Berkshire
DIVIDEND STRATEGY

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"Casual Friday" Commentary

Casual Friday: Supply Chain Issues + Future of Wholesaling? *– Oct 15th, 2021*

Recent analyst question we fielded:
"Please share thoughts how supply chain issues may be impacting the portfolio."

Response: Berkshire company holdings, in general, have not seen material impact from supply disruptions so far and appear to be in very good shape overall. We believe the majority of businesses we own are mitigating these issues and will effectively pass cost on to the consumer without hampering demand. Our mega cap / quality bias has alleviated material risks arising in aggregate but there are company specific issues worth noting and monitoring.

Big Picture: Company variables for consideration on these issues? [ii]

- Financial strength and flexibility
  - Power of supply chain / diversity / financial strength to adapt
  - Our mega cap / quality focus helps here
- Ability to pass on higher costs (margins)
  - Strong brands, patents and intellectual capital, high switching costs let you raise prices
- Asset utilization (turns)
  - How many sales can a $1 in assets generate? Inventory disruptions lower sales near term and usually lower this ratio
- Are the disruptions / inflated prices short term or permanent?
- Does it REALLY materially affect long run earnings power?
- Is the impact already priced in to the stocks?
- Can the disruptions create opportunity?
  - I.e., Need for capital expenditures – Who benefits?
  - Temporary problem creates buying opportunity?

We've been researching our portfolio, monitoring closely for material impact:

- Financials/Banks: 20% - Very limited effect -- 100% service business. Exception? If loan clients can't repay because of business interruption. Risks of this being widespread is low. Banks are well reserved.

- Consumer Staples: 10% - Likely to pass on higher input costs. We have strong brands. Examples - Pepsi will raise prices to offset higher sugar prices. At some point generic subs may kick in but brands mitigate this affect. Walmart sees minor disruptions but took steps to hire its own vessels to help mitigate. This space offers plenty of financial flexibility, we believe pricing power and earnings remain solid.

- Pharma: 18% - The pandemic has raised the question of the US pharma supply chain. Currently 80% of active pharmaceutical ingredients (API's) are sourced from China and India. While there have been some drug shortages, we have not heard material earnings announcements or changes in guidance as a result. The speed at which big pharma brought Covid related products to market is a testimony to supply chain and nimbleness.

- Industrials: 15% - Lockheed Martin has already announced they will deliver fewer F-35s than originally agreed to the Pentagon in 2022. This doesn't appear to be a material impact overall and the stock price has already been adjusted to incorporate this change. Other industrial companies we own have limited impact from supply chain issues, and those considered "best in class", such as Honeywell, should have a significant advantage. This may also be a net positive for companies like Norfolk Southern and Waste Management – need for improved domestic infrastructure. Leggett and Platt cited multiple supply chain problems amidst huge demand. They still raised the dividend and increased guidance for 2021.

- Tech: 17% - There appears to be the most exposure in our portfolio in the tech space (capital expenditures, delays, pressured margins possible). Although the most exposure, our companies have been navigating well thus far -- Global semiconductor chip shortage & scarcity is likely to last "a couple of years", according to Intel's CEO Pat Geisinger. In response, Intel is ramping up manufacturing capacity, investing $20bn to build 2 new factories in Arizona and lessen reliance on international demand. Apple research analysts expect, despite already high profit margins, Apple will pass any cost increase onto the consumer, pushing prices of new iPhones to potentially their highest level ever. Qualcomm has been strong financially, despite the supply strains, with fiscal third quarter revenue beating both analyst expectations and the company's own guidance. Cisco is experiencing high demand and said they would have raised near term revenue guidance if there were no supply chain issues.

We're seeing relatively modest effect on company fundamentals in the short term. Supply chain issues are unlikely to produce changes in the portfolio. We currently don't believe there are companies in the portfolio where we would say "wow this is going to be such a problem we need to sell". (Source: Bloomberg)

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Berkshire State of the Union 9.30.2021 includes the following:

- Firm Overview
- Strategy Objectives / Profile
- Strategy Process Edge
- Expectations for Equity Investors
- Case for Growing Dividends Going Forward?
- Investment results
- Current Special Interests / Research

Future of Wholesaling?

Covid ***forced*** asset managers to connect with advisors via zoom, email, webinars. Some version of the virtual wholesaling model has always been a Berkshire strong suit vs. the traditional in person branch visits. Manager access, practice management and education have always been our focus vs. the "same old product pitch". We feel Casual Friday in itself is a great example of this commitment. Successful Zoom's added how we can deliver ideas to you.

Feedback wanted:

- Do you think the virtual wholesaling will stick or will the traditional in person branch visits return?
- What content do you think will be most valuable in the future? (Continuing ed, client acquisition strategies, market commentary etc).
- What are your priorities?

https://www.fa-mag.com/news/the-future-of-financial-wholesalers-61643.html

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