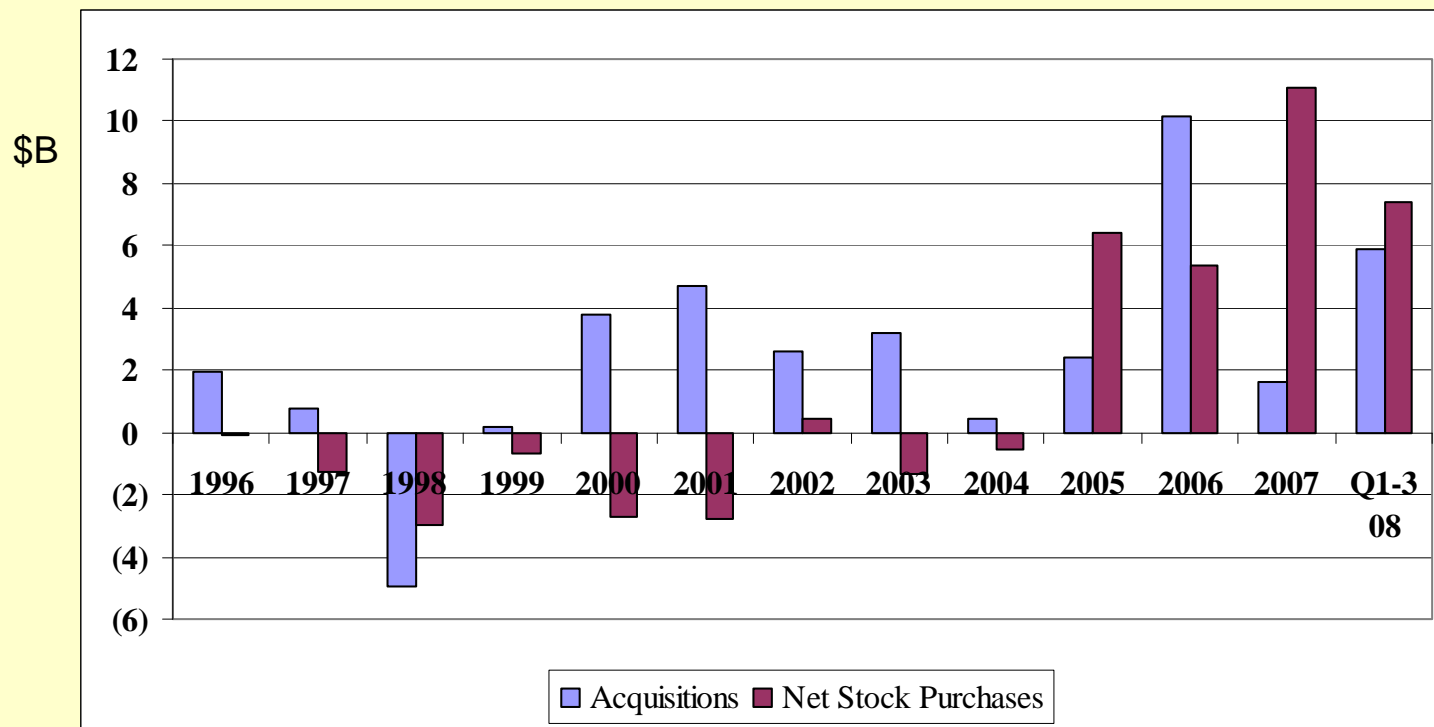
* Investments per share plus 12x pre-tax earnings per share (excluding all income from investments) for the prior year.

Valuation Approach #2: Pro-Forma Earnings

- Market cap: \$140B
- 2007 company earnings: approximately \$11.5B
 - adjusted for normal super-cat losses and pricing, and for unusually high capital gains in 2007
- Plus 2007 estimated look-through after-tax earnings after cash distributions: \$2.2B
- Equals total pro-forma earnings of \$13.7B
- P/E: $\$140\text{B} / \$13.7\text{B} = 10.2\text{x}$

Buffett Is Putting Berkshire's Money to Work Rapidly

We estimate that Berkshire has made more than \$50 billion in commitments this year, only a fraction of which appears on the Q3 cash flow statement



- He's doing a good job – but the cash is coming in so fast!
 - A high-class problem
- Markets have a way of presenting big opportunities on short notice
 - Current chaos, junk bonds in 2002
 - Buffett has reduced average maturity of bond portfolio so he can act quickly

12-Month Investment Return

- Current intrinsic value: \$136,000/share
- Plus 10% growth of intrinsic value of the business
- Plus cash build over next 12 months: \$5,000/share
- Equals intrinsic value in one year of \$154,600
- 72% above today's price

Catalysts

- Continued earnings growth of operating businesses
- New equity investments
- Additional cash build
- Potential for more meaningful acquisitions and investments
 - If the credit crunch continues or worsens, this becomes more likely

Risks

- Major recession impacts earnings
- Recent investments turn out badly
- No catalysts
 - Intrinsic value will likely continue to grow nicely
- Buffett's health
 - In good health; turned 78 last Aug. 30th
 - Strong board and succession plan in place
 - Little Buffett premium in stock today
- Major super-cats
- Can't find place to invest cash
 - Not a problem currently
 - There are worse things than sitting on a lot of cash
 - Buffett has said Berkshire will distribute cash if he doesn't think he can allocate it

Conclusion

- Cheap stock: 65-cent dollar, giving no value to recent investments and immense optionality
- Extremely safe: huge cash and other assets provide downside protection