Mr. Warren Buffet

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[Omaha] Warren Buffett [WB] while drinking a cherry coke – "drink more coke, with 8 percent ownership, after every 12 servings the profit goes to us."

Q. (Morningstar) With your large cash holdings did you have any in troubled money market funds?

A. We always have cash or near cash as we may need to deploy $ billions very quickly. That means treasuries, government agencies and money market funds that only invest in those two. Berkshire is totally conservative and that way we not only avoided the chaos of last fall but we profited from it.

Q. (Financial Times) Many have suggested that the next CEO will come from Mr. Jain, Mr. Sokol or Mr. Nicely (all current Berkshire CEO's). Could you list the strengths of each?

A. No way to back into a name (laughter). Those managers are all highly qualified but we also have many other great managers like Brad Knistler of Sees Candies and Cathy Tamraz of Business Wire. They did not join Berkshire in order to be chief CEO. Charlie Munger [CM]- we have some awesome talent capable of playing on a higher scale and they are all perfectly happy doing their current job.

Q. (Market Watch) What do you think about the bank stress tests? Will banks that Berkshire is invested in (Wells Fargo, U.S. Bank, SunTrust, M&T, Bank of America) be required to convert preferred shares into common?

A. These banks don't need capital although I haven't recently looked at SunTrust so can't comment there. Lou Simpson owns bank of America in the GEICO portfolio. The stress test ratios do not show the whole picture. For example, Wells Fargo's own originated home loans have way lower delinquencies than the brokered home loans by a factor of four. Yet the government doesn't differentiate, as they are both lumped under home equity. Each of the banks has a different business model and it’s unsophisticated to try and stress test them in the way the government is doing it. We would buy stocks in the three banks (Wells Fargo, U.S. Bancorp & M&T) at today's prices but there is no one you can call up to takeover Citi (Citigroup: NYSE: C). There is a public misconception on banks. Since 1934 FDIC has assisted in 3600 bank failures and not one penny has been lost by depositors. This has been achieved at no cost to the taxpayer. Shareholders and bondholders may lose money. In 2008 a full 8% of all deposits were moved from one institution to another without the loss of a penny. Munger - government stress tests will be quite different from the ones Berkshire would have made.

Q. (Independent UK) Have you followed Apple (Nasdaq: AAPL) CEO Steve Jobs health disclosures and would Berkshire give a full disclosure in the event that you had health problems?

A. Berkshire would always disclose if I knew that I had any serious health problems. I'm due for a cataract operation and that wouldn't be announced. Munger (who is 7 years older) - I'm here to give hope that shareholders will get at least another 7 years out of Warren!

Q. (Reuters) What level of disclosure is appropriate for the bank stress tests - from the government or from the banks?

A. Any form of disclosure is likely to confuse people. You can over disclose and obfuscate. If you don’t understand 10Ks you shouldn’t invest. When we bought Gen Re they had 23,000 derivative contracts and I couldn’t understand them so we sold them. Munger - I can see why (politically) the government did it this way with banks "too big to fail" but the old way of sorting it out (behind closed doors) might have been better. Buffett - only the top four of the 19 banks are too big to fail. Deals could be made for the other 15 without taxpayer's money just as Wells Fargo was delighted to get Wachovia's deposits and distribution. Good deals can be made for failing institutions. On the other hand there are some banks (Citi) I would not even attempt to understand. Munger - the one size fits all stress test won't work.

Q. (Smart Money) Your evolution from nerdy capital allocator to media star seems to have an inverse correlation to the Berkshire share price, can you comment?

A. That's what we call a false correlation. Both are caused by size and asset size is an anchor on performance. As we get bigger there is more media interest and being larger makes it harder to grow at previous rates.

Q. (NIKKEI - Japan) What needs to be done by CEO Jeffrey Immelt at GE to get their ailing business back to being great?

A. The problem is not Immelt he is a first class manager. GE manufacturing business is not the problem, GE finance division is. He has done very well with the hand he was dealt, in particular in the credit business which had a $500 billion portfolio and the under funded pension obligations. The operating businesses have been successful given the economy. GE stock price does not reflect the CEO’s performance.

Q. (Korea) What is your opinion on investment in Korea?

A. Korea is 3rd largest economy in Asia. We own Posco Steel (we added more in the last 2 months) and think it’s the finest steel company in the world. Both Warren and Charlie admirer Korea. Bought Posco bonds. We are not buying individual equities and are focusing on acquisitions. Not specifically in Korea but at the right price we would be happy to do a deal in Korea. Warren personally owns 1 Korean stock. Charlie personally owns stocks in 3 countries including Korea.

