Note: The following table appears in the printed Annual Report on the facing page of the Chairman's Letter and is referred to in that letter.

Berkshire's Corporate Performance vs. the S&P 500

Year	Annual Percentage Change in Per-Share Book Value of Berkshire (1)	Annual Percentage Change in S&P 500 with Dividends Included (2)	Relative Results (1)-(2)
1965	23.8	10.0	13.8
1966	20.3	(11.7)	32.0
1967	11.0	30.9	(19.9)
1968	19.0	11.0	8.0
1969	16.2	(8.4)	24.6
1970	12.0	3.9	8.1
1971	16.4	14.6	1.8
1972	21.7	18.9	2.8
1973	4.7	(14.8)	19.5
1974	5.5	(26.4)	31.9
1975	21.9	37.2	(15.3)
1976	59.3	23.6	35.7
1977	31.9	(7.4)	39.3
1978	24.0	6.4	17.6
1979	35.7	18.2	17.5
1980	19.3	32.3	(13.0)
1981	31.4	(5.0)	36.4
1982	40.0	21.4	18.6
1983	32.3	22.4	9.9
1984	13.6	6.1	7.5
1985	48.2	31.6	16.6
1986	26.1	18.6	7.5
1987	19.5	5.1	14.4
1988	20.1	16.6	3.5
1989	44.4	31.7	12.7
1990	7.4	(3.1)	10.5
1991	39.6	30.5	9.1
1992	20.3	7.6	12.7
1993	14.3	10.1	4.2
1994	13.9	1.3	12.6
1995	43.1	37.6	5.5
1996	31.8	23.0	8.8
1997	34.1	33.4	.7
1998	48.3	28.6	19.7
1999	.5	21.0	(20.5)
2000	6.5	(9.1)	15.6
2001	(6.2)	(11.9)	5.7
Average Annual Gain – 1965-2001	22.6%	11.0%	11.6%
Overall Gain – 1964-2001	194,936%	4,742%	190,194%

Notes: Data are for calendar years with these exceptions: 1965 and 1966, year ended 9/30; 1967, 15 months ended 12/31.

Starting in 1979, accounting rules required insurance companies to value the equity securities they hold at market rather than at the lower of cost or market, which was previously the requirement. In this table, Berkshire's results through 1978 have been restated to conform to the changed rules. In all other respects, the results are calculated using the numbers originally reported.

The S&P 500 numbers are **pre-tax** whereas the Berkshire numbers are **after-tax**. If a corporation such as Berkshire were simply to have owned the S&P 500 and accrued the appropriate taxes, its results would have lagged the S&P 500 in years when that index showed a positive return, but would have exceeded the S&P in years when the index showed a negative return. Over the years, the tax costs would have caused the aggregate lag to be substantial.

BERKSHIRE HATHAWAY INC.

To the Shareholders of Berkshire Hathaway Inc.:

Berkshire's *loss* in net worth during 2001 was $3.77 billion, which decreased the per-share book value of both our Class A and Class B stock by 6.2%. Over the last 37 years (that is, since present management took over) per-share book value has grown from $19 to $37,920, a rate of 22.6% compounded annually.*

Per-share intrinsic grew somewhat faster than book value during these 37 years, and in 2001 it probably decreased a bit less. We explain intrinsic value in our Owner's Manual, which begins on page 62. I urge new shareholders to read this manual to become familiar with Berkshire's key economic principles.

Two years ago, reporting on 1999, I said that we had experienced both the worst absolute and relative performance in our history. I added that "relative results are what concern us," a viewpoint I've had since forming my first investment partnership on May 5, 1956. Meeting with my seven founding limited partners that evening, I gave them a short paper titled "The Ground Rules" that included this sentence: "Whether we do a good job or a poor job is to be measured against the general experience in securities." We initially used the Dow Jones Industrials as our benchmark, but shifted to the S&P 500 when that index became widely used. Our comparative record since 1965 is chronicled on the facing page; last year Berkshire's advantage was 5.7 percentage points.

Some people disagree with our focus on relative figures, arguing that "you can't eat relative performance." But if you expect – as Charlie Munger, Berkshire's Vice Chairman, and I do – that owning the S&P 500 will produce reasonably satisfactory results over time, it follows that, for long-term investors, gaining small advantages annually over that index *must* prove rewarding. Just as you can eat well throughout the year if you own a profitable, but highly seasonal, business such as See's (which loses considerable money during the summer months) so, too, can you regularly feast on investment returns that beat the averages, however variable the absolute numbers may be.

Though our corporate performance last year was satisfactory, *my* performance was anything but. I manage most of Berkshire's equity portfolio, and my results were poor, just as they have been for several years. Of even more importance, I allowed General Re to take on business without a safeguard I knew was important, and on September 11th, this error caught up with us. I'll tell you more about my mistake later and what we are doing to correct it.

Another of my 1956 Ground Rules remains applicable: "I cannot promise results to partners." But Charlie and I *can* promise that your economic result from Berkshire will parallel ours during the period of your ownership: We will not take cash compensation, restricted stock or option grants that would make our results superior to yours.

Additionally, I will keep well over 99% of my net worth in Berkshire. My wife and I have never sold a share nor do we intend to. Charlie and I are disgusted by the situation, so common in the last few years, in which shareholders have suffered billions in losses while the CEOs, promoters, and other higher-ups who fathered these disasters have walked away with extraordinary wealth. Indeed, many of these people were urging investors to buy shares while concurrently dumping their own, sometimes using methods that hid their actions. To their shame, these business leaders view shareholders as patsies, not partners.

Though Enron has become the symbol for shareholder abuse, there is no shortage of egregious conduct elsewhere in corporate America. One story I've heard illustrates the all-too-common attitude of managers toward

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*All figures used in this report apply to Berkshire's A shares, the successor to the only stock that the company had outstanding before 1996. The B shares have an ec onomic interest equal to 1/30th that of the A.

owners: A gorgeous woman slinks up to a CEO at a party and through moist lips purrs, "I'll do anything – *anything* – you want. Just tell me what you would like." With no hesitation, he replies, "Reprice my options."

One final thought about Berkshire: In the future we won't come close to replicating our past record. To be sure, Charlie and I will strive for above-average performance and will not be satisfied with less. But two conditions at Berkshire are far different from what they once were: Then, we could often buy businesses and securities at much lower valuations than now prevail; and more important, we were then working with far less money than we now have. Some years back, a good $10 million idea could do wonders for us (witness our investment in Washington Post in 1973 or GEICO in 1976). Today, the combination of *ten* such ideas and a triple in the value of *each* would increase the net worth of Berkshire by only ¼ of 1%. We need "elephants" to make significant gains now – and they are hard to find.

On the positive side, we have as fine an array of operating managers as exists at any company. (You can read about many of them in a new book by Robert P. Miles: *The Warren Buffett CEO*.) In large part, moreover, they are running businesses with economic characteristics ranging from good to superb. The ability, energy and loyalty of these managers is simply extraordinary. We now have completed 37 Berkshire years without having a CEO of an operating business elect to leave us to work elsewhere.

Our star-studded group grew in 2001. First, we completed the purchases of two businesses that we had agreed to buy in 2000 – Shaw and Johns Manville. Then we acquired two others, MiTek and XTRA, and contracted to buy two more: Larson-Juhl, an acquisition that has just closed, and Fruit of the Loom, which will close shortly if creditors approve our offer. All of these businesses are led by smart, seasoned and trustworthy CEOs.

