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The Warren & Charlie Show--2006

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I was in Omaha on Saturday to attend Berkshire Hathaway's annual shareholders' meeting at the Qwest Center there. As they do every year, CEO Warren Buffett and Vice Chairman Charlie Munger spent the bulk of the session answering questions from shareholders. Here are my notes from the gathering:

WB: Yesterday we announced the acquisition of Iscar, a large, well-managed, profitable business. I got a page-and-a-half letter from Eitan Wertheimer, the Chairman, that told me about their business. The character and talent of management jumped off the page. Soon after, we met management in Omaha. Charlie liked them a lot. This is one deal where Charlie's as enthusiastic as I am. We signed the contract yesterday.

CM: From very modest beginnings this company has become the best company in its field. It's not the biggest—yet. The average quality of the people who run it is off the charts. And they're young.

This is a very high-quality enterprise. Its people know how to do things that no one else knows how to do. We always like having the opportunity to work with some of the best people in the world.

WB: Iscar is the second-largest cutting-tool manufacturer in the world. It has revolutionized every aspect of machining. It has operations all over the world. We paid $4 billion for 80%. The family will keep the other 20%.

This is the first time we've bought a business that's based outside the U.S.

CM: We'll look back in 5 to 10 years and see this as a significant event in Berkshire's history.

WB: We hear from people all the time who think their businesses are too important to auction. We don't do auctions, generally.

We tend to buy from people who care enough about their businesses that they don't want to put them up for auction as if they were pieces of meat. This is a very useful filter for us. There's something going on in their brains; they care about their customers and employees. This works to our advantage. Our crowning acquisition along this line is Iscar. I'm going to Israel in September to try to find more companies like it.

Where should a rich country like the U.S. draw the line on entitlements?

WB: Every society decides what to do with its oldest and youngest members. They are its least productive members; they don't turn out goods and services, but consume them. In 1935, the country decided that the federal government should play a role in helping to take care of older citizens, when it enacted the Social Security program. There is some merit in the idea that 65 is too low a retirement age. That's in the process of being changed. But in a society as wealthy as ours, where GDP per capita is $40,000, there are plenty of resources to use to help support older people. Not everyone needs help. Some people, like Charlie and me, have been wired to be able to make money. Those people will have more than enough to provide for themselves as long as they live. But not everyone is wired that way. They won't be able to take care of themselves once they stop working. The country is wealthy enough that it can easily handle the Social Security question.

I find it ironic that this administration, which thinks nothing of running up fiscal deficits of $300 billion to $400 billion per year, is so concerned about the idea that Social Security could have a $100 billion deficit several years from now.

It's true that the ratio of workers to retirees is only 2 to 1. But worker productivity is going up every year. There's always been a struggle over how to divvie up the wealth pie. But that pie is big, and it's growing. This is a problem that the country can easily take care of.

CM: I've read the evidence put together by people like Pete Peterson, but have come to a different conclusion. If the country grows in real terms by 2% to 3% per year, it should be child's play to take a share of that pie and divert it to older people. It's crazy to freeze the share of wealth devoted to retirees at some arbitrary level set sometime in the past. The society has a responsibility to pay a little more than it has in the past, as the population of retirees grows. Social Security is one of the most successful programs in the history of the country. It is very efficient and has low overhead.

WB: The government had no reluctance counting the Social Security surplus as part of the overall fiscal surplus, when the budget was first unified in 1969. But now that the trust fund is set to go into deficit, suddenly the system has pay for itself.

What's the best way to design a compensation system in a highly cyclical industry, such as oil, that's prone to booms and busts, without avoiding overpaying people in the good times, and underpaying them during the bad ones?

WB: That's a terrific question. If you're a copper company and copper's at $3.50 a pound the way it is now, even the village idiot could run it and you'll make money. But once copper prices go down, it's a tough business. We design different compensation systems at Berkshire for the different businesses. Some of our businesses are very capital intensive. Some of our companies are in tough businesses. Some run themselves. So we have a wide variety of compensation systems. Often people have standardized systems, regardless of what business a company's in. That's crazy.

If we owned a copper company, we'd measure management's effectiveness by looking at the business's cost of production--not the price of copper. Management has control of operating conditions, not market prices. So management's comp wouldn't fluctuate a lot, even though the unit’s results might fluctuate a lot.

Tie compensation to what management can control and have an impact on. At Geico, for instance, we look at growth and profitability of seasoned business. (New business loses money for awhile.) Don't pay for the wrong things, or for what management can't control. I think it's ironic that energy executives are being paid well recently as oil prices have gone up, but then go up and testify before Congress that they don't have anything to do with high energy prices. Energy companies should pay management based on finding costs. If a company can achieve and maintain lower-than-average unit finding costs over an extended period, say 3 to 5 years, then management should be paid well.

CM: It's easy to have a fair compensation system. In about half of public companies, the top people are paid too much. Berkshire can't influence what other companies pay their executives, however.

WB: Berkshire owns 68 operating companies. I have responsibility for determining the comp of around 40 managers. I can't think of anyone we've lost due to differing views on compensation. We've never brought in compensation consultants. Maybe they have at the subsidiaries. (But if they have, they're smart enough to not tell me.) This is not rocket science. It's not something we spend a lot of time on. Complexity serves the needs of those who have their hands on the switch, such as the consultant or the compensation committee.

CM: We don't do well when we sit on comp committees. At Salomon Brothers, Warren was on the comp committee. When he remonstrated softly regarding how much some people were paid, he was outvoted. I think a lot of this isn't driven by greed, but rather by envy. Pay a guy $2 million, and he's happy--until he learns that the next guy got $2.1 million. Then he's miserable.

WB: I've always believed that of all the seven deadly sin, envy is the silliest. When you're envious, you're making yourself miserable. At least with the other deadly sins, you're enjoying yourself. Some of the best times I've ever had have come during sustained rounds of gluttony. And I won't even get into lust. But when you're envious, you feel miserable.

This new proposal by the S.E.C. for more full and transparent disclosure of executive comp is a good idea. But I'm afraid it could be counterproductive when executives see the full list of what other people are getting. It becomes a shopping list.

How do you train your successors and measure their effectiveness?

