BUFFETT PARTNERSHIP, LTD.
810 KIEWIT PLAZA
OMAHA, NEBRASKA 68101
TELEPHONE 042-4110

WARREN E. BUFFETT, GENERAL PARTNER
WILLIAM SCOTT
JOHN M. HARDING

July 12, 1966

First Half Performance

During the first half of 1966, the Dow-Jones Industrial Average (hereinafter called the "Dow") declined from 969.26 to 870.10. If one had owned the Dow during this period, dividends of approximately 14.70 would have been received, reducing the overall loss of the Dow to about 8.7%.

It is my objective and my hope (but not my prediction!) that we achieve over a long period of time, an average yearly advantage of ten percentage points relative to the Dow. During the first half we did considerably better than expected with an overall gain of approximately 8.2%. Such results should be regarded as decidedly abnormal. I have previously complimented partners on the good-natured tolerance they display in shrugging off such unexpected positive variances. The nature of our business is such that, over the years, we will not disappoint the many of you who must also desire a test of your capacity for tolerance of negative variances.

The following summarizes the year-by-year performance of the Dow, the performance of the Partnership before allocation to the general partner, and the results for limited partners:

Year	Overall Results From Dow (1)	Partnership Results (2)	Limited Partners' Results (3)
1957	- 8.4%	+10.4%	+ 9.3%
1958	+38.5	+40.9	+32.2
1959	+20.0	+25.9	+20.9
1960	- 6.2	+22.8	+18.6
1961	+22.4	+45.9	+35.9
1962	- 7.6	+13.9	+11.9
1963	+20.6	+38.7	+30.5
1964	+18.7	+27.8	+22.3
1965	+14.2	+47.2	+36.9
First half 1966	- 8.7	+ 8.2	+ 7.7
Cumulative results	+141.1	+1028.7	+641.5
Annual compounded rate	9.7	29.0	23.5

(1) Based on yearly changes in the value of the Dow plus dividends that would have been received through ownership of the Dow during that year. The table includes all complete years of partnership activity.

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

(3) For 1957-61 computed on the basis of the preceding column of partnership results allowing for allocation to the general partner based upon the present partnership agreement, but before monthly withdrawals by limited partners.

Even Samson gets clipped occasionally. If you had invested $100,000 on January 1 equally among -

a. the world's largest auto company (General Motors);
b. the world's largest oil company (Standard of New Jersey);
c. the world's largest retailing company (Sears Roebuck);
d. the world's largest chemical company (duPont);
e. the world's largest steel company (U. S. Steel);
f. the world's largest stockholder-owned insurance company (Aetna);
g. the world's largest public utility (American Telephone & Telegraph);
h. the world's largest bank (Bank of America);

your total portfolio (including dividends received) would have been worth $83,370 on June 30 for a loss of 16.6%. The total market value on January 1 of these eight giants was well over $100 billion. Every one of them was selling lower on June 30.

<u>Investment Companies</u>

On the next page we bring up to date our regular comparison with the results of the two largest open-end investment companies (mutual funds) that follow a policy of being, typically, 95-100% invested in common stocks, and the two largest diversified closed-end investment companies.

Year	Mass Inv. Trust (1)	Investors Stock (1)	Lehman (2)	Tri-Cont. (2)	Dow	Limited Partners
1957	-11.4%	-12.4%	-11.4%	- 2.4%	- 8.4%	+ 9.3%
1958	+42.7	+47.5	+40.8	+33.2	+38.5	+32.2
1959	+ 9.0	+10.3	+ 8.1	+ 8.4	+20.0	+20.9
1960	- 1.0	- 0.6	+ 2.5	+ 2.8	- 6.2	+18.6
1961	+25.6	+24.9	+23.6	+22.5	+22.4	+35.9
1962	- 9.8	-13.4	-14.4	-10.0	- 7.6	+11.9
1963	+20.0	+16.5	+23.7	+18.7	+20.6	+30.5
1964	+15.9	+14.3	+14.0	+13.6	+18.7	+22.3
1965	+10.2	+ 9.8	+19.0	+11.1	+14.2	+36.9
First half 1966	- 7.9	- 7.9	- 1.0	- 5.2	- 8.7	+ 7.7
Cumulative results	+118.1	+106.3	+142.8	+126.9	+141.1	+641.5
Annual compounded rate	8.6	7.9	9.8	9.0	9.7	23.5