Additionally, all of our purchases last year were for cash, which means our shareholders became owners of these additional businesses without relinquishing any interest in the fine companies they already owned. We will continue to follow our familiar formula, striving to increase the value of the excellent businesses we have, adding new businesses of similar quality, and issuing shares only grudgingly.

Acquisitions of 2001

A few days before last year's annual meeting, I received a heavy package from St. Louis, containing an unprepossessing chunk of metal whose function I couldn't imagine. There was a letter in the package, though, from Gene Toombs, CEO of a company called MiTek. He explained that MiTek is the world's leading producer of this thing I'd received, a "connector plate," which is used in making roofing trusses. Gene also said that the U.K. parent of MiTek wished to sell the company and that Berkshire seemed to him the ideal buyer. Liking the sound of his letter, I gave Gene a call. It took me only a minute to realize that he was our kind of manager and MiTek our kind of business. We made a cash offer to the U.K. owner and before long had a deal.

Gene's managerial crew is exceptionally enthusiastic about the company and wanted to participate in the purchase. Therefore, we arranged for 55 members of the MiTek team to buy 10% of the company, with each putting up a minimum of $100,000 in cash. Many borrowed money so they could participate.

As they would *not* be if they had options, all of these managers are true *owners*. They face the downside of decisions as well as the upside. They incur a cost of capital. And they can't "reprice" their stakes: What they paid is what they live with.

Charlie and I love the high-grade, truly entrepreneurial attitude that exists at MiTek, and we predict it will be a winner for all involved.

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In early 2000, my friend, Julian Robertson, announced that he would terminate his investment partnership, Tiger Fund, and that he would liquidate it entirely except for four large holdings. One of these was XTRA, a leading lessor of truck trailers. I then called Julian, asking whether he might consider selling his XTRA block or whether, for that matter, the company's management might entertain an offer for the entire company. Julian referred me to Lew Rubin, XTRA's CEO. He and I had a nice conversation, but it was apparent that no deal was to be done.

Then in June 2001, Julian called to say that he had decided to sell his XTRA shares, and I resumed conversations with Lew. The XTRA board accepted a proposal we made, which was to be effectuated through a tender offer expiring on September 11th. The tender conditions included the usual "out," allowing us to withdraw if the stock market were to close before the offer's expiration. Throughout much of the 11th, Lew went through a particularly wrenching experience: First, he had a son-in-law working in the World Trade Center who couldn't be located; and second, he knew we had the option of backing away from our purchase. The story ended happily: Lew's son-in-law escaped serious harm, and Berkshire completed the transaction.

Trailer leasing is a cyclical business but one in which we should earn decent returns over time. Lew brings a new talent to Berkshire, and we hope to expand in leasing.

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On December 3rd, I received a call from Craig Ponzio, owner of Larson-Juhl, the U.S. leader in custom-made picture frames. Craig had bought the company in 1981 (after first working at its manufacturing plant while attending college) and thereafter increased its sales from $3 million to $300 million. Though I had never heard of Larson-Juhl before Craig's call, a few minutes talk with him made me think we would strike a deal. He was straightforward in describing the business, cared about who bought it, and was realistic as to price. Two days later, Craig and Steve McKenzie, his CEO, came to Omaha and in ninety minutes we reached an agreement. In ten days we had signed a contract.

Larson-Juhl serves about 18,000 framing shops in the U.S. and is also the industry leader in Canada and much of Europe. We expect to see opportunities for making complementary acquisitions in the future.

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As I write this letter, creditors are considering an offer we have made for Fruit of the Loom. The company entered bankruptcy a few years back, a victim both of too much debt and poor management. And, a good many years before that, I had some Fruit of the Loom experience of my own.

In August 1955, I was one of five employees, including two secretaries, working for the three managers of Graham-Newman Corporation, a New York investment company. Graham-Newman controlled Philadelphia and Reading Coal and Iron ("P&R"), an anthracite producer that had excess cash, a tax loss carryforward, and a declining business. At the time, I had a significant portion of my limited net worth invested in P&R shares, reflecting my faith in the business talents of my bosses, Ben Graham, Jerry Newman and Howard (Micky) Newman.

This faith was rewarded when P&R purchased the Union Underwear Company from Jack Goldfarb for $15 million. Union (though it was then only a licensee of the name) produced Fruit of the Loom underwear. The company possessed $5 million in cash – $2.5 million of which P&R used for the purchase – and was earning about $3 million pre-tax, earnings that could be sheltered by the tax position of P&R. And, oh yes: Fully $9 million of the remaining $12.5 million due was satisfied by non-interest-bearing notes, payable from 50% of any earnings Union had in excess of $1 million. (*Those* were the days; I get goosebumps just thinking about such deals.)

Subsequently, Union bought the licensor of the Fruit of the Loom name and, along with P&R, was merged into Northwest Industries. Fruit went on to achieve annual pre-tax earnings exceeding $200 million.

John Holland was responsible for Fruit's operations in its most bountiful years. In 1996, however, John retired, and management loaded the company with debt, in part to make a series of acquisitions that proved disappointing. Bankruptcy followed. John was then rehired, and he undertook a major reworking of operations. Before John's return, deliveries were chaotic, costs soared and relations with key customers deteriorated. While correcting these problems, John also reduced employment from a bloated 40,000 to 23,000. In short, he's been restoring the old Fruit of the Loom, albeit in a much more competitive environment.

Stepping into Fruit's bankruptcy proceedings, we made a proposal to creditors to which we attached no financing conditions, even though our offer had to remain outstanding for many months. We did, however, insist on a very unusual proviso: John had to be available to continue serving as CEO after we took over. To us, John and the brand are Fruit's key assets.

I was helped in this transaction by my friend and former boss, Micky Newman, now 81. What goes around truly does come around.

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Our operating companies made several "bolt-on" acquisitions during the year, and I can't resist telling you about one. In December, Frank Rooney called to tell me H.H. Brown was buying the inventory and trademarks of Acme Boot for $700,000.

That sounds like small potatoes. But – would you believe it? – Acme was the second purchase of P&R, an acquisition that took place just before I left Graham-Newman in the spring of 1956. The price was $3.2 million, part of it again paid with non-interest bearing notes, for a business with sales of $7 million.

After P&R merged with Northwest, Acme grew to be the world's largest bootmaker, delivering annual profits many multiples of what the company had cost P&R. But the business eventually hit the skids and never recovered, and that resulted in our purchasing Acme's remnants.

In the frontispiece to *Security Analysis*, Ben Graham and Dave Dodd quoted Horace: "Many shall be restored that now are fallen and many shall fall that are now in honor." Fifty-two years after I first read those lines, my appreciation for what they say about business and investments continues to grow.

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In addition to bolt-on acquisitions, our managers continually look for ways to grow internally. In that regard, here's a postscript to a story I told you two years ago about R.C. Willey's move to Boise. As you may remember, Bill Child, R.C. Willey's chairman, wanted to extend his home-furnishings operation beyond Utah, a state in which his company does more than $300 million of business (up, it should be noted, from $250,000 when Bill took over 48 years ago). The company achieved this dominant position, moreover, with a "closed on Sunday" policy that defied conventional retailing wisdom. I was skeptical that this policy could succeed in Boise or, for that matter, anyplace outside of Utah. After all, Sunday is the day many consumers most like to shop.

Bill then insisted on something extraordinary: He would invest $11 million of his own money to build the Boise store and would sell it to Berkshire at cost (without interest!) if the venture succeeded. If it failed, Bill would keep the store and eat the loss on its disposal. As I told you in the 1999 annual report, the store immediately became a huge success — and it has since grown.

