

# Leyland Lines

January 2011

Leyland Lines is our monthly newsletter providing investors with our insights on the overall market, individual companies and other relevant issues. All the information contained in this newsletter is for general reading only and should not be taken as a personal recommendation. Companies and ideas discussed in this newsletter are not necessarily buy or sell recommendations. We don't know when the opportunity to purchase or sell at favourable prices may occur, but when it does we act decisively. For that reason we encourage clients to allow us discretion using our Individually Managed Account service.



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## Welcome to the January 2011 edition of Leyland Lines.

Firstly, we wish all those dealing with the floods across Australia all the very best in their efforts to regroup and rebuild.

Last year was flat, and we seemed to constantly espouse the frailties of forecasting markets. Investors can often feel uncomfortable with a lack of activity on their portfolio, and begin trading in the pursuit of short-term gains. Whilst this activity satisfies a trader's requirement to feel busy, it rarely results in a positive outcome for the investors. Patience is a virtue, and activity for activities sake is more often than not value destructive.

The market has appreciated c. 4.5% this year, due in large part by a slowdown in negative news-flow from off-shore. It is the measure of a successful investor to buy whilst the broader market is nervous, and sell when others are

overly optimistic. Volatility is a function of the market, and should be embraced by investors taking advantage of price discrepancies. Whilst diversification is effective in smoothing fluctuations too much diversification can encroach on performance. Investors often diversify into sectors and companies they have little or no knowledge of in an attempt to achieve an efficient 'asset allocation'. The question should be asked, why?

In this edition of Leyland Lines we take a look at Asciano Limited, Panoramic Resources Limited, and provide the latest instalment of Warren Buffett's early letter to shareholders. We wish you all the best for the year ahead, and as always please feel free to contact our portfolio managers if you if you would like to discuss your investment strategy for 2011.

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# Leyland Lines

## Asciano Group

Asciano Limited (AIO) is a transport infrastructure business, with a focus on ports and rail.

Asciano announced two downgrades in 2010. A weaker operating environment led to the first, and the second was due to the recent rain out of the control of management. Notwithstanding, Asciano remain exposed to a structurally growing coal market, especially in Queensland.

### Key Numbers

Price: \$1.56

EPS		P/E		ROE	DPS (CPS)	Yield	Debt/Equity
2010	2011(e)	2010	2011(e)				
0.064	0.09	17.8	14	10.20%	\$0.02	1.28%	82%

### Impact of flooding in Queensland and NSW

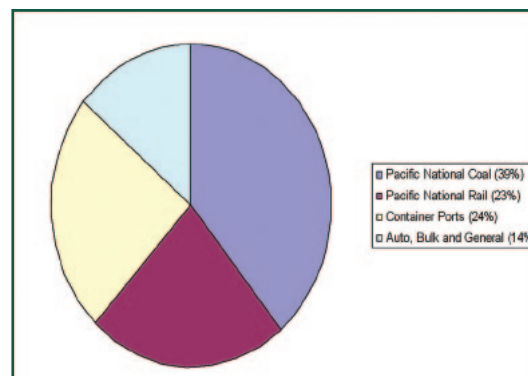
The recent wet weather has had a long-term impact on AIO's Coal and Intermodal business. The impact from the wet weather is largely recoverable through take-or-pay contracts. Under these agreements end-user companies agree to use AIO, or pay a fee. Notwithstanding, labour is a fixed cost, and will impact earnings given no revenue offset. Adverse weather conditions will affect rail operations in NSW and Queensland, with the impact estimated at circa 3-5% of NPAT.

**Queensland:** A number of AIO's coal customers have declared 'force majeure', enabling them to give up contracted capacity for up to 12 months. This indicates that they don't anticipate coming back on line any time soon. Assuming a full shut-down of Asciano's Qld operations for 1 month, the impact would be \$7m, or 1% of forecast EBIT.

**Hunter Valley (NSW):** Operations are being affected by wet weather and coal chain congestion. Hunter Valley operations account for 20% of EBIT, however, disruption on the scale of Queensland is not anticipated. If the Hunter Valley network was closed, the impact would be \$12m/month, or 2% of forecast EBIT

The total cost of the floods is estimated to be \$10-15m, or 3-5% of NPAT. The exact impact will not be known until the duration of the disruption is known, and ongoing wet weather will have an obvious impact.

Asciano is made up on four separate divisions;



### Pacific National Coal

Pacific National Coal operates in Qld, SA, and NSW and is the second largest coal haulage operator in Australia. Organic growth is being promoted through improvements in coal supply chain capacity.

NSW: 80% mkt share  
(reduced from 100% in 2005)

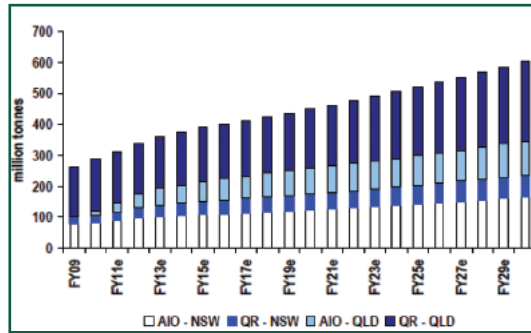
Qld: 15% mkt share  
(aims to secure 30% by 2015)

Coal volumes were up 27% pcp in the Sept Quarter 2010. Queensland expansion remains the primary driver of growth. Congestion in NSW and poor weather will continue to negatively impact volumes.