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

(2) From 1966 Moody's Bank & Finance Manual for 1957-1965. Estimated for first half of 1966.

Proponents of institutional investing frequently cite its conservative nature. If "conservative" is interpreted to mean "productive of results varying only slightly from average experience" I believe the characterization is proper. Such results are almost bound to flow from wide diversification among high grade securities. Since, over a long period, "average experience" is likely to be good experience, there is nothing wrong with the typical investor utilizing this form of investment medium.

However, I believe that conservatism is more properly interpreted to mean "subject to substantially less temporary or permanent shrinkage in value than total experience". This simply has not been achieved, as the record of the four largest funds (presently managing over $5 billion) illustrates. Specifically, the Dow declined in 1957, 1960, 1962 and the first half of 1966. Cumulating the shrinkage in the Dow during the three full year periods produces a decline of 20.6%. Following a similar technique for the four largest funds produces declines of 9.7%, 20.9%, 22.3% and 24.6%. Including the interim performance for the first half of 1966 results in a decline in the Dow of 27.5% and for the funds declines of 14.4%, 23.1%, 27.1% and 30.6%. Such funds (and I believe their results are quite typical of institutional experience in common stocks) seem to meet the first definition of conservatism but not the second one.

Most investors would climb a rung intellectually if they clearly delineated between the above two interpretations of conservatism. The first might be better labeled "conventionalism" - what it really says is that "when others are making money in the general run of securities, so will we and to about the same degree; when they are losing money, we'll do it at about the same rate." This is not to be equated with "when others are making it, we'll make as much and when they are losing it, we will lose less." Very few investment programs accomplish the latter - we certainly don't promise it but we do intend to keep trying. (I have always felt our objectives should be somewhat loftier than those Herman Hickman articulated during the despera[illegible] years when Yale was losing eight games a season. Said Herman, "I see my job as one of keeping the alumni sullen but not mutinous.")

Hochschild, Kohn & Co.

During the first half we, and two 10% partners, purchased all of the stock o[illegible] Hochschild, Kohn & Co., a privately owned Baltimore department store. This is the first time in the history of the Partnership that an entire busines[illegible] has been purchased by negotiation, although we have, from time to time, negotiated purchase of specific important blocks of marketable securities. However, no new principles are involved. The quantitative and qualitative aspects of the business are evaluated and weighed against price, both on an absolute basis and relative to other investment opportunities. HK (learn to call it that - I didn't find out how to pronounce it until the deal was conclude[illegible] stacks up fine in all respects.

We have topnotch people (both from a personal and business standpoint) han[illegible] the operation. Despite the edge that my extensive 75¢ an hour experience a[illegible] the Penney's store in Omaha some years back gives us (I became an authori[illegible] on the Minimum Wage Act), they will continue to run the business as in the past. Even if the price had been cheaper but the management had been run-of-the-mill, we would not have bought the business.

It is impossible to avoid some public notice when a business with several thousand employees is acquired. However, it is important that you do not infer the degree of financial importance to BPL from its news value to the public. We have something over $50 million invested, primarily in marketable securities, of which only about 10% is represented by our net investme[illegible] in HK. We have an investment of over three times this much in a marketab[illegible] security where our ownership will never come to public attention. This is not to say an HK is not important - a 10% holding definitely is. However, i[illegible] is not as significant relative to our total operation as it would be easy to think. I still prefer the iceberg approach toward investment disclosure.