Shortly after the Boise opening, Bill suggested we try Las Vegas, and this time I was even more skeptical. How could we do business in a metropolis of that size and be closed on Sundays, a day that all of our competitors would be exploiting? Buoyed by the Boise experience, however, we proceeded to locate in Henderson, a mushrooming city adjacent to Las Vegas.

The result: This store outsells all others in the R.C. Willey chain, doing a volume of business that far exceeds the volume of any competitor and that is twice what I had anticipated. I cut the ribbon at the grand opening in October – this was after a "soft" opening and a few weeks of exceptional sales – and, just as I did at Boise, I suggested to the crowd that the new store was my idea.

It didn't work. Today, when I pontificate about retailing, Berkshire people just say, "What does Bill think?" (I'm going to draw the line, however, if he suggests that we also close on Saturdays.)

The Economics of Property/Casualty Insurance

Our main business — though we have others of great importance — is insurance. To understand Berkshire, therefore, it is necessary that you understand how to evaluate an insurance company. The key determinants are: (1) the amount of float that the business generates; (2) its cost; and (3) most critical of all, the long-term outlook for both of these factors.

To begin with, float is money we hold but don't own. In an insurance operation, float arises because premiums are received before losses are paid, an interval that sometimes extends over many years. During that time, the insurer invests the money. This pleasant activity typically carries with it a downside: The premiums that an insurer takes in usually do not cover the losses and expenses it eventually must pay. That leaves it running an "underwriting loss," which is the cost of float. An insurance business has value if its cost of float over time is less than the cost the company would otherwise incur to obtain funds. But the business is a lemon if its cost of float is higher than market rates for money.

Historically, Berkshire has obtained its float at a very low cost. Indeed, our cost has been less than zero in about half of the years in which we've operated; that is, we've actually been paid for holding other people's money. Over the last few years, however, our cost has been too high, and in 2001 it was terrible.

The table that follows shows (at intervals) the float generated by the various segments of Berkshire's insurance operations since we entered the business 35 years ago upon acquiring National Indemnity Company (whose traditional lines are included in the segment "Other Primary"). For the table we have calculated our float — which we generate in large amounts relative to our premium volume — by adding net loss reserves, loss adjustment reserves, funds held under reinsurance assumed and unearned premium reserves, and then subtracting insurance-related receivables, prepaid acquisition costs, prepaid taxes and deferred charges applicable to assumed reinsurance. (Got that?)

Yearend Float (in $ millions)

Year	GEICO	General Re	Other Reinsurance	Other Primary	Total
1967				20	20
1977			40	131	171
1987			701	807	1,508
1997	2,917		4,014	455	7,386
1998	3,125	14,909	4,305	415	22,754
1999	3,444	15,166	6,285	403	25,298
2000	3,943	15,525	7,805	598	27,871
2001	4,251	19,310	11,262	685	35,508

Last year I told you that, barring a mega-catastrophe, our cost of float would probably drop from its 2000 level of 6%. I had in mind natural catastrophes when I said that, but instead we were hit by a man-made catastrophe on September 11th – an event that delivered the insurance industry its largest loss in history. Our float cost therefore came in at a staggering 12.8%. It was our worst year in float cost since 1984, and a result that to a significant degree, as I will explain in the next section, we brought upon ourselves.

If no mega-catastrophe occurs, I – once again – expect the cost of our float to be low in the coming year. We will indeed need a low cost, as will *all* insurers. Some years back, float costing, say, 4% was tolerable because government bonds yielded twice as much, and stocks prospectively offered still loftier returns. Today, fat returns are nowhere to be found (at least *we* can't find them) and short-term funds earn less than 2%. Under these conditions, each of our insurance operations, save one, must deliver an underwriting profit if it is to be judged a good business. The exception is our retroactive reinsurance operation (a business we explained in last year's annual report), which has desirable economics even though it currently hits us with an annual underwriting loss of about $425 million.

Principles of Insurance Underwriting

When property/casualty companies are judged by their cost of float, very few stack up as satisfactory businesses. And interestingly – unlike the situation prevailing in many other industries – neither size nor brand name determines an insurer's profitability. Indeed, many of the biggest and best-known companies regularly deliver mediocre results. What counts in this business is underwriting discipline. The winners are those that unfailingly stick to three key principles:

1. *They accept only those risks that they are able to properly evaluate (staying within their circle of competence) and that, after they have evaluated all relevant factors including remote loss scenarios, carry the expectancy of profit. These insurers ignore market-share considerations and are sanguine about losing business to competitors that are offering foolish prices or policy conditions.*

2. *They limit the business they accept in a manner that guarantees they will suffer no aggregation of losses from a single event or from related events that will threaten their solvency. They ceaselessly search for possible correlation among seemingly-unrelated risks.*

3. *They avoid business involving moral risk: No matter what the rate, trying to write good contracts with bad people doesn't work. While most policyholders and clients are honorable and ethical, doing business with the few exceptions is usually expensive, sometimes extraordinarily so.*

The events of September 11th made it clear that our implementation of rules 1 and 2 at General Re had been dangerously weak. In setting prices and also in evaluating aggregation risk, we had either overlooked or dismissed the possibility of large-scale terrorism losses. That was a relevant underwriting factor, and we ignored it.

In pricing property coverages, for example, we had looked to the past and taken into account only costs we might expect to incur from windstorm, fire, explosion and earthquake. But what will be the largest insured property loss in history (after adding related business-interruption claims) originated from none of these forces. In short, all of us in the industry made a fundamental underwriting mistake by focusing on experience, rather than exposure, thereby assuming a huge terrorism risk for which we received no premium.

Experience, of course, is a highly useful starting point in underwriting most coverages. For example, it's important for insurers writing California earthquake policies to know how many quakes in the state during the past century have registered 6.0 or greater on the Richter scale. This information will not tell you the exact probability of a big quake next year, or where in the state it might happen. But the statistic has utility, particularly if you are writing a huge statewide policy, as National Indemnity has done in recent years.

At certain times, however, using experience as a guide to pricing is not only useless, but actually dangerous. Late in a bull market, for example, large losses from directors and officers liability insurance ("D&O") are likely to be relatively rare. When stocks are rising, there are a scarcity of targets to sue, and both questionable accounting and management chicanery often go undetected. At that juncture, experience on high-limit D&O may look great.

But that's just when *exposure* is likely to be exploding, by way of ridiculous public offerings, earnings manipulation, chain-letter-like stock promotions and a potpourri of other unsavory activities. When stocks fall, these sins surface, hammering investors with losses that can run into the hundreds of billions. Juries deciding whether those losses should be borne by small investors or big insurance companies can be expected to hit insurers with verdicts that bear little relation to those delivered in bull-market days. Even one jumbo judgment, moreover, can cause settlement costs in later cases to mushroom. Consequently, the correct rate for D&O "excess" (meaning the insurer or reinsurer will pay losses above a high threshold) might well, if based on *exposure*, be five or more times the premium dictated by *experience*.

Insurers have always found it costly to ignore new exposures. Doing that in the case of terrorism, however, could literally bankrupt the industry. No one knows the probability of a nuclear detonation in a major metropolis this year (or even multiple detonations, given that a terrorist organization able to construct one bomb might not stop there). Nor can anyone, with assurance, assess the probability in this year, or another, of deadly biological or chemical agents being introduced simultaneously (say, through ventilation systems) into multiple office buildings and manufacturing plants. An attack like that would produce astronomical workers' compensation claims.

Here's what we *do* know:

(a) The probability of such mind-boggling disasters, though likely very low at present, is not zero.

