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July 10, 1963

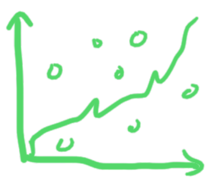
March 30, 2022

First Half Performance

Dow +10%

During the first half of 1963, the Dow Jones Industrial Average (hereinafter called the "Dow") advanced from 652.10 to 706.88. If one had owned the Dow during this period, dividends of $10.66 would have been received, bringing the overall return from the Dow during the first half to plus 10.0%

Bubbling market



Our incantation has been: (1) that short-term results (less than three year have little meaning, particularly in reference to an investment operation such as ours that devotes a portion of resources to control situations, and; (2) that our results, relative to the Dow and other common-stock-form me will be better in declining markets and may well have a difficult time just matching such media in bubbling markets.

Nevertheless, our first-half performance, excluding any change in Dempst valuation (and its valuation did change--I'm saving this for dessert later in the letter) was plus 14%. This 14% is computed on total net assets (not no Dempster assets) and is after expenses, but before monthly payments (to those who take them) to partners and allocation to the General Partner. S allocations are academic on an interim basis, but if we were also plus 14% at yearend, the first 6% would be allocated to partners according to their capital, plus three-quarters of the balance of 8% (14% - 6%), or an additio 6%, giving the limited partners a plus 12% performance.

+14% for the team!

+10% v. +14% less than satisfactory

Despite the relatively pleasant results of the first half, the admonitions stated two paragraphs earlier hold in full force. At plus 14% versus plus 10% for the Dow, this six months has been a less satisfactory period than the first half of 1962 when we were minus 7.5% versus minus 21.7% for th Dow. You should completely understand our thinking in this regard which has been emphasized in previous letters.

generals ↓ but workouts + controls ↑

During the first half, we had an average net investment in "generals" (lo positions in generals minus short positions in generals) of approximately $5,275,000. Our overall gain from this net investment in generals (for a description of our investment categories see the last annual letter) was about $1,100,000 for a percentage gain from this category of roughly 21% This again illustrates the extent to which the allocation of our resources among various categories affects short-term results. In 1962 the genera were down for the year and only an outstanding performance by both of th other two categories, "work-outs" and "controls," gave us our unusually favorable results for that year.

can't predict the future + can't swiftly shift allocations from work-outs to generals

Now this year, our work-outs have done poorer than the Dow and have been a drag on performance, as they are expected to be in rising markets. Whi it would be very nice to be 100% in generals in advancing markets and 100% in work-outs in declining markets, I make no attempt to guess the course of the stock market in such a manner. We consider all three of our categories to be good businesses on a long-term basis, although their short-term price behavior characteristics differ substantially in various types of markets. We consider attempting to gauge stock market fluctuations to be a very poor business on a long-term basis and are not going to be in it, either directly or indirectly through the process of trying to guess which of our categories is likely to do best in the near future.

Investment Companies

Shown below are the usual statistics on a cumulative basis for the Dow anc Buffett Partnership, Ltd. (including predecessor partnerships) as well as for the two largest open-end (mutual funds) and two largest closed-end inv ment companies following a diversified common-stock investment policy:

Year	Dow	Mass. Inv. Trust (1)	Investors Stock (1)	Tri-Cont. (2)
1957	- 8.4%	-11.4%	-12.4%	- 2.4%
1957-8	+26.9	+26.4	+29.2	+30.0
1957-9	+52.3	+37.8	+42.5	+40.9
1957-60	+42.9	+36.4	+41.6	+44.8
1957-61	+74.9	+71.3	+76.9	+77.4
1957-62	+61.6	+54.5	+53.2	+59.7
1957-6/30/63	+77.8	+72.4	+69.3	+75.7
Annual Compounded Rate	9.3	8.7	8.4	9.1

Year	Lehman (2)	Partnership (3)	Limited Partners (4)
1957	- 11.4%	+ 10.4%	+ 9.3%
1957-8	+ 24.7	+ 55.6	+ 44.5
1957-9	+ 34.8	+ 95.9	+ 74.7
1957-60	+ 38.2	+140.6	+107.2
1957-61	+ 70.8	+251.0	+181.6
1957-62	+ 46.2	+299.8	+215.1
1957-6/30/63	+ 60.8	+355.8	+252.9
Annual Compounded Rate	7.6	26.3	21.4

Please see next page for footnotes.

Footnotes:

(1) Computed from changes in asset value plus any distributions to holders of record during year.

(2) From 1963 Moody's Bank & Finance Manual for 1957-62. Estimated for first half 1963.