Q. (Germany) How do you reconcile your statement on derivatives as being "weapons of financial mass destruction" and Berkshire's own derivative holdings.

A. There are three factors to measure and price risk whether it be an insurance policy or derivative contract or options; 1.) do you understand the risk, 2.) do you get a premium or rate greater than the probability of loss, and 3.) make sure you do not take on too much aggregated loss events. The way our derivative contracts are set up is fundamentally the same business as insurance. We assess the risk and if we feel that we are being adequately compensated we will write the contract, whether it is insurance or a derivative. Where people have a hard time is understanding why the accounting for derivatives is completely different causing wide volatility in financial statements but not in cash transactions. If they are mis-priced and good for Berkshire shareholders they’ll continue to write the business. We never have too much exposure and are careful to avoid correlation with other risks we have underwritten. Even though we have taken advantage of the ability to write derivative contracts we would vote against their use if asked because of their general misuse.

Q. (Japan) The US has taken in a lot of foreign cash to balance its trade deficit, will it continue, is it sustainable & what will be the effect. (Note Warren & Charlie disagreed here)

A. It will be a problem over time, as the US will deflate the dollar as that makes it easier to pay back. That will put a lot of tension in relations with our debtors, particularly China, as when you deflate an obligation others get angry and that leads to conflict. Some countries behave badly by inflating their currencies. Munger - even with deflated dollar holdings this is a great deal for China and it is likely to continue because it increases China's manufacturing muscle and economic position as others become dependent on China. China is taking on currency risk in exchange for developing its manufacturing base. It is likely to continue because it is working for China.

Q. (Grants Interest Rate Observer) Do you have any examples of unusual insurance risks like natural disasters, hurricanes and earthquakes written by Berkshire and how does Ajit Jain (CEO of Berkshire Reinsurance and star underwriter) figure out the proper premium?

A. We start with historical data and then figure out what else could go wrong. For example historical hurricane data has relevance but we also assess how climate change might affect it. We are pessimistic. We have insured against a pandemic and would insure against a swine flu pandemic if someone asked us but I don't think they'd like our price! We've insured Alex Rodriguez the highest paid baseball player with a $250 million work disability policy, heavy weight boxer Mike Tyson against dying within 2 years when he was in his mid-twenties and a Pepsico (NYSE: PEP) competition that had a $1 billion payout. Munger - Ajit has a considerable knack for it and we could not put anyone in Ajit's place. We’re not giving our fountain pen to some else. Buffett - If Ajit's on holiday we don't write the policy. If we don't know that we have an edge we won't write. If you give us 2 to 1 odds on a coin flip, we would risk $1 billion with those odds.

Q. (AP) What is the most important lesson from the financial and economic crisis?

A. The world needs a lot less leverage and proper incentives and disincentives. Human nature is to be paid disproportionately. Executive incentives need to be properly aligned as they encourage the use of leverage. However this is unlikely because who wants to be appropriately paid? Executives should have a disincentive to use leverage. Intense regulation does not work - just look at Fannie and Freddie they had a government oversight body whose sole job was to ensure the safety of just two companies. Munger – What we had was what I call a Lollapalooza event – a convergence of leverage and immorality combined with consumer credit being offered to the less advantaged. There was a gross immorality in sucking in those who could not afford credit and in the trading of derivative contracts. There was too much stupidity at universities, governments, and government regulators preaching free market economics - free markets in restaurants are fine but not in the financial industry. It is wrong for the accounting industry to allow an artificial spike in earnings just before bankruptcy. The accounting profession has failed us in looking for consistency, which has lead to creation of the wrong incentives - insane!

Q. (Motley Fool - Robert Brokamp) We asked our readers for input on what question we should ask, and one common thread was regulation. We all understand that capitalism relies on healthy self-interest, but many feel that that has given way to too much greed on Wall Street, at the investor's expense. You have already talked about how regulation didn't work at Fannie and Freddie. But do you believe there should be any new regulations? If so, where would you start? With counterproductive financial incentives? Or something like credit default swaps and other complex financial instruments?

A. Warren Buffett: Compensation and management incentives are the most important things to change right now, but regulating them is difficult. Our local construction company Peter Kiewit Sons' has some of the best we've ever seen. You can create good compensation:

• First, get rid of compensation consultants who simply reinforce what everyone else is doing.