(b) The probabilities are increasing, in an irregular and immeasurable manner, as knowledge and materials become available to those who wish us ill. Fear may recede with time, but the danger won't – the war against terrorism can never be won. The best the nation can achieve is a long succession of stalemates. There can be no checkmate against hydra-headed foes.

(c) Until now, insurers and reinsurers have blithely assumed the financial consequences from the incalculable risks I have described.

(d) Under a "close-to-worst-case" scenario, which could conceivably involve $1 trillion of damage, the insurance industry would be destroyed unless it manages in some manner to dramatically limit its assumption of terrorism risks. Only the U.S. Government has the resources to absorb such a blow. If it is unwilling to do so on a prospective basis, the general citizenry must bear its own risks and count on the Government to come to its rescue after a disaster occurs.

Why, you might ask, didn't I recognize the above facts *before* September 11th? The answer, sadly, is that I did – but I didn't convert thought into action. I violated the Noah rule: Predicting rain doesn't count; building arks does. I consequently let Berkshire operate with a dangerous level of risk – at General Re in particular. I'm sorry to say that much risk for which we haven't been compensated remains on our books, but it is running off by the day.

At Berkshire, it should be noted, we have for some years been willing to assume more risk than any other insurer has *knowingly* taken on. That's still the case. We are perfectly willing to lose $2 billion to $2½ billion in a single event (as we did on September 11th) if we have been paid properly for assuming the risk that caused the loss (which on that occasion we weren't).

Indeed, we have a major competitive advantage because of our tolerance for huge losses. Berkshire has massive liquid resources, substantial non-insurance earnings, a favorable tax position and a knowledgeable shareholder constituency willing to accept volatility in earnings. This unique combination enables us to assume risks that far exceed the appetite of even our largest competitors. Over time, insuring these jumbo risks should be profitable, though periodically they will bring on a terrible year.

The bottom-line today is that we will write some coverage for terrorist-related losses, including a few non-correlated policies with very large limits. But we will not knowingly expose Berkshire to losses beyond what we can comfortably handle. We will control our total exposure, no matter what the competition does.

Insurance Operations in 2001

Over the years, our insurance business has provided ever-growing, low-cost funds that have fueled much of Berkshire's growth. Charlie and I believe this will continue to be the case. But we stumbled in a big way in 2001, largely because of underwriting losses at General Re.

In the past I have assured you that General Re was underwriting with discipline – and I have been proven wrong. Though its managers' intentions were good, the company broke each of the three underwriting rules I set forth in the last section and has paid a huge price for doing so. One obvious cause for its failure is that it did not reserve correctly – more about this in the next section – and therefore severely miscalculated the cost of the product it was selling. Not knowing your costs will cause problems in any business. In long-tail reinsurance, where years of unawareness will promote and prolong severe underpricing, ignorance of true costs is dynamite.

Additionally, General Re was overly-competitive in going after, and retaining, business. While all concerned may intend to underwrite with care, it is nonetheless difficult for able, hard-driving professionals to curb their urge to prevail over competitors. If "winning," however, is equated with market share rather than profits, trouble awaits. "No" must be an important part of any underwriter's vocabulary.

At the risk of sounding Pollyannaish, I now assure you that underwriting discipline is being restored at General Re (and its Cologne Re subsidiary) with appropriate urgency. Joe Brandon was appointed General Re's CEO in September and, along with Tad Montross, its new president, is committed to producing underwriting profits. Last fall, Charlie and I read Jack Welch's terrific book, *Jack, Straight from the Gut* (get a copy!). In discussing it, we agreed that Joe has many of Jack's characteristics: He is smart, energetic, hands-on, and expects much of both himself and his organization.

When it was an independent company, General Re often shone, and now it also has the considerable strengths Berkshire brings to the table. With that added advantage and with underwriting discipline restored, General Re should be a huge asset for Berkshire. I predict that Joe and Tad will make it so.

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At the National Indemnity reinsurance operation, Ajit Jain continues to add enormous value to Berkshire. Working with only 18 associates, Ajit manages one of the world's largest reinsurance operations measured by assets, and *the* largest, based upon the size of individual risks assumed.

I have known the details of almost every policy that Ajit has written since he came with us in 1986, and never on even a single occasion have I seen him break any of our three underwriting rules. His extraordinary discipline, of course, does not eliminate losses; it does, however, prevent foolish losses. And that's the key: Just as is the case in investing, insurers produce outstanding long-term results primarily by avoiding dumb decisions, rather than by making brilliant ones.

Since September 11th, Ajit has been particularly busy. Among the policies we have written and retained entirely for our own account are (1) $578 million of property coverage for a South American refinery once a loss there exceeds $1 billion; (2) $1 billion of non-cancelable third-party liability coverage for losses arising from acts of terrorism at several large international airlines; (3) £500 million of property coverage on a large North Sea oil platform, covering losses from terrorism and sabotage, above £600 million that the insured retained or reinsured elsewhere; and (4) significant coverage on the Sears Tower, including losses caused by terrorism, above a $500 million threshold. We have written many other jumbo risks as well, such as protection for the World Cup Soccer Tournament and the 2002 Winter Olympics. In all cases, however, we have attempted to avoid writing groups of policies from which losses might seriously aggregate. We will not, for example, write coverages on a large number of office and apartment towers in a single metropolis without excluding losses from both a nuclear explosion and the fires that would follow it.

No one can match the speed with which Ajit can offer huge policies. After September 11th, his quickness to respond, always important, has become a major competitive advantage. So, too, has our unsurpassed financial strength. Some reinsurers – particularly those who, in turn, are accustomed to laying off much of their business on a second layer of reinsurers known as retrocessionaires – are in a weakened condition and would have difficulty surviving a second mega-cat. When a daisy chain of retrocessionaires exists, a single weak link can pose trouble for all. In assessing the soundness of their reinsurance protection, insurers must therefore apply a stress test to all participants in the chain, and must contemplate a catastrophe loss occurring during a very unfavorable economic environment. After all, you only find out who is swimming naked when the tide goes out. At Berkshire, we retain our risks and depend on no one. And whatever the world's problems, our checks will clear.

Ajit's business will ebb and flow – but his underwriting principles won't waver. It's impossible to overstate his value to Berkshire.

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GEICO, by far our largest primary insurer, made major progress in 2001, thanks to Tony Nicely, its CEO, and his associates. Quite simply, Tony is an owner's dream.

GEICO's premium volume grew 6.6% last year, its float grew $308 million, and it achieved an underwriting profit of $221 million. This means we were actually paid that amount last year to hold the $4.25 billion in float, which of course doesn't belong to Berkshire but can be used by us for investment.

The only disappointment at GEICO in 2001 – and it's an important one – was our inability to add policyholders. Our preferred customers (81% of our total) grew by 1.6% but our standard and non-standard policies fell by 10.1%. Overall, policies in force fell .8%.

New business has improved in recent months. Our closure rate from telephone inquiries has climbed, and our Internet business continues its steady growth. We, therefore, expect at least a modest gain in policy count during 2002. Tony and I are eager to commit much more to marketing than the $219 million we spent last year, but at the moment we cannot see how to do so effectively. In the meantime, our operating costs are low and far below those of our major competitors; our prices are attractive; and our float is cost-free and growing.

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Our other primary insurers delivered their usual fine results last year. These operations, run by Rod Eldred, John Kizer, Tom Nerney, Michael Stearns, Don Towle and Don Wurster had combined premium volume of $579 million, up 40% over 2000. Their float increased 14.5% to $685 million, and they recorded an underwriting profit of $30 million. In aggregate, these companies are one of the finest insurance operations in the country, and their 2002 prospects look excellent.