WB: We write the annual shareholder letter to convey what Berkshire is all about. This meeting, too, is intended to convey the company's culture. We're not saying we do things better, but rather that this is us. We want our people to have a lifetime commitment to their businesses, and to underscore the values we have. Everything we do we want to be consistent with Berkshire's culture. Everything they see, hear, and read from the company should be consistent. It's just like children in a home. They see what the grown-ups do and how they act, and learn to act the same way. Homes have cultures. Companies have cultures. Countries have cultures. At Berkshire, people buy into it and see that it works. This kind of thing doesn't require mentoring. Managers see consistency in how Charlie and I act.

Not everyone buys it. I have a guy coming in to meet with me shortly. I know nothing will come of it, because his brain works differently; he wouldn't buy in to the way we do things here. So it's very unlikely we'll do a deal. But I want to learn about his business, so I'll meet with him.

But there's no formal training needed for successors. If I die tonight, there are three obvious candidates to be my successor. Any of the three would not miss a beat if they took over. It's their culture too.

CM: Warren has kept the faith for 75 years. Does anyone think he will blow the job of passing that faith on? You all have more important things to worry about than that. That faith will go on for a long time. We don't train executives here. We find them--and they're not that hard to find.

A number of closed-end country funds are currently trading at premiums to their NAVs. Is that rational?

WB: A premium on a closed-end fund tends to be irrational. I haven't looked at pricing on closed-end country funds recently, and so can't speak to this instance directly. But most go to discounts once they've been priced. For one thing, the commission, usually 6%, comes out of the price right away. Investors who buy on the deal end up paying $1 for 94 cents of assets. If I had an interest in buying into an emerging market, and a fund that invested in that market were trading at, say, 1.2 times NAV, you'd have to convince me that the manager of the fund is truly superior to get me to buy it. But the premiums can be huge. I've seen premiums of 30%-40% or more. Years ago Overseas Securities sold at a huge premium, and everyone was baffled. But eventually the prices come down to earth.

Do you think the trend toward majority voting for directors, away from plurality voting, will help governance?

CM: I don't believe it will improve ethics at all. From time to time different fashions pop up in corporate governance, and this is one of them. But they don't fix governance problems. New governance rules need to be considered in light of who'll be activist in using their new powers. On most boards, it's a mixed lot, at best.

WB: The quality of a company's governance is determined by whether the people on the board truly think like owners, and whether or not they're any good at overseeing a business. I haven't seen any changes in behavior based on switches to majority voting. The big difference in whether a board is effective or not is whether or not the people in the board room have a lot of business savvy. I'm not sure a certain rule or other will make a big difference. The board's job is to get the right CEO, and prevent him overreacting to problems and issues. Also, a board needs to exercise independent judgment on important acquisitions. Many CEOs are motivated by non-rational reasons when they consider doing big deals.

The only cure for bad governance is to have the largest shareholders, say the 8-10 largest, make sure that these issues are addressed. So if they don't like a comp plan, for instance, they tell the company, "this comp plan is no good, and we're not going to vote to re-elect the directors." Yet some big holders actually farm out their voting decisions to outsiders. I don't understand it. You want board members, and large holders, to think like owners.

What have you learned about technology investing?

WB: I know enough about tech to know that I don't know very much about tech. We know our circle of competence; we know what sorts of businesses we understand. There are some businesses that no one can understand. They change too fast. We like to bet on businesses that will be basically the same in 5 to 10 years as they are now. Iscar will be bigger in 5 to 10 years, but its fundamentals won't be any different. The telecom business has been through startling change over the past 5 to 10 years.

Charlie says that we have three boxes: "In," "Out," and "Too Hard." It doesn't bother us if we have to put something in the "Too Hard" box. If you make it to the Olympics as a sprinter, why should you worry that you didn't make it as a javelin thrower? Tom Watson, Sr. used to say, "I'm no genius, but I'm smart in spots—and I stay around those spots." You don't want to compete with Pete Liegl at Forest River. He'll kill you. But Pete doesn't try to tell us how to run the insurance business.

It's not that I haven't been exposed to technology. I was present at the birth of Intel. I was on the board of Grinnell with Bob Noyes. But I don't think anyone in the industry has a clue how to forecast the future of the business. At Intel they've had some surprises lately. AMD's recent success has been a surprise. I don't think in that industry you can tell what's going to happen. It's very hard to predict.

CM: A reporter once asked me, "How is that you've had such success running a multi-industry company? You're not smart enough to have done so much better." We know the edge of our competence better than most people. It's not a competence if you don't know the edge of it.

Which would you prefer to own: 1 share of median family income (which has been stagnant for 30 years), 1 share of all corporate income (which is lately a very high percentage of GDP), or 1 share of all corporate assets (even intangibles)?

WB: I'd rather buy Iscar. It's true that corporate profits as a portion of GDP is near a historical high. But corporate income taxes aren't so high. I'm not shooting to achieve median family income. The tax breaks for the wealthy that have been enacted are extraordinary. Most members of the *Forbes* 400 pay a lower portion of their income in taxes than the receptionist on our office does. That wasn't true 30 years ago—and it should not be true in a rich society. In 2004, my tax rate was the lowest of anyone among the 15 or 16 people who work in our office. And that wasn't because of any tax shelters I invested in (I don't own any tax shelters) or any special tax advice I got. It's crazy.

The media hasn't conveyed the extent to which the typical individual hasn't shared in the prosperity of the past 10 years as much as the wealthy have.

CM: I'm not as concerned about the levels of median family income. The important issue is how fast GDP per capita growing. People's economic status will change over time, and will move up and down deciles. The most important thing is that the pie grows. Some changes in the tax system have been crazy. But I don't think they've been all that important one way or the other in determining the rate of growth.

What do you think of investing in ethanol?

WB: Charlie and I don't know enough to figure out what the return on capital of an ethanol-related investment might be over the next 5 or 10 years. It's easier to predict how many people will be drinking Coke or eating candy. I don't know anything about the government regulation of ethanol production and use and how that might change. But I know it's easy to raise money for ethanol-related investments lately. It's a hot area. That's usually not a good sign. My son is the head of the ethanol board for the state of Nebraska. If he starts getting richer than I am, then I'll be interested. There's no question interest in ethanol will grow. But ag processing businesses tend to have low returns on capital. I don't see how you gain a big competitive advantage.

CM: I'm more hostile. It takes more fossil energy to create the ethanol than the ethanol itself will create. It's a stupid way to create energy.

Are we in a commodities bubble?

Energy, oil, and metals have all seen terrific moves. Copper may have had the biggest. The start of most trends is driven by the fundamentals of supply and demand, but then speculation takes over. People have been watching the fundamentals of commodities for years. There's an old saying, "What wise men do in the beginning, fools do in the end." Any move that starts with fundamentals will sooner or later draw speculators, and eventually the speculators will dominate. Probably the best known example is the tulip craze of the 1600s.