• Second, have directors behave like owners. Too many are in it for the compensation and social cache, and their compensation fosters cronyism. Half or more of corporate directors don't understand business. Money is important to most directors. Incentives probably won't be realigned, because any director suggesting it would get kicked off the board and would find he was off other boards too.

• Third, get rid of compensation committees and have the entire board draw up compensation. But it’s going to be very tough to get anything through the U.S. Congress.

Charlie Munger: Even after this mess, it’ll be tough to get anything passed. Financial companies spent $500 million over the past decade in lobbying and financial contributions. Wall Street had a strong interest in getting derivatives approved, but no one paid attention to them. This is a very serious problem. You know, this never would have happened in a place like Singapore, is the best example of how an organization should be run, with a benevolent despot.

Warren Buffett: You mentioned greed. There hasn’t been more greed in the last 10 years; there’s just been more opportunity. When people get a chance to be greedy, they’ll take it. When you see someone get paid $25 million for failure, and the board and compensation committee will always approve it, who wouldn’t take a golden parachute? Even as the largest shareholder in some companies, we have been unable to change incentives. When an executive only has upside and no downside, it will always lead to excessive risk-taking.

Q. (Montreal) It seems many franchises are having their moats filled with sand, do you see the opposite, with a deeper moat filled with alligators and sharks?

A. Google has a huge new moat filled with sharks, alligators and piranhas. Google’s keywords generate huge money all electronically with little to no human effort. Some companies pay as much as $70 per click to be the first up in a search for certain key words. Geico (Berkshire car insurance company) pays $10 per click to be on the top when you search for auto insurance - so please don't click just go to geico.com you'll save us $10! It doesn't matter how much money you throw at it you can't take the business away from Google. Generally moats are really hard to build and by definition there can't be many of them. A good example is Sees Candies. If I gave you $500 million to take away the California retail chocolate market share, you couldn’t do it. That’s how to recognize and define a moat. Moats ebb and flow. For example, trucking used to have a moat and it is now shifting back to railroads as the cost of fuel rises.

Q. (Guardian UK) You said that when the financial tide went out we'd see who had been swimming naked. With the large drop in Berkshire's book value it seems you might have been swimming naked!

A. WB Well on a relative and compounded basis to the S&P 500 index we were 27.4% better this year so I wouldn't say we were swimming naked. We were better than most but not immune and we would not consider 2008 our worst year; we made $20 billion in new investments that will pay off down the road. You can't judge just by share price - it looks like suffering now but we get opportunities out of this that won't show immediately in financial results. Three times before in our history our stock has dropped by 50% or more, 1974, 1987 and 2000 but in each of those cases the underlying or intrinsic value of Berkshire didn't change that much. We are probably the best insurer in the world and have the best utility company and many other great companies with earnings power. If you are running your business right these are the times that you lay the foundations for future success. GEICO signed 13,000 more policyholders in the first 2 days of May. 68 new policyholders signed up at Saturday's annual meeting, which will pay for the total cost of the shareholder's weekend. CM = Tough periods allow the strong and capable to strengthen. Over time the stock price will gain if you build business value. Carnegie Steel built its business during bad times. Opportunities happen with trouble.

Q. (National Public Radio) Will making the bank stress tests public cause a run on the banks?

A. No as no depositor in US banks will lose money as the U.S. government and the FDIC has quite rightly demonstrated that it will take whatever measures are necessary to avoid it. The current unease is in the stock market not among depositors.

Q. (Omaha World Herald) We are told that another wave of ARM (adjustable rate mortgage) resets is about to hit us. Can we fend it off?

A. It's a payment reset rather than an interest rate reset because mortgages have paid less than the original amortization indicated. I think the drop in interest rates will ease the problem that we had with interest rate resets. The government's low interest rate policy has been hugely successful and intelligent. There will be some problems but the ability to re-finance at a lower level will help enormously. CM = The current 4 ¾% is a bargain mortgage rate and an intelligent thing for the government to do.

Q. (WSJ) Do you draw a line in the sand at holding a minimum $10 billion cash level and does that mean less acquisitions? Also would Berkshire issue shares or bonds to finance an acquisition?