"Loss Development" and Insurance Accounting

Bad terminology is the enemy of good thinking. When companies or investment professionals use terms such as "EBITDA" and "pro forma," they want you to unthinkingly accept concepts that are dangerously flawed. (In golf, my score is frequently below par on a *pro forma* basis: I have firm plans to "restructure" my putting stroke and therefore only count the swings I take before reaching the green.)

In insurance reporting, "loss development" is a widely used term – and one that is seriously misleading. First, a definition: Loss reserves at an insurer are not funds tucked away for a rainy day, but rather a liability account. If properly calculated, the liability states the amount that an insurer will have to pay for *all* losses (including associated costs) that have occurred prior to the reporting date but have not yet been paid. When calculating the reserve, the insurer will have been notified of many of the losses it is destined to pay, but others will not yet have been reported to it. These losses are called IBNR, for incurred but not reported. Indeed, in some cases (involving, say, product liability or embezzlement) the insured itself will not yet be aware that a loss has occurred.

It's clearly difficult for an insurer to put a figure on the ultimate cost of all such reported and unreported events. But the ability to do so with reasonable accuracy is vital. Otherwise the insurer's managers won't know what its actual loss costs are and how these compare to the premiums being charged. GEICO got into huge trouble in the early 1970s because for several years it severely underreserved, and therefore believed its product (insurance protection) was costing considerably less than was truly the case. Consequently, the company sailed blissfully along, underpricing its product and selling more and more policies at ever-larger losses.

When it becomes evident that reserves at past reporting dates understated the liability that truly existed at the time, companies speak of "loss development." In the year discovered, these shortfalls penalize reported earnings because the "catch-up" costs from prior years must be added to current-year costs when results are calculated. This is what happened at General Re in 2001: a staggering $800 million of loss costs that actually occurred in earlier years, but that were not then recorded, were belatedly recognized last year and charged against current earnings. The mistake was an honest one, I can assure you of that. Nevertheless, for several years, this underreserving caused us to believe that our costs were much lower than they truly were, an error that contributed to woefully inadequate pricing. Additionally, the overstated profit figures led us to pay substantial incentive compensation that we should not have and to incur income taxes far earlier than was necessary.

We recommend scrapping the term "loss development" and its equally ugly twin, "reserve strengthening." (Can you imagine an insurer, upon finding its reserves excessive, describing the reduction that follows as "reserve weakening"?) "Loss development" suggests to investors that some natural, uncontrollable event has occurred in the current year, and "reserve strengthening" implies that adequate amounts have been further buttressed. The truth, however, is that management made an error in estimation that in turn produced an error in the earnings previously reported. The losses didn't "develop" – they were there all along. What developed was management's understanding of the losses (or, in the instances of chicanery, management's willingness to finally fess up).

A more forthright label for the phenomenon at issue would be "loss costs we failed to recognize when they occurred" (or maybe just "oops"). Underreserving, it should be noted, is a common – and serious – problem throughout the property/casualty insurance industry. At Berkshire we told you of our own problems with underestimation in 1984 and 1986. Generally, however, our reserving has been conservative.

Major underreserving is common in cases of companies struggling for survival. In effect, insurance accounting is a self-graded exam, in that the insurer gives some figures to its auditing firm and generally doesn't get an argument. (What the *auditor* gets, however, is a letter from management that is designed to take his firm off the hook if the numbers later look silly.) A company experiencing financial difficulties – of a kind that, if truly faced, could put it out of business – seldom proves to be a tough grader. Who, after all, wants to prepare his own execution papers?

Even when companies have the best of intentions, it's not easy to reserve properly. I've told the story in the past about the fellow traveling abroad whose sister called to tell him that their dad had died. The brother replied that it was impossible for him to get home for the funeral; he volunteered, however, to shoulder its cost. Upon returning, the brother received a bill from the mortuary for $4,500, which he promptly paid. A month later, and a month after that also, he paid $10 pursuant to an add-on invoice. When a third $10 invoice came, he called his sister for an explanation. "Oh," she replied, "I forgot to tell you. We buried dad in a rented suit."

There are a lot of "rented suits" buried in the past operations of insurance companies. Sometimes the problems they signify lie dormant for decades, as was the case with asbestos liability, before virulently manifesting themselves. Difficult as the job may be, it's management's responsibility to adequately account for *all* possibilities. Conservatism is essential. When a claims manager walks into the CEO's office and says "Guess what just happened," his boss, if a veteran, does not expect to hear it's good news. Surprises in the insurance world have been far from symmetrical in their effect on earnings.

Because of this one-sided experience, it is folly to suggest, as some are doing, that all property/casualty insurance reserves be *discounted*, an approach reflecting the fact that they will be paid in the future and that therefore their present value is less than the stated liability for them. Discounting might be acceptable *if* reserves could be precisely established. They can't, however, because a myriad of forces – judicial broadening of policy language and medical inflation, to name just two chronic problems – are constantly working to make reserves inadequate. Discounting would exacerbate this already-serious situation and, additionally, would provide a new tool for the companies that are inclined to fudge.

I'd say that the effects from telling a profit-challenged insurance CEO to lower reserves through discounting would be comparable to those that would ensue if a father told his 16-year-old son to have a normal sex life. Neither party needs that kind of push.

Sources of Reported Earnings

The table that follows shows the main sources of Berkshire's reported earnings. In this presentation, purchase-accounting adjustments (primarily relating to "goodwill") are not assigned to the specific businesses to which they apply, but are instead aggregated and shown separately. This procedure lets you view the earnings of our businesses as they would have been reported had we not purchased them. In recent years, our "expense" for goodwill amortization has been large. Going forward, generally accepted accounting principles ("GAAP") will no longer require amortization of goodwill. This change will increase our reported earnings (though not our true economic earnings) and simplify this section of the report.

	(in millions)			
	Pre-Tax Earnings		*Berkshire's Share of Net Earnings (after taxes and Minority interests)*	
	2001	*2000*	*2001*	*2000*
Operating Earnings:				
Insurance Group:				
Underwriting – Reinsurance	$(4,318)	$(1,416)	$(2,824)	$(911)
Underwriting – GEICO	221	(224)	144	(146)
Underwriting – Other Primary	30	25	18	16
Net Investment Income	2,824	2,773	1,968	1,946
Building Products[1]	461	34	287	21
Finance and Financial Products Business	519	530	336	343
Flight Services	186	213	105	126
MidAmerican Energy (76% owned)	600	197	230	109
Retail Operations	175	175	101	104
Scott Fetzer (excluding finance operation)	129	122	83	80
Shaw Industries[2]	292	--	156	--
Other Businesses	179	221	103	133
Purchase-Accounting Adjustments	(726)	(881)	(699)	(843)
Corporate Interest Expense	(92)	(92)	(60)	(61)
Shareholder-Designated Contributions	(17)	(17)	(11)	(11)
Other	25	39	16	30
Operating Earnings	488	1,699	(47)	936
Capital Gains from Investments	1,320	3,955	842	2,392
Total Earnings – All Entities	$1,808	$5,654	$ 795	$3,328

(1) *Includes Acme Brick from August 1, 2000; Benjamin Moore from December 18, 2000; Johns Manville from February 27, 2001; and MiTek from July 31, 2001.*

(2) *From date of acquisition, January 8, 2001.*

Here are some highlights (and lowlights) from 2001 relating to our non-insurance activities:

- Our shoe operations (included in "other businesses") lost $46.2 million pre-tax, with profits at H.H. Brown and Justin swamped by losses at Dexter.