(3) For 1957-61 consists of combined results of all predecessor limited partnerships operating throughout entire year after all expenses but before distributions to partners or allocations to the general partner.

(4) For 1957-61 computed on basis of preceding column of partnership results allowing for allocation to general partner based upon present partnership agreement.

high paid fund managers don't outperform the unmanaged dow

The results continue to show that the most highly paid and respected investment advice has difficulty matching the performance of an unmanaged index of blue-chip stocks. This in no sense condemns these institutions or the investment advisers and trust departments whose methods, reasoning, and results largely parallel such investment companies. These media perform a substantial service to millions of investors in achieving adequate diversification, providing convenience and peace of mind, avoiding issues of inferi quality, etc. However, their services do not include (and in the great majc ity of cases, are not represented to include) the compounding of money at a rate greater than that achieved by the general market.

this should be the goal

Our partnership's fundamental reason for existence is to compound funds at a better-than-average rate with less exposure to long-term loss of capit than the above investment media. We certainly cannot represent that we will achieve this goal. We can and do say that if we don't achieve this goal over any reasonable period, excluding an extensive speculative boom, we will cease operation.

1 compound funds
2 at better than avg rate
3 less risk of permanent loss of capital

Dempster Mill Manufacturing Company

In our most recent annual letter, I described Harry Bottle as the "man of the year." This was an understatement.

Last year Harry did an extraordinary job of converting unproductive asset into cash which we then, of course, began to invest in undervalued securities. Harry has continued this year to turn under-utilized assets into cas but in addition, he has made the remaining needed assets productive. Thi we have had the following transformation in balance sheets during the last nineteen months:

November 30, 1961 (000's omitted)

Assets	Book Figure	Valued @	Adjusted Valuation	Liabilities	
Cash	$ 166	100%	$ 166	Notes payable	$1,2
Accts. rec. (net)	1,040	85	884		
Inventory	4,203	60	2,522	Other liabilities	1,C
Ppd. exp. etc.	82	25	21		
Current assets	5,491		3,593	Total liabilities	2,:
Cash value life ins., etc.	45	100	45	Net worth:	
				Per books	4,(
Net plant & equipment	1,383	Est. net auction value	800	As adjusted to quickly realizable values	2,
				Shares outstanding 60,146	
Total assets	$6,919		$4,438	Adj. value per share	$35

realistically could get at auction

November 30, 1962 (000's omitted)

Assets	Book Figure	Valued @	Adjusted Valuation	Liabilities	
Cash	$ 60	100%	$ 60	Notes payable	$
Marketable securities	758	Mkt. 12/31/62	834	Other liabilities	
Accts. rec. (net)	796	85%	676		
Inventory	1,634	60	981	Total liabilities	
Cash value life ins.	41	100	41	Net worth:	
Recoverable income tax	170	100	170	Per books	4
Ppd. exp. etc.	14	25	4	As adjusted to quickly realizable values	3
Current assets	3,473		2,766	Add: proceeds from potential exercise of option to Harry Bottle	
Misc. invest.	5	100	5		
				Shares outstanding 60,146	
Net plant & equipment	945	Est. net auction value	700	Add: shs. potentially outstanding under option	2,000
				Total	62,146
Total assets	$4,423		$3,471	Adj. value per share	$

June 30, 1963 (000's omitted)

Assets	Book Figure	Valued @	Adjusted Valuation	Liabilities	
Cash	$ 144	100%	$ 144	Notes payable (paid 7/3/63)	$ 12
Marketable securities	1,772	Mkt. 6/30/63	2,029	Other liabilities	39
Accts. rec. (net)	1,262	85%	1,073		
Inventory	977	60%	586	Total liabilities	51
Ppd. exp. etc.	12	25%	3		
				Net worth:	
Current assets	4,167		3,835	Per books	4,5
Misc. invest.	62	100%	62	As adjusted to quickly realizable values	4,0
Net plant & equip.	872	Est. Net auction value	650	Shares outstanding 62,146	
Total assets	$5,101	Nice!	$4,547	Adj. value per share	$64.

I have included above the conversion factors we have previously used in valuing Dempster for B.P.L. purposes to reflect estimated immediate sale values of non-earning assets.

As can be seen, Harry has converted the assets at a much more favorable basis than was implied by my valuations. This largely reflects Harry's expertise and, perhaps, to a minor degree my own conservatism in valuation

↑ roI

As can also be seen, Dempster earned a very satisfactory operating profit in the first half (as well as a substantial unrealized gain in securities) and there is little question that the operating business, as now conducted, has at least moderate earning power on the vastly reduced assets needed to conduct it. Because of a very important seasonal factor and also the presenc of a tax carryforward, however, the earning power is not nearly what migh be inferred simply by a comparison of the 11/30/62 and 6/30/63 balance sheets. Partly because of this seasonality, but more importantly, becaus of possible developments in Dempster before 1963 yearend, we have left our Dempster holdings at the same $51.26 valuation used at yearend 1962 in our figures for B.P.L's first half. However, I would be very surprise if it does not work out higher than this figure at yearend.