Once a move starts, people get envious. My guess is that we've seen some speculative activity in the commodity area, and in housing, too. How far it will go—who knows? My guess is that a lot of the activity on both sides of the commodity market is speculative.

CM: To get a sense of how little we know about commodities, look at our operations in silver.

WB: Right. We bought early and sold early—otherwise it was perfect. We're not good at figuring out how far booms will go. If we get the fundamentals right, we'll make some money. Booms tend to get wildest at the end. People gather around the punch bowl and it gets later and later, and all the girls look prettier. But at midnight everything turns to pumpkins and mice again. But everyone plans to be out before midnight. The problem, as Adam Smith (Jerry Goodman), has pointed out, is that during the party, there are no clocks on the wall. We saw it with the Internet stocks. We saw it with the uranium stocks in the 1950s. There were no clocks on the wall.

Do you see investment opportunities in South America?

WB: The problem that we have with emerging markets is that, because we're so big, we have to be able to put a lot of money to work to move the needle. The opportunity has to be at least several hundred million dollars. So that narrows the field of what we can look at. We invested in PetroChina 5 years ago. We could only invest $400 million. That's worth a few billion now. We weren't afraid to go into China. We wanted to be paid more than we'd earn in the U.S., because we didn't know the game. There's a terrific brewer in Brazil that I should have invested in. But opportunities in emerging markets have to be cheaper than opportunities in the U.S., because we don't know the tax laws as well, and we aren't familiar with the nuances of government regulation.

What is the outlook for manufactured housing?

WB: The manufactured housing business has an interesting history. Volume is lower now than it was 30 or 40 years ago—and quality is higher. Some years back then, 1 out of 5 houses built was a manufactured home. Last year 130,000 manufactured homes were constructed (ex FEMA-related construction), or around 6% or 7% of total home construction. You can install a manufactured home for $45 per square foot. There's a lot of resistance to manufactured housing via restrictive zoning laws in many locations, spurred by local builders. But in many areas, developers are building entire subdivisions of manufactured homes.

The industry got into a problem a few years back because manufactured homes were being mis-sold. Retailers would sell against a down payment. The buyer would take out a long-term loan and the loans were securitized and sold to investors, usually insurance companies. There was an abuse of credit. Manufactured homes should be financed on shorter terms than was the case. It's a mistake to finance a manufactured home with a 30-year loan, unless the borrower owns the land under the home. The industry is slowly working through its hangover. I believe the market will get bigger—but not this year.

The number of retailers and manufacturers has fallen, too. Clayton has a much better record than the rest of the industry does.

CM: One of the problems for manufactured-home makers is that builders of stick-built houses have become much more efficient. One of the reasons for that is efficiency-enhancing products made by companies like MiTek. But the manufactured housing business will get better, and will take more share of the market.

WB: Some day, the industry will deliver 200,000 units per year, but not in the next year or two. The industry has to think through how to finance its sales so that, after 5 to 10 years, the buyer has an asset that's worth more than the loan that's financed it. It can't just make loans and sell them to Wall Street. Clayton could be the biggest homebuilder in the U.S. in a few years.

Some of the sins of manufactured-home finance have shifted to stick-built-home finance. There's a lot of ridiculous credit in loans being made lately. My guess is that there will be trouble in the stick-built finance area. Dumb lending always has its consequences. It's like an epidemic in which no symptoms appear for years. Then when they finally do appear they are severe. What's going on now is like what happened in commercial finance in the late 1980s and early 1990s. A developer will develop anything, if someone gives him the money to.

We saw it in commercial real estate finance. We saw it in manufactured-housing finance. I think that's what's happening in residential real estate finance. If you go through the Qs and Ks of residential lenders and look at the balances of interest accrued but not paid, the numbers are big.

CM: A lot of this is being facilitated by contemptible accounting.

What needs to happen in Russia for you to consider investing there?

WB: Walter Wriston once said that sovereign governments don't default. We found out in 1998 that they do. We inherited some energy-related assets in Russian, via Salomon Brothers, a number of years ago. The authorities were happy to let us invest when we were drilling the holes. But when the time came to take the oil out, they weren't so crazy about us being investors. It might be awhile before we invest there again. Maybe things have changed, but I'm not sure. Three years ago, I had breakfast with Khodorkovsky, when he was considering listing Yukos on the NYSE. Now he's in jail and the company is in bankruptcy. It's hard to develop confidence that the Russia changed much in its view of capitalism and outside capitalists. At one point, we were concerned about the lives of our people there. When we went to pull the equipment out of the country, we got word that if we tried to pull the equipment out, not only would we not get the equipment, we wouldn't get the people out, either.

What do you think about the residential real estate market?

WB: Well, I invested in some property in California once, and after 20 years I got my money back—with interest! When we developed the property we were cashing out on a piece of land and got $5 million or $6 million. Now it's worth at least $100 million. It's a great piece. Terrific climate, wonderful location, on the water. But even in great locations, the swings in value can be huge. What we're seeing in our residential brokerage business is a slowdown just about everywhere. The markets that had been the hottest are slowing the most, especially at the high end, and in markets where people had been buying houses for speculation, rather than to live in.

In areas where spec buying was low, any cooling shouldn't be too severe. If somebody takes out a $270,000 mortgage to buy a house for $300,000, he's not going to sell it and move out if its value falls to $250,000. For investment-type holders, it may be a different story.

There's a tendency for seller to think about the house down the street that went for a big price. Or to convince himself that he just needs that one buyer to come in.

In Dade and Broward counties in Florida, the average condo is worth $500,000. Not long ago, there'd be 9,000 units on the market at any given time, and around 2,400 would sell per month. So the available inventory would turn over every four moths or so. Now there are 30,000 units on the market--$15 billion worth—and just 2,000 selling per month. We have had a bubble in residential real estate to some degree. I think there will be downward pressure in price, especially on higher-end properties. In Omaha, prices are OK.

The housing boom has been great for our home furnishings retailers. In 1997, the Nebraska Furniture Mart did $5.5 million in sales on annual meeting weekend. That rose to $17 million by 2003, and $27 million in 2004. This year NFM is on track to do $30 million. That's equivalent to a normal month.

Shouldn't you either find something to invest in with Berkshire's $40 billion, or think about giving it to shareholders?