  I've made three decisions relating to Dexter that have hurt you in a major way: (1) buying it in the first place; (2) paying for it with stock and (3) procrastinating when the need for changes in its operations was obvious. I would like to lay these mistakes on Charlie (or anyone else, for that matter) but they were mine. Dexter, prior to our purchase – and indeed for a few years after – prospered despite low-cost foreign competition that was brutal. I concluded that Dexter could continue to cope with that problem, and I was wrong.

  We have now placed the Dexter operation – which is still substantial in size – under the management of Frank Rooney and Jim Issler at H.H. Brown. These men have performed outstandingly for Berkshire, skillfully contending with the extraordinary changes that have bedeviled the footwear industry. During part of 2002, Dexter will be hurt by unprofitable sales commitments it made last year. After that, we believe our shoe business will be reasonably profitable.

- MidAmerican Energy, of which we own 76% on a fully-diluted basis, had a good year in 2001. Its reported earnings should also increase considerably in 2002 given that the company has been shouldering a large charge for the amortization of goodwill and that this "cost" will disappear under the new GAAP rules.

  Last year MidAmerican swapped some properties in England, adding Yorkshire Electric, with its 2.1 million customers. We are now serving 3.6 million customers in the U.K. and are its 2nd largest electric utility. We have an equally important operation in Iowa as well as major generating facilities in California and the Philippines.

  At MidAmerican – this may surprise you – we also own the second-largest residential real estate brokerage business in the country. We are market-share leaders in a number of large cities, primarily in the Midwest, and have recently acquired important firms in Atlanta and Southern California. Last year, operating under various names that are locally familiar, we handled about 106,000 transactions involving properties worth nearly $20 billion. Ron Peltier has built this business for us, and it's likely he will make more acquisitions in 2002 and the years to come.

- Considering the recessionary environment plaguing them, our retailing operations did well in 2001. In jewelry, same-store sales fell 7.6% and pre-tax margins were 8.9% versus 10.7% in 2000. Return on invested capital remains high.

  Same-store sales at our home-furnishings retailers were unchanged and so was the margin – 9.1% pre-tax – these operations earned. Here, too, return on invested capital is excellent.

  We continue to expand in both jewelry and home-furnishings. Of particular note, Nebraska Furniture Mart is constructing a mammoth 450,000 square foot store that will serve the greater Kansas City area beginning in the fall of 2003. Despite Bill Child's counter-successes, we will keep this store open on Sundays.

- The large acquisitions we initiated in late 2000 – Shaw, Johns Manville and Benjamin Moore – all came through their first year with us in great fashion. Charlie and I knew at the time of our purchases that we were in good hands with Bob Shaw, Jerry Henry and Yvan Dupuy, respectively – and we admire their work even more now. Together these businesses earned about $659 million pre-tax.

  Shortly after yearend we exchanged 4,740 Berkshire A shares (or their equivalent in B shares) for the 12.7% minority interest in Shaw, which means we now own 100% of the company. Shaw is our largest non-insurance operation and will play a big part in Berkshire's future.

- All of the income shown for Flight Services in 2001 – and a bit more – came from FlightSafety, our pilot-training subsidiary. Its earnings increased 2.5%, though return on invested capital fell slightly because of the $258 million investment we made last year in simulators and other fixed assets. My 84-year-old friend, Al Ueltschi, continues to run FlightSafety with the same enthusiasm and competitive spirit that he has exhibited since 1951, when he invested $10,000 to start the company. If I line Al up with a bunch of 60-year-olds at the annual meeting, you will not be able to pick him out.

After September 11th, training for commercial airlines fell, and today it remains depressed. However, training for business and general aviation, our main activity, is at near-normal levels and should continue to grow. In 2002, we expect to spend $162 million for 27 simulators, a sum far in excess of our annual depreciation charge of $95 million. Those who believe that EBITDA is in any way equivalent to true earnings are welcome to pick up the tab.

Our NetJets® fractional ownership program sold a record number of planes last year and also showed a gain of 21.9% in service income from management fees and hourly charges. Nevertheless, it operated at a small loss, versus a small profit in 2000. We made a little money in the U.S., but these earnings were more than offset by European losses. Measured by the value of our customers' planes, NetJets accounts for about half of the industry. We believe the other participants, in aggregate, lost significant money.

Maintaining a premier level of safety, security and service was always expensive, and the cost of sticking to those standards was exacerbated by September 11th. No matter how much the cost, we will continue to be the industry leader in all three respects. An uncompromising insistence on delivering only the best to his customers is embedded in the DNA of Rich Santulli, CEO of the company and the inventor of fractional ownership. I'm delighted with his fanaticism on these matters for both the company's sake and my family's: I believe the Buffetts fly more fractional-ownership hours – we log in excess of 800 annually – than does any other family. In case you're wondering, we use exactly the same planes and crews that serve NetJet's other customers.

NetJets experienced a spurt in new orders shortly after September 11th, but its sales pace has since returned to normal. Per-customer usage declined somewhat during the year, probably because of the recession.

Both we and our customers derive significant operational benefits from our being the runaway leader in the fractional ownership business. We have more than 300 planes constantly on the go in the U.S. and can therefore be wherever a customer needs us on very short notice. The ubiquity of our fleet also reduces our "positioning" costs below those incurred by operators with smaller fleets.

These advantages of scale, and others we have, give NetJets a significant economic edge over competition. Under the competitive conditions likely to prevail for a few years, however, our advantage will at best produce modest profits.

- Our finance and financial products line of business now includes XTRA, General Re Securities (which is in a run-off mode that will continue for an extended period) and a few other relatively small operations. The bulk of the assets and liabilities in this segment, however, arise from a few fixed-income strategies, involving highly-liquid AAA securities, that I manage. This activity, which only makes sense when certain market relationships exist, has produced good returns in the past and has reasonable prospects for continuing to do so over the next year or two.

Investments

Below we present our common stock investments. Those that had a market value of more than $500 million at the end of 2001 are itemized.

Shares	*Company*	*12/31/01* *Cost*	*Market*
		(dollars in millions)	
151,610,700	American Express Company	$ 1,470	$ 5,410
200,000,000	The Coca-Cola Company	1,299	9,430
96,000,000	The Gillette Company	600	3,206
15,999,200	H&R Block, Inc.	255	715
24,000,000	Moody's Corporation	499	957
1,727,765	The Washington Post Company	11	916
53,265,080	Wells Fargo & Company	306	2,315
	Others	4,103	5,726
	Total Common Stocks	$8,543	$28,675

We made few changes in our portfolio during 2001. As a group, our larger holdings have performed poorly in the last few years, some because of disappointing operating results. Charlie and I still like the basic businesses of all the companies we own. But we do not believe Berkshire's equity holdings as a group are undervalued.

Our restrained enthusiasm for these securities is matched by decidedly lukewarm feelings about the prospects for stocks in general over the next decade or so. I expressed my views about equity returns in a speech I gave at an Allen and Company meeting in July (which was a follow-up to a similar presentation I had made two years earlier) and an edited version of my comments appeared in a December 10th *Fortune* article. I'm enclosing a copy of that article. You can also view the *Fortune* version of my 1999 talk at our website www.berkshirehathaway.com.

Charlie and I believe that American business will do fine over time but think that today's equity prices presage only moderate returns for investors. The market outperformed business for a very long period, and that phenomenon had to end. A market that no more than parallels business progress, however, is likely to leave many investors disappointed, particularly those relatively new to the game.

