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Our Performance in 1961

I have consistently told partners that it is my expectation and hope (it's alwa hard to tell which is which) that we will do relatively well compared to the ge eral market in down or static markets, but that we may not look so good in a vancing markets. In strongly advancing markets I expect to have real diffic keeping up with the general market.

Although 1961 was certainly a good year for the general market and, in addi a very good year for us on both an absolute and relative basis, the expectati in the previous paragraph remain unchanged.

During 1961, the general market as measured by the Dow-Jones Industrial A age (hereinafter called the "Dow") showed an over-all gain of 22.2% includir dividends received through ownership of the Dow. The gain for all partners operating throughout the entire year, after all expenses of operation, but be payments to limited partners or accrual to the general partner, averaged 4 The details of this gain by partnership are shown in the appendix along with sults for the partnerships started during the year.

We have now completed five full years of partnership operation, and the re of these five years are shown below on a year-by-year basis and also on a c lative or compounded basis. These results are stated on the basis describ the preceding paragraph; after expenses, but <u>before</u> division of gains amon partners or payments to partners.

Year	Partnerships Operating Entire Year	Partnership Gain	Dow-Jones Industrials Gain *
1957	3	10.4%	-8.4%
1958	5	40.9	38.5
1959	6	25.9	19.9
1960	7	22.8	-6.3
1961	7	45.9	22.2

* Including dividends received through ownership of the Dow.

On a compounded basis, the cumulative results have been:

Year	Partnership Gain	Dow-Jones Industrials Gain
1957	10.4%	-8.4%
1957-8	55.6	26.9
1957-9	95.9	52.2
1957-60	140.6	42.6
1957-61	251.0	74.3

These results do not measure the gain to the limited partner, which of course, is the figure in which you are most interested. Because of the varying partner ship arrangements that have existed in the past, I have used the over-all net gain (based on market values at the beginning and end of the year) to the partne ship as being the fairest measure of over-all performance.

On a pro-forma basis adjusted to the division of gains entailed in our present Buffett Partnership, Ltd. agreement, the results would have been:

Year	Limited Partners' Gain	Dow Gain
1957	9.3%	-8.4%
1958	32.2	38.5
1959	20.9	19.9
1960	18.6	-6.3
1961	35.9	22.2
	COMPOUNDED	
1957	9.3%	-8.4%
1957-8	44.5	26.9
1957-9	74.7	52.2
1957-60	107.2	42.6
1957-61	181.6	74.3

A Word About Par

The outstanding item of importance in my selection of partners, as well as in my subsequent relations with them, has been the determination that we use th same yardstick. If my performance is poor, I expect partners to withdraw, and indeed, I should look for a new source of investment for my own funds. I performance is good, I am assured of doing splendidly, a state of affairs to which I am sure I can adjust.

The rub, then, is in being sure that we all have the same ideas of what is goo and what is poor. I believe in establishing yardsticks prior to the act; retro spectively, almost anything can be made to look good in relation to somethin or other.

I have continuously used the Dow-Jones Industrial Average as our measure of par. It is my feeling that three years is a very minimal test of performance, and the best test consists of a period at least that long where the terminal leve of the Dow is reasonably close to the initial level.

While the Dow is not perfect (nor is anything else) as a measure of performanc it has the advantage of being widely known, has a long period of continuity, anc reflects with reasonable accuracy the experience of investors generally with th

COMPOUNDED

Year	Mass.Inv. Trust	Investors Stock	Lehman	Tri-Cont.	Dow	Limited Partners
1957	-12.0%	-12.4%	-11.4%	- 2.4%	- 8.4%	+ 9.3%
1957-8	+26.8	+29.3	+24.7	+30.0	+26.9	+44.5
1957-9	+37.2	+42.6	+34.8	+40.9	+52.2	+74.7
1957-60	+36.0	+42.5	+38.3	+44.8	+42.6	+107.2

Massachusetts Investors Trust has net assets of about $1.8 billion; Investors Stock Fund about $1 billion; Tri-Continental Corporation about $.5 billion; and Lehman Corporation about $350 million; or a total of over $3.5 billion.