WB: We're too big to hit any home runs with the cash. We had $37 billion at the end of March. For us, a "normal" level of cash is around $10 billion. We need to keep some liquidity because of the cat business. We spent $4 billion on Iscar. We'd be happy to just have $10 billion in cash, and to put the rest to work. I'm looking at one idea now, that's low probability, that could take $15 billion. Whether it comes to fruition, who knows. But if I don't like holding a lot of cash, I like doing dumb deals even less. They're forever. You don't want to go out and make an investment for its own sake. It's likely (but not certain) that within three years we'll have significantly less cash. You're right to keep jabbing at us, though. Neither of us likes cash. People come to us because they know we're so liquid. But we don't need to be *this* liquid. We'll get more chances like

PacifiCorp.

CM: If you go back and look at our annual from ten years ago, and look at Berkshire now, you'll see that we've managed to get a lot of great stuff into Berkshire over the past ten years. We're not gloomy about the process.

What's your view of Coca-Cola now that you're no longer on the board?

WB: Coke is a fabulous company. It sold the equivalent of 21 billion cases last year, and that number goes up every year. Back in 1997 and 1998, when the stock was trading at $80, earnings per share were $1.50. Last year the company earned $2.17—and earnings were of much higher quality than back in the late 1990s. Every year the company gets a little higher share of the liquids that people consume. The company has $5 billion or $6 billion in tangible assets (ex bottler assets), and earns about that much annually. A 100% pretax return on tangible assets is pretty attractive.

In the late 1990s the stock got a little crazy, but we can't hold management responsible for that. But long-term it's a wonderful business. Volume grows by 5%, year in and year out, while global population grows at just 2%. It's just that for awhile the stock got to a silly price. You can fault me for not selling any. We'll own Coke years from now.

How much have insurance rates hardened? Have you seen a flight to quality?

When you say insurance, I assume you're talking about reinsurance. Other lines, like auto, have been softening.

In reinsurance, there's been a big variance in how much rates are rising. Rates for marine platforms in the Gulf of Mexico are up by a lot—and they should be. In the past 2 years in the Gulf, reinsurers have taken in $2.5 billion in marine-related premiums, and have endured $15 billion in losses. We have been the biggest meg-cat carrier, but our mix has changed. Prices are up, but we don't know if our exposure has gone up. On hurricanes, the question is which is a more meaningful indicator, the experience of the past two years, or the experience of the past 100 years. It's silly to assume that the 100-year experience is right. We don't know all the variables and causes that go into hurricane frequency and severity. If the past two years are the most reliable indicator, we're not getting paid enough. If the past 100 years record is more reliable, we'll be making a lot of money.

The scary possibility is that the changes haven't stopped yet, and that the past two years are not as bad as things get. When you start getting down to chaos theory—where seemingly insignificant changes can lead to huge effects, you can dream up some scary scenarios. We will write in certain areas and certain coverages. We are willing to risk a lot of money, if we think we're getting paid adequately.

We have a lot of exposure to wind, heading into the third quarter, though not as much as we had a couple of years ago. Prices have hardened in that particular area. If we think pricing becomes overdone, we'll take down more risk.

We don't believe in modeling at all. We don't think modelers know a thing.

We get paid for making guesses. Years can go by and we still won't know if we guessed right. The reinsurance business is still a business we like. We bring a lot to the party. Figure that the biggest possible insured loss would be $250 billion. (Katrina was $60 billion.)   We would have 4% of that. We can easily pay that; but a large part of the industry would be in trouble.

We'll see in 5 or 10 years whether we're right or not.

CM: Why not use our financial strength to get into an area that gets people frightened?

How do you value the retro policies you've written? How is NetJets doing?

WB: There are some deferred charges on the balance sheet related to some retro business we wrote. On these policies, we reinsure losses on an event that has already occurred—although the magnitude is not known. So we'll have that money over a period of time. It has been as high as $3 billion, and gets amortized over time. I mis-estimated on a retro contract a few years ago, and we ended up losing money on the deal.

NetJets is growing fast—but its expenses are growing faster. It offers outstanding worldwide service, and is in a strong position in larger planes. When we bought the business, we thought it could realize some economies of scale. That hasn't been the case. If anything, there have been diseconomies of scale. Expenses got out of hand last year, and we're in the process of fixing that. We can't have a better operator than Rick Santulli. NetJets provides an important service—it's just that it's tough to make money at it. Rising fuel prices have hurt the business somewhat, even though they're a pass-through.

We thought the company would make money last year for the first time, but costs rose more than we expected. I expect that NetJets will be profitable before long, although you're entitled to take that with some skepticism, since I've been wrong about its profitability before.

You should hold me responsible. We paid a lot of money for the company several years ago, and haven't earned any money on that investment since.

CM: There's enormous product integrity both at NetJets and FlightSafety International. Pilots are subjected oxygen withdrawal, so that they'll recognize the sensation should it occur when they're flying. Not everyone does that.

What's your exposure to silver? How do you value non-interest-bearing items such as commodities?

WB: We owned silver at one time, but not now. When we owned it, annual production and reclamation was 100 million ounces less than annual consumption. So supply and demand were out of balance. But there was lots of metal above the ground, that had already been mined and refined, that was available to come on the market. And some could be reclaimed from other uses, such as photography. It's hard to bring on new production. There aren't that many pure silver mines (the metal is usually mined as a byproduct from mining other metals.) As I say, we were in early and out early. When an investment doesn't pay interest, you have to hope it rises in price.

CM: We didn't get where we are by owning non-interest-bearing investments. It's a good habit to get into to trumpet your failures and be quiet about your successes.

Is it a good idea to invest in countries that have plenty of natural resources and a strong infrastructure?

WB: That would be a little too macro for us. We prefer to worry about whether or not people will keep eating candy, and will they pay more for it each year. We don’t play big trends. They take too long to play out. There’s too much money to be made year to year, in the meantime.

CM: You’ll note that we have failed to profit from one of the biggest moves in commodity prices in history.

What’s the best way to address the risk of nuclear terrorism in the U.S.?

WB: It would depend on the severity of the event. If you’re looking for a way to profit from such an event, I’m sure there’s some bank somewhere that will sell you a mortality derivative. But a nuclear terrorist event will happen. The world has always had evil people. Thousands of years ago, they threw rocks. Later, they used swords, and then shot each other. Since 1945, man has had the capacity to use nuclear weapons. It’s the most important problem mankind faces. Some people say that the global elimination of poverty will end the nuclear risk, but the U.S. used nuclear weapons in 1945 when it was the richest nation on earth. In order to get nuclear capability, people need to be able to deliver a device, they need access to knowledge about how to build a device, and they need access to the materials needed. We’ve been losing ground in controlling all three of those items. Controlling this should be a top priority. Some people are crazy.