A. We would not issue shares or bonds for acquisitions. When I say $10 billion I would not likely run it down that low and remember we produce more cash every month. On April 1st we came up with $3 billion for the Dow Chemical acquisition. We currently have $20 billion excluding cash at Mid-American and we are willing to do a $10 billion deal. For the right acquisition opportunity (like a GEICO and AXP deals) we would sell some of our equity holdings.

Q. (Brazil) Would you make an investment in Brazil and what businesses would you be interested in?

A. We have owned the Brazilian currency, the Real, although we don't now own any foreign currencies. We would invest in Brazil for the right deal. We are looking for great businesses anywhere. We make money in Brazil with our ownership interest in Coke.

Q. (Taiwan) Berkshire investment BYD (Chinese producer of lithium batteries) was accused of document theft & patent infringement by rival Foxcroft. Isn't there an ethical problem?

A. Munger - the ethical problem was not with BYD. Foxcroft was trying to obstruct an up and coming rival. This CEO is highly ethical - when he wanted to give stock to his managers he gave them some of his stock instead of issuing new company stock. The company had a patent challenge from a Japanese company and won their case in a Japanese court! If you want to bet against this man it will be your ticket to the poor house. WB = We have a litigious society, particularly in the US. There are 2 million automobile accidents each year and most people don't think it was their fault.

Q. (Bloomberg) There seems to be a systematic risk posed by some large life insurance companies like AIG. Should they get TARP (Troubled asset relief program) funds?

A. There were some troubles with certain life equity products, particularly those that guaranteed losses below a certain floor in the stock market index. There was also trouble on the asset side by stretching for yield (essentially buying much riskier investments) because of competitive pressures. They bought things based on ratings instead of doing their own research. You should never reach for yield because you'll lose it on your principle. Life and annuity policies were sold without enough premium. Never let sales offices decide what should be sold. Policies were sold that if you assets went down the insurance company would guarantee to make you whole. Competition made them do foolish things.

Q. (Brazil) Are you investing outside the U.S. and do you like the Brazilian currency (Real)?

A. We've held the Real before but have no currency positions today. We are probably less interested in international because there are so many opportunities in the U.S. today. We would do an international deal at the right price. We have exposure all over the world through our U.S. companies and investments and foreign exchange advantages and disadvantages usually balance out. Our international investments are not currency driven. We usually do not hedge against currencies.

Q. (Harpers) What brings people here to Berkshire and what do you want them to take away?

A. In 1981 we had just 12 people and two of those were family! People get more by coming here than we write in our annual report and what is reported in the media. We want them to feel that they truly are our partners and to have fun with other shareholders. Most have a good time and learn something. Of course we want them to buy our products and they like doing so (note: usually up to 30% discounts) and we make money. We've sold $180,000 of Sees Candies this year up from $160,000 last year. We've sold enough new Geico insurance that it will pay for the cost of the annual meeting (lifetime benefit of the new policy holders). Plus we feel better because we like to be close to our shareholders and partners. Munger – There is no other annual meeting like Berkshire’s. It’s what I call a lollapalooza effect due to a confluence of events. For a shareholder to say, ‘I've been going every year since 1981" it is a nice way to say you’re very smart and rich!’

Q. (BBC)You mentioned that Singapore had been the least foolish of all financial authorities. Where do you think the future financial center will move to, Singapore?

A. It is easy for Singapore because they are a small country. I don't think there will be much change in the near future.

Q. (BBC) Why do you continue to hold Moody's (NYSE: MCO) shares despite their involvement in the financial crisis?

A. The government and many companies got it wrong so there is no sense in picking on just the rating agencies. The media also got it wrong but they do a good job and that means less crazy things get done. Government agency OFHEO only had to regulate two companies, Freddie & Fannie and look how that turned out. Greed, stupidity and the mentality that "everyone was doing it" caused the problems. Our managers at Berkshire must always have a better reason than ‘everyone else is doing it.’ For ratings agencies it was an over reliance on their mathematical models rather than any conflict of interest. The biggest mistake that they and everyone else, bar a few notable exceptions, made was to assume that housing prices couldn't fall too much (note: when Inside Value sold Fannie Mae the company was assuming a 7% peak to trough fall in house prices - that's why we sold). Munger - they were more delusional than mendacious (dishonest). Everyone was looking for the tooth ferry. It was like going to Las Vegas and staying up all night playing against the odds. I admire a contrarian press. Carol Loomis once said that ‘the press operates in two worlds; isn’t it wonderful and wasn’t it awful.’ WB = Noah built his arch but no one else did.

And that ends our press conference. Thank you. (applause)