Bought $1,454,373 of securities PLUS the business for $1,262,577!

One sidelight for the fundamentalists in our group. B.P.L. owns 71.7% o Dempster acquired at a cost of $1,262,577.27. On June 30, 1963 Dempst had a small safe deposit box at the Omaha National Bank containing securi worth $2,028,415.25. Our 71.7% share of $2,028,415.25 amounts to $1,454,373.70. Thus, everything above ground (and part of it undergroun is profit. My security analyst friends may find this a rather primitive method of accounting, but I must confess that I find a bit more substance in this fingers and toes method than in any prayerful reliance that someon will pay me 35 times next year's earnings.

winning

Lots of profits to be had

no need to do an earnings multiplier

Advance Payments and Advance Withdrawals

We accept advance payments from partners and prospective partners at 6% interest from date of receipt until the end of the year. While there is no obligation to convert the payment to a partnership interest at the end of the year, this should be the intent at the time of payment.

Similarly, we allow partners to withdraw up to 20% of their partnership account prior to yearend and charge them 6% from date of withdrawal until yearend when it is charged against their capital account. Again, it is not intended that partners use us like a bank, but that they use the withdrawal right for unanticipated need for funds.

The willingness to both borrow and lend at 6% may seem "un-Buffett-like." We look at the withdrawal right as a means of giving some liquidity for unexpected needs and, as a practical matter, are reasonably sure it will be far more than covered by advance payments.

Why then the willingness to pay 6% for advance payment money when we can borrow from commercial banks at substantially lower rates? For example, in the first half we obtained a substantial six-month bank loan at 4%. The answer is that we expect on a long-term basis to earn better than 6% (the general partner's allocation is zero unless we do) although it is largely a matter of chance whether we achieve the 6% figure in any short period. Moreover, I can adopt a different attitude in the investment of money that can be expected to soon be a part of our equity capital than I can on short-term borrowed money. The advance payments have the added advantage to us of spreading the investment of new money over the year, rather than having it hit us all at once in January. On the other hand, 6% is more than can be obtained in short-term dollar secure investments by our partners, so I consider it mutually profitable. On June 30, 1963, we had advance withdrawals of $21,832.00 and advance payments of $562,437.11.

Taxes

There is some possibility that we may have fairly substantial realized gains this year. Of course, this may not materialize at all and actually does not have anything to do with our investment performance this year. I am an outspoken advocate of paying large amounts of income taxes -- at low rates. A tremendous number of fuzzy, confused investment decisions are rationalized through so-called "tax considerations."

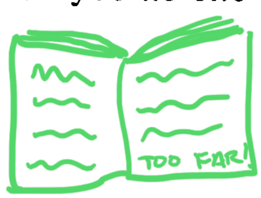
My net worth is the market value of holdings less the tax payable upon sale. The liability is just as real as the asset unless the value of the asset declines (ouch), the asset is given away (no comment), or I die with it. The latter course of action would appear to at least border on a Pyrrhic victory.

Investment decisions should be made on the basis of the most probable compounding of after-tax net worth with minimum risk. Any isolation of low-basis securities merely freezes a portion of net worth at a compounding factor identical with the assets isolated. While this may work out either well or badly in individual cases, it is a nullification of investment management. The group experience holding various low basis securities will undoubtedly approximate group experience on securities as a whole, namely compounding at the compounding rate of the Dow. We do not consider this the optimum in after-tax compounding rates.

I have said before that if earnings from the partnership can potentially amount to a sizable portion of your total taxable income, the safe thing to do is to estimate this year the same tax you incurred last year. If you do this, you cannot run into penalties. In any event, tax liabilities for those who entered the partnership on 1/1/63 will be minimal because of the terms of our partnership agreement first allocating capital gains to those having an interest in unrealized appreciation.

As in past years, we will have a letter out about November 1st (to partners and those who have indicated an interest to me by that time in becoming partners) with the amendment to the partnership agreement, commitment letter for 1964, estimate of the 1963 tax situation, etc.

My closing plea for questions regarding anything not clear always draws a blank. Maybe no one reads this far. Anyway, the offer is still open.



Cordially,

Warren E. Buffett

Jamie Retherford

WEB:bf