CM: The chances of the world going another 60 to 70 years without a nuclear attack is just about zero. The only thing we can do is elect leaders who understand the seriousness of the problem.

How should Berkshire holders react when Berkshire buys stakes in Wal-Mart and Anheuser-Busch rather than buying back its own stock? Does that mean that you think that WMT and BUD are at bigger discounts to intrinsic value than Berkshire is?

WB: Most of the time, we can’t buy a material amount of stock. If you compare the average trading volume of Berkshire compared to other large-cap companies such as ExxonMobil, G.E., G.M., or Wal-Mart, volume in our stock is a tiny fraction of trading in those other stocks.

CM: Often now, share repurchases by companies are designed to prop up the stock, and are not signals that the company thinks that it is buying a bargain.

WB: Thirty or 40 years ago, it was a great strategy to buy companies that bought back a lot of their own stock. Teledyne was a great example. Management thought its stock was trading a big discount to its real value, so it repurchased shares. Now, though, buybacks are a fashionable way to try to prop up the stock price.

At Berkshire, we have the most honest-to-god owners of any big public company. That's reflected in the stock's low turnover. We're not looking to buy out our partners at a discount.

What is the state of business school education? What advice would you give the new generation of budding "helpers"?

CM: Helpers who come to this meeting are the best in the helper class. What should you do to be like Warren Buffett? The best thing to do is to reduce your expectations.

WB: The activities of most professions are safe and necessary. If your wife is going to have a baby, it's better to call the obstetrician rather than try to deliver it yourself. Most professions add value. But the investment profession does not do that, in aggregate. It makes $140 billion per year, and it basically does the same thing that one person could do if he spent ten minutes per year thinking about his investments. I can't think of another business like that. Plus, the business is unique in that, the more you charge, the more money you bring in.

One of the great businesses is business schools. The more you charge, the better your reputation. The vast majority of professional investors can't add value. In aggregate, you can't pay people 2 and 20 in an economy that produces 7% annual growth and have investors be net better off. People will say that they're the exception, though. Name 10 partnerships, and I'll bet you that those partnerships won't beat the S&P over the following ten years.

Then again, I've identified good managers before the fact. In 1969, when I closed my partnership, I recommended my investors go with Bill Ruane and Sandy Gottesman. The ones who did did very well.

But it's very hard for institutions such as pension funds to select superior investors. They end up going with the best salesman, not the best investor.

CM: It should be a crime to entertain a state pension official. Watching these managers go after the business is not a pretty sight.

How would Berkshire's businesses be affected by immigration reform, were it to pass?

WB: In Nebraska, there are plenty of illegal aliens. They work in the meatpacking business in particular. I was at the airport and saw 100 people all shackled together. They were illegals in the process of being deported. Illegal immigration is a problem that should be addressed, and promptly. I can't see shipping the 11 million people who are here illegally back to their home countries. But we should enforce the rules more aggressive (and perhaps liberalize them some). A reduction in the number of illegal aliens in the work force might cause prices to rise somewhat. But it wouldn't likely have a big effect on the economy overall, or on specific industries. Who's to say, if we were born in Mexico or some other underdeveloped country, that we wouldn't try to enter the U.S. illegally?

CM: My advice is: if you don't like the results, get used to it. The country will never have the will to enforce the immigration laws. What you see is what you'll get.

What school has the best finance program?

WB: I speak to students from around 40 business schools over the course of the year. Now we're doubling up, so that we put to groups together in one visit.

The teaching of finance has improved over the past 20 years, but from a very low base. The flat-earth orthodoxy of 20 years ago, of modern portfolio theory and the efficient market hypothesis, is breaking down. Kansas, Missouri, Florida, Columbia, and Stanford, among others, have good programs. Twenty-five years ago you couldn't get a job or advance if you didn't go along with the EMH and MPT orthodoxy.

Nowadays students all think they'll get rich doing what Charlie and I do. The amount of brainpower going into money management is somewhat distressing. But it's a great time to be 20 or 25 years old and be getting out of school. A lot of students who come visit say that they want to go into private equity or hedge funds. I'm not sure what the economy is going to do for basics like food and clothes. The Kansas students put on skits and try to sell me companies. Students at all these schools are looking for companies I might buy.

CM: Half the business school graduates at the elite Eastern schools say that they want to go into private equity or hedge funds. Their goal seems to be to keep up with their age cohort at Goldman Sachs. This can't possibly end well.

Once you're no longer CEO, will sellers still be as eager to sell to Berkshire? Should you consider becoming Chairman now, so the new CEO could gain experience?

WB: My successor will probably be put on probation by the media for awhile. Maybe a year or so. The phone won't ring less, but the calls will be different. Bankers will try the new guy out to see if he'll bite on their deals. But soon it will become clear that the culture has not changed. Yardsticks won't change. The board won't change. There will be a hiatus, but it won't last long. My successor will be very smart, and has bought into the corporate personality.

CM: We could set up an arrangement that Warren continues to do deals, and a co-CEO runs operations. But that wouldn't work well. We don't really need an operating guy. I'm not sure what he'd do except show the world that Warren hasn't been doing anything.

WB: Even after I'm gone, Berkshire will have the reputation of being a one-of-a-kind place for a business owner who cares about the future off his business, but has to sell for some tax or family reason.

CM: But we prefer to wring the last drop of good out of Warren.

WB: And at low pay! But the arrival of my successor could be a positive since it would demonstrate to the market that the Berkshire culture is institutionalized, and doesn't depend on one individual. I'm not in the same league as Sam Walton, but that's what happened after he died. People saw that the business didn't depend on just one man.

How do you allocate capital to charities?

WB: Pick what's important to you. Most people give to their churches or schools. Give to causes that give you personal satisfaction. I look for things that I think are important, but that don't have a natural source of funding. But there's nothing wrong with giving to a cause that gives you pleasure. I often go where my gut leads me. If I'm looking at giving larger amounts, I feel I have a reason, or even an obligation, to focus on problems that wouldn't get a lot of attention otherwise.

Did you buy into the electric utility business thinking you might be able to use those lines for something else, like telecom?