I do not present the above tabulations and information with the idea of indictin investment companies. My own record of investing such huge sums of money with restrictions on the degree of activity I might take in companies where we had investments, would be no better, if as good. I present this data to indica the Dow as an investment competitor is no pushover, and the great bulk of investment funds in the country are going to have difficulty in bettering, or per even matching, its performance.

Our portfolio is very different from that of the Dow. Our method of operatio is substantially different from that of mutual funds.

However, most partners, as an alternative to their investment in the partner would probably have their funds invested in a media producing results compa to the Dow, therefore, I feel it is a fair test of performance.

Our Method of Operation

Our avenues of investment break down into three categories. These categor have different behavior characteristics, and the way our money is divided among them will have an important effect on our results, relative to the Dow in any given year. The actual percentage division among categories is to so degree planned, but to a great extent, accidental, based upon availability fac

The first section consists of generally undervalued securities (hereinafter c "generals") where we have nothing to say about corporate policies and no tin table as to when the undervaluation may correct itself. Over the years, thi has been our largest category of investment, and more money has been mad here than in either of the other categories. We usually have fairly large po tions (5% to 10% of our total assets) in each of five or six generals, with smaller positions in another ten or fifteen.

Sometimes these work out very fast; many times they take years. It is diff at the time of purchase to know any specific reason why they should appreci in price. However, because of this lack of glamour or anything pending wh might create immediate favorable market action, they are available at very cheap prices. A lot of value can be obtained for the price paid. This substa tial excess of value creates a comfortable margin of safety in each transacti This individual margin of safety, coupled with a diversity of commitments creates a most attractive package of safety and appreciation potential. Over for a long period, this might very well happen. If it moves up before we have a substantial percentage of the company's stock, we sell at higher levels and complete a successful general operation. We are presently acquiring stock in what may turn out to be control situations several years hence.

Dempster Mill Manufacturing Company

We are presently involved in the control of Dempster Mill Manufacturing Com pany of Beatrice, Nebraska. Our first stock was purchased as a generally undervalued security five years ago. A block later became available, and I went on the Board about four years ago. In August, 1961, we obtained majori control, which is indicative of the fact that many of our operations are not ex actly of the "overnight" variety.

Presently we own 70% of the stock of Dempster with another 10% held by a fe associates. With only 150 or so other stockholders, a market on the stock is virtually non-existent, and in any case, would have no meaning for a controll block. Our own actions in such a market could drastically affect the quoted p

Therefore, it is necessary for me to estimate the value at yearend of our con trolling interest. This is of particular importance since, in effect, new part are buying in based upon this price, and old partners are selling a portion of their interest based upon the same price. The estimated value should not be what we hope it would be worth, or what it might be worth to an eager buyer, etc., but what I would estimate our interest would bring if sold under curren conditions in a reasonably short period of time. Our efforts will be devoted ward increasing this value, and we feel there are decent prospects of doing t

Dempster is a manufacturer of farm implements and water systems with sal in 1961 of about $9 million. Operations have produced only nominal profits i relation to invested capital during recent years. This reflected a poor mana ment situation, along with a fairly tough industry situation. Presently, cons dated net worth (book value) is about $4.5 million, or $75 per share, consoli working capital about $50 per share, and at yearend we valued our interest a

The Question of Conservatism

[redacted]

as to how conservatively our portoflio is invested. Many people some years back thought they were behaving in the most conservative manner by purchas medium or long-term municipal or government bonds. This policy has prod substantial market depreciation in many cases, and most certainly has failec maintain or increase real buying power.

Conscious, perhaps overly conscious, of inflation, many people now feel tha they are behaving in a conservative manner by buying blue chip securities al regardless of price-earnings ratios, dividend yields, etc. Without the benef hindsight as in the bond example, I feel this course of action is fraught with ger. There is nothing at all conservative, in my opinion, about speculating to just how high a multiplier a greedy and capricious public will put on earni

You will not be right simply because a large number of people momentarily agree with you. You will not be right simply because important people agre with you. In many quarters the simultaneous occurence of the two above fac tors is enough to make a course of action meet the test of conservatism.