Here's one for those who enjoy an odd coincidence: The Great Bubble ended on March 10, 2000 (though we didn't realize that fact until some months later). On that day, the NASDAQ (recently 1,731) hit its all-time high of 5,132. That same day, Berkshire shares traded at $40,800, their lowest price since mid-1997.

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During 2001, we were somewhat more active than usual in "junk" bonds. These are not, we should emphasize, suitable investments for the general public, because too often these securities live up to their name. We have *never* purchased a newly-issued junk bond, which is the only kind most investors are urged to buy. When losses occur in this field, furthermore, they are often disastrous: Many issues end up at a small fraction of their original offering price and some become entirely worthless.

Despite these dangers, we periodically find a few – a *very* few – junk securities that are interesting to us. And, so far, our 50-year experience in distressed debt has proven rewarding. In our 1984 annual report, we described our purchases of Washington Public Power System bonds when that issuer fell into disrepute. We've also, over the years, stepped into other apparent calamities such as Chrysler Financial, Texaco and RJR Nabisco – all of which returned to grace. Still, if we stay active in junk bonds, you can expect us to have losses from time to time.

Occasionally, a purchase of distressed bonds leads us into something bigger. Early in the Fruit of the Loom bankruptcy, we purchased the company's public and bank debt at about 50% of face value. This was an unusual bankruptcy in that interest payments on senior debt were continued without interruption, which meant we earned about a 15% current return. Our holdings grew to 10% of Fruit's senior debt, which will probably end up returning us about 70% of face value. Through this investment, we indirectly reduced our purchase price for the whole company by a small amount.

In late 2000, we began purchasing the obligations of FINOVA Group, a troubled finance company, and that, too, led to our making a major transaction. FINOVA then had about $11 billion of debt outstanding, of which we purchased 13% at about two-thirds of face value. We expected the company to go into bankruptcy, but believed that liquidation of its assets would produce a payoff for creditors that would be well above our cost. As default loomed in early 2001, we joined forces with Leucadia National Corporation to present the company with a prepackaged plan for bankruptcy.

The plan as subsequently modified (and I'm simplifying here) provided that creditors would be paid 70% of face value (along with full interest) and that they would receive a newly-issued 7½% note for the 30% of their claims not satisfied by cash. To fund FINOVA's 70% distribution, Leucadia and Berkshire formed a jointly-owned entity – mellifluently christened Berkadia – that borrowed $5.6 billion through FleetBoston and, in turn, re-lent this sum to FINOVA, concurrently obtaining a priority claim on its assets. Berkshire guaranteed 90% of the Berkadia borrowing and also has a secondary guarantee on the 10% for which Leucadia has primary responsibility. (Did I mention that I am simplifying?).

There is a spread of about two percentage points between what Berkadia pays on its borrowing and what it receives from FINOVA, with this spread flowing 90% to Berkshire and 10% to Leucadia. As I write this, each loan has been paid down to $3.9 billion.

As part of the bankruptcy plan, which was approved on August 10, 2001, Berkshire also agreed to offer 70% of face value for up to $500 million principal amount of the $3.25 billion of new 7½% bonds that were issued by FINOVA. (Of these, we had already received $426.8 million in principal amount because of our 13% ownership of the original debt.) Our offer, which was to run until September 26, 2001, could be withdrawn under a variety of conditions, one of which became operative if the New York Stock Exchange closed during the offering period. When that indeed occurred in the week of September 11th, we promptly terminated the offer.

Many of FINOVA's loans involve aircraft assets whose values were significantly diminished by the events of September 11th. Other receivables held by the company also were imperiled by the economic consequences of the attack that day. FINOVA's prospects, therefore, are not as good as when we made our proposal to the bankruptcy court. Nevertheless we feel that overall the transaction will prove satisfactory for Berkshire. Leucadia has day-to-day operating responsibility for FINOVA, and we have long been impressed with the business acumen and managerial talent of its key executives.

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It's déjà vu time again: In early 1965, when the investment partnership I ran took control of Berkshire, that company had its main banking relationships with First National Bank of Boston and a large New York City bank. Previously, I had done no business with either.

Fast forward to 1969, when I wanted Berkshire to buy the Illinois National Bank and Trust of Rockford. We needed $10 million, and I contacted both banks. There was no response from New York. However, two representatives of the Boston bank immediately came to Omaha. They told me they would supply the money for our purchase and that we would work out the details later.

For the next three decades, we borrowed almost nothing from banks. (Debt is a four-letter word around Berkshire.) Then, in February, when we were structuring the FINOVA transaction, I again called Boston, where First National had morphed into FleetBoston. Chad Gifford, the company's president, responded just as Bill Brown and Ira Stepanian had back in 1969 – "you've got the money and we'll work out the details later."

And that's just what happened. FleetBoston syndicated a loan for $6 billion (as it turned out, we didn't need $400 million of it), and it was quickly oversubscribed by 17 banks throughout the world. Sooooo . . . if you ever need $6 billion, just give Chad a call – assuming, that is, your credit is AAA.

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One more point about our investments: The media often report that "Buffett is buying" this or that security, having picked up the "fact" from reports that Berkshire files. These accounts are sometimes correct, but at other times the transactions Berkshire reports are actually being made by Lou Simpson, who runs a $2 billion portfolio for GEICO that is quite independent of me. Normally, Lou does not tell me what he is buying or selling, and I learn of his activities only when I look at a GEICO portfolio summary that I receive a few days after the end of each month. Lou's thinking, of course, is quite similar to mine, but we usually end up in different securities. That's largely because he's working with less money and can therefore invest in smaller companies than I. Oh, yes, there's also another minor difference between us: In recent years, Lou's performance has been far better than mine.

Charitable Contributions

Berkshire follows a highly unusual policy in respect to charitable contributions – but it's one that Charlie and I believe is both rational and fair to owners.

First, we let our operating subsidiaries make their own charitable decisions, requesting only that the owners/managers who once ran these as independent companies make all donations to their *persona*l charities from their own funds, instead of using company money. When our managers are using company funds, we trust them to make gifts in a manner that delivers commensurate tangible or intangible benefits to the operations they manage. Last year contributions from Berkshire subsidiaries totaled $19.2 million.

At the parent company level, we make no contributions except those designated by shareholders. We do not match contributions made by directors or employees, nor do we give to the favorite charities of the Buffetts or the Mungers. However, prior to our purchasing them, a few of our subsidiaries had employee-match programs and we feel fine about their continuing them: It's not our style to tamper with successful business cultures.

To implement our *owners'* charitable desires, each year we notify registered holders of A shares (A's represent 86.6% of our equity capital) of a per-share amount that they can instruct us to contribute to as many as three charities. Shareholders name the charity; Berkshire writes the check. Any organization that qualifies under the Internal Revenue Code can be designated by shareholders. Last year Berkshire made contributions of $16.7 million at the direction of 5,700 shareholders, who named 3,550 charities as recipients. Since we started this program, our shareholders' gifts have totaled $181 million.

Most public corporations eschew gifts to religious institutions. These, however, are favorite charities of our shareholders, who last year named 437 churches and synagogues to receive gifts. Additionally, 790 schools were recipients. A few of our larger shareholders, including Charlie and me, designate their personal foundations to get gifts, so that those entities can, in turn, disburse their funds widely.