WB: No. We will earn an attractive return on capital employed if we do a good job in keeping our costs down and our customers happy. We follow the rules and regulations of the states we do business in. We don't expect any big changes in the economics of what we're doing. We're not invested in the electric utility business on the expectation of deriving revenues from other activities.

Do you think that the media business has become permanently less profitable due to new technology?

WB: People will always want to be entertained and informed. But people just have two eyeballs, and there are only 24 hours in a day. Fifty or 60 years ago, media for most people consisted of the local movie theater, radio, and the local newspaper. Now people have a variety of ways of being informed faster (if not necessarily better), and have more entertainment options, too. But no one has figured out a way to increase the time available to watch entertainment.

Whenever more competitors enter a business, the economics of that business tends to deteriorate. Newspapers are still highly profitable, but returns are falling. The size of the audience for network TV is declining. For years, cable TV was thought to operate in its own world, but that's changing. Few businesses get better with more competitors.

The outlook for newspapers is not great. In the TV business, a license from the government was essentially the right to a royalty stream. There were basically three highways to people's eyeballs, and companies like P&G, Ford, Gillette, and GM would pay a significant amount of money to be get on those highways and advertise their products to a mass audience. But as the ways to get in front of people's eyeballs increases, the value of those highways goes down.

World Book used to sell 300,000 sets per year in the mid-1980s, each for $600. Then the Internet cam along; it didn't require printing or shipping, and people became less willing to pay for World Book sets. It doesn't mean that it's not worth $600. But competition has eroded returns.

CM: It's a rare business that doesn't have a way worse future than it has a past.

WB: The thing to do was to buy the NFL when it was first organized. There are now more ways than ever to transit events; value can be extracted from them in different ways.

What's your view on the renminbi, the yen, and the euro?

WB: My view on the dollar is as strong as ever. We're doing our investing in other currencies less directly than we used to. As interest rates have changed, the carry on currency contracts has gone from being positive to quite negative. There are better ways for us to invest in other currencies. We like the idea of owning earnings power in other currencies. That's one reason we're enthusiastic about Iscar.

The fundamental outlook hasn't changed. There's still a very high probability that the dollar will weaken over time. The country is following policies that don't leave much of an alternative. In February of 2002, Alan Greenspan pointed out that the current account deficit was unsustainably large. Now, four years later, it's twice that big.

People talk about a soft landing, but I have yet to hear anyone explain how that soft landing is supposed to work. We will see significant consequences of the current policies. Berkshire will always be invested mainly in the U.S. More will come from overseas, via investments such as Iscar. But the bulk will always come from the U.S. The odds that inflation will return are rising.

CM: I have no special capacity to predict if the euro is priced right. The fact that half of Berkshire's cash was held in non-dollar currencies at one point was an absolute non-event. It's been a very profitable non-event, but it's still a non-event.

WB: Generally it's not a good thing to run a large and rapidly growing current-account deficit. This is a great country. But in the end there could be a comeuppance, and it won't be pleasant. People talk about a "soft landing," but I don't see the logic of how you get from A to B to C to see how a soft landing would work. The longer it goes on, the more in debt the country becomes. It could be very chaotic as it all unravels.

In the 1980s, "portfolio insurance" caught on. It was sold as a highly sophisticated way for large institutions to manage money. People paid a lot of money for mechanical ways to manage portfolios.

Then on October 19, 1987, a relatively small amount of money that had been invested in portfolio insurance led to a one-day, 22% decline in the stock market. Each of the individuals who invested in portfolio insurance was intelligent. In aggregate, though, they created a doomsday machine. The potential for that sort of thing has been magnified quite a lot. Who knows how it will start? Who knows who will yell “fire!”?

Do you believe the CPI is a good measure of inflation?

Bill Gross has written a lot on this topic. At the Furniture Mart, there hasn’t been a whole lot of inflation. DVD players are selling for one quarter of what they used to sell for. The CPI is not a particularly good or accurate measure of inflation. People talk about the “core” rate, that excludes food and energy prices. Well, food and energy are pretty core, too! Years ago, the CPI included home prices. People said that distorted it because home prices tended to rise faster than other prices. Now the CPI contains imputed rent, rather than home prices. The rent factor has lagged what the true change in housing costs have been.

I believe that the CPI has understated inflation. But different people have different expense bases. If you sit and drink Coke all day, you don’t face any inflation. But if you drive 30 to 40 miles per day, your cost of living has gone up pretty fast lately.

CM: At Costco, there’s been almost no inflation. But elsewhere, there has been. I’m not going to feel too sorry, though, for people who’ve paid $27 million for an 8,000-square-foot condo in Manhattan.

WB: If you take a look in Wal-Mart’s annual report, its LIFO adjustment is peanuts. Here’s a company with $200 billion in sales in the U.S., and its LIFO adjustment is not worth a dime. But some of our businesses have seen substantial LIFO adjustment. Our jewelry retailers, for instance. And our steel inventories, at MiTek. Input costs in the carpet business went nowhere for 20 years, but now the adjustments are big, since oil is the main component.

Can you tell us about the acquisitions you’ve done over the past year?

WB: Russell is still in process. We bought BusinessWire after I got a letter from Cathy Tamraz. We bought MedPro on the suggestion of Jeff Immelt. We bought PacifiCorp.

We have not participated in any auctions. We get pitch books occasionally, but the projections are just plain silly. Maybe that's why no one actually signs the books. I'd love talk to the people who wrote the books, and bet them whether their projections will turn out to be right.

I don't know how many $4 billion deals you'll see, like Iscar, where there was no banker on either side.

CM: The interesting thing is the mindset. A lot of these new "helpers" don't have our mindset. We try to welcome partners, not a guy who "does deals" or wants to make a large, quick profit. Our system works better, we think. There are so many deal flippers now that pretty soon they're going to be getting into each other's way.

How might a derivatives meltdown happen?

WB: It's hard to tell. Why do people yell "Fire!"? LTCM happened. The Fed had to step in. Strange things happen in financial markets. Look at the junk bond market in 2002. It was basically closed for awhile.

In 1991, on a Sunday in the middle of August, Salomon was within a half an hour of filing for bankruptcy. It was terrifying. At the last minute, the Treasury reversed itself. On the same day, Gorbachev was spirited away by would-be coup plotters. What would have happened to Solly's derivatives book on Monday morning if it had filed the day before? What would have happened in Japan that morning when it came time to deliver securities from Friday's transactions?

CM: It could have been absolute chaos. Luckily, Nick Brady, who was Treasury Secretary, knew about Berkshire, and trusted Warren. So the element of personal reputation played a role.