You will be right, over the course of many transactions, if your hypotheses correct, your facts are correct, and your reasoning is correct. True cons tism is only possible through knowledge and reason.

I might add that in no way does the fact that our portfolio is not conventional prove that we are more conservative or less conservative than standard met of investing. This can only be determined by examining the methods or exa ing the results.

Larger funds tug in two directions. From the standpoint of "passive" investments, where we do not attempt by the size of our investment to influence corporate policies, larger sums hurt results. For the mutual fund or trust department investing in securities with very broad markets, the effect of large sums should be to penalize results only very slightly. Buying 10,000 shares of General Motors is only slightly more costly (on the basis of mathematical expectancy) than buying 1,000 or 100 shares.

In some of the securities in which we deal (but not all by any means) buying 10,000 shares is much more difficult than buying 100 and is sometimes impossible. Therefore, for a portion of our portfolio, larger sums are definitely disadvantageous. For a larger portion of the portfolio, I would say increased sums are only slightly disadvantageous. This category includes most of our work-outs and some generals.

However, in the case of control situations increased funds are a definite advantage. A "Sanborn Map" cannot be accomplished without the wherewithal. My definite belief is that the opportunities increase in this field as the funds increase. This is due to the sharp fall-off in competition as the ante mounts plus the important positive correlation that exists between increased size of company and lack of concentrated ownership of that company's stock.

... creasing prospects of profitability in passive dividends and market value gain. Despite the experience of recent years, anyone expecting substantially better than that from the general market probably faces disappointment.

Our job is to pile up yearly advantages over the performance of the Dow without worrying too much about whether the absolute results in a given year are a plus or a minus. I would consider a year in which we were down 15% and the Dow declined 25% to be much superior to a year when both the partnership and the Dow advanced 20%. I have stressed this point in talking with partners money's worth from this expenditure, and you are most cordially invited to drop in and see how the money is being spent.

With over 90 partners and probably 40 or so securities, you can understand that it is quite a welcome relief to me to shake loose from some of the details.

We presently have partners residing in locations from California to Vermont, and net assets at the beginning of 1962 amounted to $7,178,500.00. Susie and I have an interest in the partnership amounting to $1,025,000.00, and other relatives of mine have a combined interest totaling $782,600.00. The minimum for new partners last year was $25,000, but I am giving some thought to increasing it this year.

Peat, Marwick, Mitchell & Company did an excellent job of expediting the aud providing tax figures much earlier than in the past. They assure me this performance can be continued.

Let me hear from you regarding questions you may have on any aspects of this letter, your audit, status of your partnership interest, etc., that may puzzle you.

Cordially,

Warren E. Buffett

Warren E. Buffett

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APPENDIX

Partnerships Operating Throughout 1961

Partnership	1/1/61 Capital at Market	Over-all Gain in 1961 *	Percentage Gain
Buffett Associates	$ 486,874.27	$ 225,387.80	46.3%
Buffett Fund	351,839.29	159,696.93	45.4
Dacee	235,480.31	116,504.47	49.5
Emdee	140,005.24	67,387.28	48.1
Glenoff	78,482.70	39,693.80	50.5
Mo-Buff	325,844.71	149,163.71	45.8
Underwood	582,256.82	251,951.26	43.3
	$2,200,783.34	$1,009,785.25	45.9%

Partnerships Started in 1961

Partnership	Paid-in	Over-all Gain in 1961	Percentage Gain
Ann Investments	$ 100,100 (1-30-61)	$ 35,367.93	35.3%
Buffett-TD	250,100 ($200,100 on 3-8-61, $50,000 on 5-31-61)	70,294.08	28.1
Buffett-Holland	125,100 (5-17-61)	16,703.76	13.3

* Gain in net assets at market values plus payments to limited partners during year.