I get a few letters every week criticizing Berkshire for contributing to Planned Parenthood. These letters are usually prompted by an organization that wishes to see boycotts of Berkshire products. The letters are invariably polite and sincere, but their writers are unaware of a key point: It's not Berkshire, but rather its owners who are making charitable decisions – and these owners are about as diverse in their opinions as you can imagine. For example, they are probably on both sides of the abortion issue in roughly the same proportion as the American population. We'll follow their instructions, whether they designate Planned Parenthood or Metro Right to Life, just as long as the charity possesses 501(c)(3) status. It's as if we paid a dividend, which the shareholder then donated. Our form of disbursement, however, is more tax-efficient.

In neither the purchase of goods nor the hiring of personnel, do we ever consider the religious views, the gender, the race or the sexual orientation of the persons we are dealing with. It would not only be wrong to do so, it would be idiotic. We need all of the talent we can find, and we have learned that able and trustworthy managers, employees and suppliers come from a very wide spectrum of humanity.

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To participate in our future charitable contribution programs, you must own Class A shares that are registered in the name of the actual owner, not the nominee name of a broker, bank or depository. Shares not so registered on August 31, 2002 will be ineligible for the 2002 program. When you get the contributions form from us, return it promptly. Designations received after the due date will not be honored.

The Annual Meeting

This year's annual meeting will be on Saturday, May 4, and we will again be at the Civic Auditorium. The doors will open at 7 a.m., the movie will begin at 8:30, and the meeting itself will commence at 9:30. There will be a short break at noon for food. (Sandwiches can be bought at the Civic's concession stands.) Except for that interlude, Charlie and I will answer questions until 3:30. Give us your best shot.

For at least the next year, the Civic, located downtown, is the only site available to us. We must therefore hold the meeting on either Saturday or Sunday to avoid the traffic and parking nightmare sure to occur on a weekday. Shortly, however, Omaha will have a new Convention Center with plenty of parking facilities. Assuming that we then head for the Center, I will poll shareholders to see whether you wish to return to the Monday meeting that was standard until 2000. We will decide that vote based on a count of shareholders, not shares. (This is *not* a system, however, we will ever institute to decide who should be CEO.)

An attachment to the proxy material that is enclosed with this report explains how you can obtain the credential you will need for admission to the meeting and other events. As for plane, hotel and car reservations, we have again signed up American Express (800-799-6634) to give you special help. They do a terrific job for us each year, and I thank them for it.

In our usual fashion, we will run buses from the larger hotels to the meeting. Afterwards, the buses will make trips back to the hotels and to Nebraska Furniture Mart, Borsheim's and the airport. Even so, you are likely to find a car useful.

We have added so many new companies to Berkshire this year that I'm not going to detail all of the products that we will be *selling* at the meeting. But come prepared to carry home everything from bricks to candy. And underwear, of course. Assuming our Fruit of the Loom purchase has closed by May 4, we will be selling Fruit's latest styles, which will make you your neighborhood's fashion leader. Buy a lifetime supply.

GEICO will have a booth staffed by a number of its top counselors from around the country, all of them ready to supply you with auto insurance quotes. In most cases, GEICO will be able to give you a special shareholder discount (usually 8%). This special offer is permitted by 41 of the 49 jurisdictions in which we operate. Bring the details of your existing insurance and check out whether we can save you money.

At the Omaha airport on Saturday, we will have the usual array of aircraft from NetJets® available for your inspection. Just ask a representative at the Civic about viewing any of these planes. If you buy what we consider an appropriate number of items during the weekend, you may well need your own plane to take them home. And, if you buy a fraction of a plane, we might even throw in a three-pack of briefs or boxers.

At Nebraska Furniture Mart, located on a 75-acre site on 72nd Street between Dodge and Pacific, we will again be having "Berkshire Weekend" pricing, which means we will be offering our shareholders a discount that is customarily given only to employees. We initiated this special pricing at NFM five years ago, and sales during the "Weekend" grew from $5.3 million in 1997 to $11.5 million in 2001.

To get the discount, you must make your purchases on Thursday, May 2 through Monday, May 6 and also present your meeting credential. The period's special pricing will even apply to the products of several prestigious manufacturers that normally have ironclad rules against discounting but that, in the spirit of our shareholder weekend, have made an exception for you. We appreciate their cooperation. NFM is open from 10 a.m. to 9 p.m. on weekdays and 10 a.m. to 6 p.m. on Saturdays and Sundays.

Borsheim's — the largest jewelry store in the country except for Tiffany's Manhattan store — will have two shareholder-only events. The first will be a cocktail reception from 6 p.m. to 10 p.m. on Friday, May 3. The second, the main gala, will be from 9 a.m. to 5 p.m. on Sunday, May 5. Shareholder prices will be available Thursday through Monday, so if you wish to avoid the large crowds that will assemble on Friday evening and Sunday, come at other times and identify yourself as a shareholder. On Saturday, we will be open until 6 p.m. Borsheim's operates on a gross margin that is fully twenty percentage points below that of its major rivals, so the more you buy, the more you save (or at least that's what my wife and daughter tell me). Come by and let us perform a walletectomy on you.

In the mall outside of Borsheim's, we will have some of the world's top bridge experts available to play with our shareholders on Sunday afternoon. We expect Bob and Petra Hamman along with Sharon Osberg to host tables. Patrick Wolff, twice U.S. chess champion, will also be in the mall, taking on all comers — blindfolded!

Last year, Patrick played as many as six games simultaneously — with his blindfold securely in place — and this year will try for seven. Finally, Bill Robertie, one of only two players who have twice won the backgammon world championship, will be on hand to test your skill at that game. Come to the mall on Sunday for the Mensa Olympics.

Gorat's — my favorite steakhouse — will again be open exclusively for Berkshire shareholders on Sunday, May 5, and will be serving from 4 p.m. until 10 p.m. Please remember that to come to Gorat's on Sunday, you must have a reservation. To make one, call 402-551-3733 on April 1 (*but not before*). If Sunday is sold out, try Gorat's on one of the other evenings you will be in town. Show your sophistication by ordering a rare T-bone with a double order of hash browns.

The usual baseball game will be held at Rosenblatt Stadium at 7 p.m. on Saturday night. This year the Omaha Royals will play the Oklahoma RedHawks. Last year, in an attempt to emulate the career switch of Babe Ruth, I gave up pitching and tried batting. Bob Gibson, an Omaha native, was on the mound and I was terrified, fearing Bob's famous brush-back pitch. Instead, he delivered a fast ball in the strike zone, and with a Mark McGwire-like swing, I managed to connect for a hard grounder, which inexplicably died in the infield. I didn't run it out: At my age, I get winded playing a hand of bridge.

I'm not sure what will take place at the ballpark this year, but come out and be surprised. Our proxy statement contains instructions for obtaining tickets to the game. Those people ordering tickets to the annual meeting will receive a booklet containing all manner of information that should help you enjoy your visit in Omaha. There will be plenty of action in town. So come for Woodstock Weekend and join our Celebration of Capitalism at the Civic.

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Finally, I would like to thank the wonderful and incredibly productive crew at World Headquarters (all 5,246.5 square feet of it) who make my job so easy. Berkshire added about 40,000 employees last year, bringing our workforce to 110,000. At headquarters we added one employee and now have 14.8. (I've tried in vain to get JoEllen Rieck to change her workweek from four days to five; I think she likes the national recognition she gains by being .8.)

The smooth handling of the array of duties that come with our current size and scope – as well as some additional activities almost unique to Berkshire, such as our shareholder gala and designated-gifts program – takes a very special group of people. And that we most definitely have.

Warren E. Buffett
February 28, 2002 Chairman of the Board