WB: The size of the exposure was nothing then compared to what it would be now. It's true that derivatives positions are more collateralized now.

If you were looking at newspaper publishers as possible investments, what would you use as a margin of safety?

WB: What multiple should you for a company that earns $100 million per year whose earnings are falling by 5% per year rather than rising by 5% per year? Newspapers face the prospect of seeing their earnings erode indefinitely. It's unlikely that at most papers, circulation or ad pages will be larger in five years than they are now. That's even true in cities that are growing.

But most owners don’t yet see this protracted decline for what it is. The multiples on newspaper stocks are unattractively high. They are not cheap enough to compensate for the companies’ earnings power. Sometimes there’s a perception lag between the actual erosion of a business and how that erosion is seen by investors. Certain newspaper executives are going out and investing on other newspapers. I don’t see it. It’s hard to make money buying a business that’s in permanent decline. If anything, the decline is accelerating. Newspaper readers are heading into the cemetery, while newspaper non-readers are just getting out of college. The old virtuous circle, where big readership draws a lot of ads, which in turn draw more readers, has broken down.

Charlie and I think newspapers are indispensable. I read four a day. He reads five. We couldn’t live without them. But a lot of people can now. This used to be the ultimate bulletproof franchise. It’s not anymore.

CM: I used to think that GM was a bulletproof franchise. Now I’d put GM and newspapers in the “Too Hard” pile. If something is too hard to do, we look for something that isn’t too hard. What could be more obvious?

WB: It may be that no one has followed the newspaper business as closely as we have for as long as we have—50 years or more. It’s been interesting to watch newspaper owners and investors resist seeing what’s going on right in front of them. It used to be you couldn’t make a mistake managing a newspaper. It took no management skill—like TV stations. Your nephew could run one.

Who are some present-day mentors young people should follow?

WB: You don’t need to look at the present. This stuff doesn’t change. Don Keough. Tom Murphy. Just study them. The lessons are timeless. There’s going to be a Harvard Business School case study on Cap Cities. If you learn certain lessons from the right people, that knowledge won’t change.

CM: I don’t follow any 40-year-old investment professionals.

WB: Investing is not complicated. You work to find pockets of value. You didn’t need a high IQ to buy junk bonds in 2002. You needed to have the courage of your convictions when everyone else was terrified. It was the same in 1974. People were paralyzed. You need to learn to follow logic rather than emotion. That’s easier for some people to do rather than others.

CM: We had less competition when we were young, though. There weren't too many smart people in the investment business back then. (You should have seen some of the people who worked in bank trust departments.) Now all kinds of bright people want to be in investment management. But in those days, we'd often be the only buyers.

WB: But Charlie, in 2002, there was lots of money and lots of smart people, and it was still easy to make a lot of money in junk bonds.

CM: Yes, but you get a lot of weird behavior during a convulsion like that. If you can be wise when everyone else is terrified, you'll do well.

WB: Two years ago, a lot of great companies in Korea were trading at 3 times earnings.

CM: That was a result of the Asian meltdown in the late 1990s.

WB: Yes, it took a big convulsion for Korean valuations to get so low. But there were plenty of smart people around, and all the relevant information was freely available to them.

CM: Then name 20 more like that.

WB: If I had 20 more, I wouldn't name them.

If you were starting out with $1 million today, what strategy would you follow?

WB: We started out almost 50 years ago to the day—May 4, 1956, with $105,000. You don't need to have a lot of great ideas. I'd follow the same strategy we follow now, although we'd be able to look at smaller stocks than we look at now. We'd have a tougher time finding businesses to buy, since sellers wouldn't know about us. Charlie started out in real estate. In real estate, you don't need a lot of capital to start out with, because you can leverage your brainpower. But our basic process wouldn't have been different. I may have been 100% in Korean stocks.

We'd look for something that was mispriced and underowned.

CM: Finding a single investment that will return 20% per year for 40 years tends to happen only in dreamland. In the real world, you uncover an opportunity, then you compare other opportunities with that. And you only invest in the most attractive opportunities. It's all about opportunity cost. The game hasn't changed at all. That's why modern portfolio theory is so asinine.

If Warren were starting today, he'd put together a concentrated portfolio. Your 1 or 2 best ideas are way better than the rest. So when you act, you're thinking about how the alternatives compare to your best idea. But you don't want to own your 10th-best idea when you can use that cash to invest in your best idea.

What do you think of the work done by Jeremy Siegel?

CM: I think he's demented. He tries to compare apples and elephants in making accurate projections.

What are the advantages of being contrarian?

WB: Being a contrarian is neither right nor wrong. Contrarian thinking isn't a good thing in and of itself. You collect your facts and do your research, and come to a conclusion. If there's a fact that's important, but unknowable—then forget it. And if it's knowable but unimportant, then it doesn't matter.

So you care about gathering the facts that are knowable and important. When you've done that, then decide whether your information is of enough value to cause you to act.

The market is there to serve you, not to instruct you. The problem with other disciplines, such as technical analysis and momentum investing, is that in those cases, investors are being told what to do by the market.

There's always something new that pops up without warning.. If you ever get a call on a Sunday, you'll make a lot of money. Or if you hear that, say, off-run Treasuries are trading 30 basis points away from the on-the-run Treasury. But it depends on how you handle it. Can you play out your hand? Don't let the other guy call your tune, so that he's playing your game and not the other way around. Make sure that you have your facts straight, and that your judgment about those facts is sound. If all that's the case, then you'll be able to make a lot of money when somebody else's crisis occurs.

How do you look to see if Berkshire's stock is overpriced or

underpriced?

WB: You can drown people in information if you give them too much of it. When Charlie and I put the annual report together, we write it as if one of us has been on a desert island for a year and the other wants to give him the information he needs to assess the state of the business. It's worth reading the whole report. What counts is who's running the business, and the outlook for the business. But we don't carry things out to 4 decimal places. If each of us were to calculate the value of the business, we'd each come up with a different number, but both numbers would be in the same ballpark.

CM: When I try to come up with an approximate value of Berkshire, I quickly dispose of the no-brainer issues first. The insurance operation is very interesting—so is the process of determining how the excess cash will be redeployed. But take the no-brainers first.

How have worldwide underwriting standards changed, particularly as the risk of things like terrorism and hurricanes seems to be increasing?

Our float at one point was up to $49 billion. We never expected it would get that big.