It is my intention to value HK at yearend at cost plus our share of retained earnings since purchase. This policy will be followed in future years unless there is a demonstrable change in our position relative to other department stores or in other objective standards of value. Naturally we wouldn't have purchased HK unless we felt the price was quite attractive. Therefore, a valuation policy based upon cost may somewhat undervalue our holdings. Nevertheless, it seems the most objective figure to apply. All of our investments usually appear undervalued to me - otherwise we wouldn't own them.

Market Forecasting

Ground Rule No. 6 (from our November packet) says: "I am not in the business of predicting general stock market or business fluctuations. If you think I can do this, or think it is essential to an investment program, you should not be in the partnership."

Of course, this rule can be attacked as fuzzy, complex, ambiguous, vague, etc. Nevertheless, I think the point is well understood by the great majority of our partners. We don't buy and sell stocks based upon what other people think the stock market is going to do (I never have an opinion) but rather upon what we think the company is going to do. The course of the stock market will determine, to a great degree, when we will be right, but the accuracy of our analysis of the company will largely determine whether we will be right. In other words, we tend to concentrate on what should happen, not when it should happen.

In our department store business I can say with considerable assurance that December will be better than July. (Notice how sophisticated I have already become about retailing.) What really counts is whether December is better than last December by a margin greater than our competitors' and what we are doing to set the stage for future Decembers. However, in our partnership business I not only can't say whether December will be better than July, but I can't even say that December won't produce a very large loss. It sometimes does. Our investments are simply not aware that it takes 365-1/4 days for the earth to make it around the sun. Even worse, they are not aware that your celestial orientation (and that of the IRS) requires that I report to you upon the conclusion of each orbit (the earth's - not ours). Therefore, we have to use a standard other than the calendar to measure our progress. This yardstick is obviously the general experience in securities as measured by the Dow. We have a strong feeling that this competitor will do quite decently over a period of years (Christmas will come even if it's in July) and if we keep beating our competitor we will have to do something better than "quite decently". It's something like a retailer measuring his sales gains and profit margins against Sears' - beat them every year and somehow you'll see daylight.

I resurrect this "market-guessing" section only because after the Dow declined from 995 at the peak in February to about 865 in May, I received a few calls from partners suggesting that they thought stocks were going a lot lower. This always raises two questions in my mind: (1) if they knew in February that the Dow was going to 865 in May, why didn't they let me in on it then; and, (2) if they didn't know what was going to happen during the ensuing three months back in February, how do they know in May? There is also a voice or two after any hundred point or so decline suggesting we sell and wait until the future is clearer. Let me again suggest two points: (1) the future has never been clear to me (give us a call when the next few months are obvious to you - or, for that matter, the next few hours); and, (2) no one ever seems to call after the market has gone up one hundred points to focus my attention on how unclear everything is, even though the view back in February doesn't look so clear in retrospect.

If we start deciding, based on guesses or emotions, whether we will or won't participate in a business where we should have some long run edge, we're in trouble. We will not sell our interets in businesses (stocks) when they are attractively priced just because some astrologer thinks the quotations may go lower even though such forecasts are obviously going to be right some of the time. Similarly, we will not buy fully priced securities because "experts" think prices are going higher. Who would think of buying or selling a private business because of someone's guess on the stock market? The availability of a quotation for your business interest (stock) should always be an asset to be utilized if desired. If it gets silly enough in either direction, you take advantage of it. Its availability should never be turned into a liability whereby its periodic aberrations in turn formulate your judgments. A marvelous articulation of this idea is contained in chapter two (The Investor and Stock Market Fluctuations) of Benjamin Graham's "The Intelligent Investor". In my opinion, this chapter has more investment importance than anything else that has been written.

We will have a letter out about November 1 with the Commitment Letter for 1967 and an estimate of the 1966 tax situation.

Cordially,

Warren E. Buffett

WEB eh