Our float right now is around 10% of the entire industry's. We're all aware of the risks of pandemics, hurricanes, terrorism, and things like that. We talk all the time about the chances of a $50 billion-plus event, or $20 billion events. We're just making judgments about their likelihood, and whether or not we're being paid enough to insure them. If we end up paying out a big loss, it doesn't mean that we were wrong.

The earthquake experience of the past 100 years is more valuable to us in assessing earthquake risk than the hurricane experience of the past 100 years is in assessing hurricane risk. What will the hurricane experience be over the coming ten years compared to what it's been? I don't know. But I think about it every day.

CM: According to the laws of thermodynamics, if the oceans get warmer, the weather will be more turbulent. We'd be out of our mind to underwrite as if global warming has had no effect on water temperatures. The key is to charge enough and control risk enough. But small causes can have huge effects. A 1% change in temperature can cause a 100% increase in losses. So if we don't like the offer, someone else can take our place.

What are the principles you follow in investing in healthcare?

CM: We put the health care companies in the “Too Hard” pile. A lot of people made a lot of money writing health insurance. There are a lot of bad ethics, and there are a lot of good ethics too. But it all goes in the “Too Hard” pile.

WB: We have not owned much in health care. It’s a tough problem. I have no insight into the business.

What do you think about bankruptcy reform?

CM: The bankruptcy process is pretty horrible. You have a situation where courts get into bidding contests to hear cases. If you develop a culture where you overpay people, such as lawyers and bankruptcy consultants, to be involved in the bankruptcy process, you’re going to get more bankruptcies. And that’s what’s happened. It’s so unpleasant to watch, I don’t pay as much attention as I should, because I don’t like to have upset stomachs.

WB: We have bought junk bonds related to bankruptcies. We bought the Osprey bonds out of the Enron filing. A complicated bankruptcy can offer opportunities. We first got involved with Fruit-of-the-Loom when it was in bankruptcy; we bought some debt.

Penn Central was a huge mess when it filed in 1970. There’s a lot of money to be made when that happens. You tend to get a lot of mispricings as a company comes out of bankruptcy. Usually it’s on the low side—but not always.

In the Enron situation, the Ospreys were complicated. We didn’t buy them at the bottom, but we still tripled our money.

The Penn Central situation was extremely complex. There were lots liens and leaseholds and all kinds of things. Finally the judge said I’m going to ignore all that stuff and give you a quick, fast solution. That was probably a good thing. The judge is the one who determines this stuff. I asked Charlie once how much power a judge really has in a case like this. He told me, “For awhile, as much as he thinks he has.”

What is the outlook for P&G’s pharma business?

WB: Procter & Gamble is a consumer powerhouse. Gillette has as strong a competitive position as anyone in the consumer market. The big retailers are developing powerful brands on their own. Power among marketers is becoming more and more concentrated. Each side, between the retailers and consumer marketers, wants to strengthen its hand. So P&G and Gillette are stronger together in their dealings with retailers.

But I don't know a thing about the pharmaceuticals business.

CM: That makes two of us.

Do you have any interest in acquiring Oriental Trading Co.?

WB: I haven't been following that lately, although I know it's for sale. It went private a few years ago, and now the group is reselling. We get approached on deals like this all the time; invariably it's an auction. First, the seller goes out to try to find a strategic buyer who'll participate. A "strategic buyer" is defined as someone who'd willing to pay too much.

I'm skeptical of the idea that we'll find an attractive business to buy if the seller is a guy who's been looking to sell from the moment he acquired the business. We won't trust the figures he gives us. We like businesses where the seller wants to be around for 100 more years, and *has* to sell for some reason. Taxes maybe, or some family reason.

But there are some businesses that pass from one financial buyer to another. It's A to B to C, and each time the seller takes a 20% markup on the sale. We don't buy from financial buyers.

CM: In the 1930s, you could borrow more money against real estate than you could sell the real estate for. It's like that now on a lot of these transactions. This is not our field.

The current account deficit isn't as dire as you portray, since U.S. investors are taking capital gains on their non-U.S. holdings, don't you think?

WB: It's true that the current account deficit would be much smaller if you take into account that the gains that U.S. investors have on their foreign investments is much larger than the gains that foreign investors have on their U.S. investments. But even there the gap is narrowing. Our interest rates are rising, so foreign investors are earning more on their U.S. holdings than they used to. Not too long ago, Treasuries essentially paid nothing. And our investments abroad were made earlier, and are now paying high returns.

CM: It's amazing how much ruinous behavior you can get away with if, like the U.S. is, you've been well-regarded for a long time.

But what are the alternatives? Would you rather invest in Europe? The demographics and economic outlook there aren't particularly attractive. Brazil has great assets, but has the risk of political instability. Same with Venezuela. So it's not as if there are many attractive alternatives to dollar-denominated investments. It's not completely irrational that people like the U.S. Fiscal misbehavior can go on for a long time.

How do you reconcile your views on gambling with insurance underwriting? Aren't they basically the same thing?

WB: Gambling creates risks that don't need to be created. It doesn't matter whether the ball falls in the red square or the black square. But if you have a home in a coastal area, you have a real risk, and you have a real interest in having some one take on that risk. You can watch a football game without taking on risk (unless you volunteer to), but you can't live in that house without taking on risk.

CM: The whole concept of house advantage is interesting. A lot of people involved in private equity investing are taking a rate that looks awfully similar to what croupier's rake takes—only bigger.

What do you think about naked short selling?

WB: I have no objection philosophically to shorting stocks. We're not allowed to lend our shares out to short-sellers, but I'd love to be able to, because it's a very profitable activity. There's nothing evil about short-selling. But it's a tough way to make a living. It's tough emotionally. If you short a stock at $20, the most you can make is $20, but there's no limit to how much you can lose. People on the short side will do and say things to try to get their positions to fall; people on the long side do, too. Some of the things they do may be inappropriate.

As to naked shorting, where you don't have stock to deliver against your short, I don't have a big problem with that, either.

Historically, a lot of stocks that have high short interest are later shown to be frauds or semi-frauds. I've had 100 ideas to be short, and have often been right—eventually, but long after I've covered, and the stocks have risen a lot. The people who run those companies tend to be good at keeping their stock prices up.

Being short stocks is a tough psychological game. I'd never put money in a short fund.

CM: One of the most irritating experiences I can imagine is shorting a stock at X, and seeing it go to 3X, and having to look at all those happy crooks that have gotten rich with the help of your money. Why go into it?

What do you think? **Let me know!**

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