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## Asciano Group cont'd

QR National is PN Coal's major competitor in NSW and Qld.



### Result – FY10

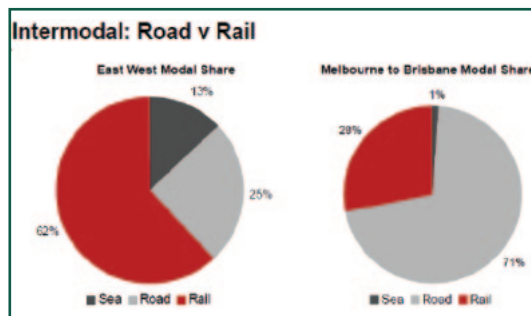
Coal delivered 60% increase in EBIT pcp, predominantly as a result of its entry into the Queensland market and ongoing strength in the NSW coal export market.

Growth in the coal export market is expected to continue to grow (1Q11 export volumes are up 7% pcp). Adverse weather conditions and supply chain congestion in NSW could impede growth.

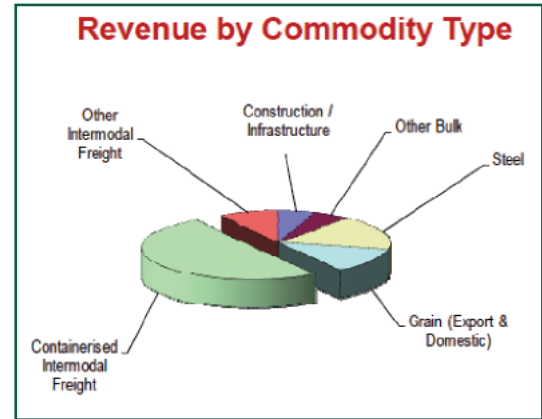
### Pacific National Rail – Intermodal

Asciano is Australia's leading provider of interstate non-bulk rail freight services. Demand comes from retail, removalists, automotive and other fast moving consumer goods. Key drivers of this business are demand for Australian commodities, crop production levels and rainfall. The A\$, global GDP growth and oil prices also impact earnings.

Competition for this business comes mainly from road transport, rather than other rail providers.



AIO is targeting improved returns in this division through improved customer service and lower costs.



Major Pacific National Rail customers include Toll, Linfox, K&S, BlueScope, OneSteel and GrainCorp, with contract duration varying from 2012 to 2017.

Active rolling stock consists of 360 locomotives and 7,089 wagons. Volumes have been reasonably flat in this division, and forecast to grow only 1.7% in FY11.

### Result – FY10

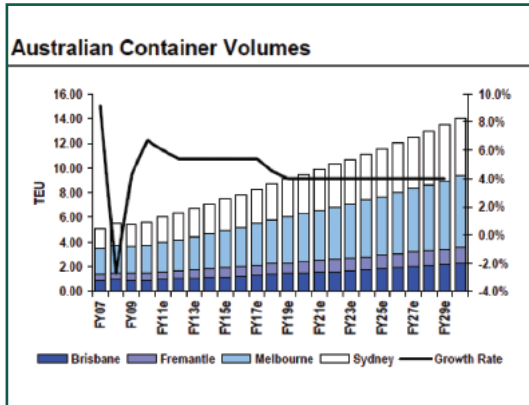
Intermodal division generated \$819m in revenue versus \$885m in the previous year. Regardless of the reduction in revenue, EBIT grew by 22% through cost controls and improved utilisation and productivity. Lower container volumes were somewhat offset by increased steel volumes.

### Container Ports (Patrick Stevedoring)

The Patrick division provides port related services to importers, exporters and shipping lines. The container port business operates at Australia's major ports in Sydney, Brisbane, Melbourne and Fremantle. This business operates as a duopoly with DP World. However, Hutchison Port Holdings, has recently been awarded new berths in Sydney and Brisbane, further increasing competition.

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## Asciano Group cont'd



### Result FY10

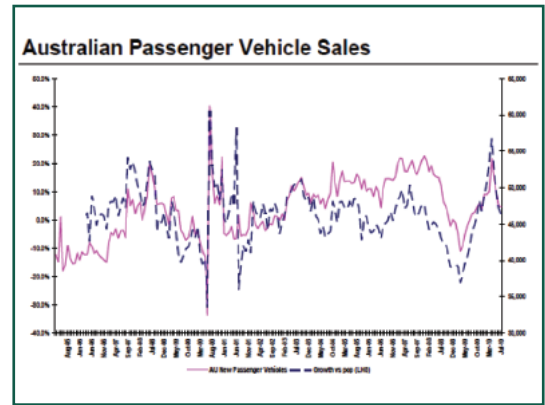
Revenue was down 3% pcp to \$721m in FY10. EBIT fell by 9% as a result of poor operating performance from the Port Logistics business, the loss of the OVSA services and Port Botany disruptions. However, actual port volumes were up 10 – 15% and forecast to continue to grow into the future as domestic and global GDP numbers improve.

Any improvement on this performance is dependant to the recovery in both the domestic and global economies, with significant leverage to any growth in container throughput. Margins are also forecast to expand to 20% through cost efficiencies.

### Auto, Bulk and General

Asciano operates three market leading units within this division;

1. Autocare: Automotive processing, storage and delivery service
2. General Stevedoring: Bulk and general stevedoring operation
3. Ports and Bulk Rail: Integrated from source, through rail, to ship



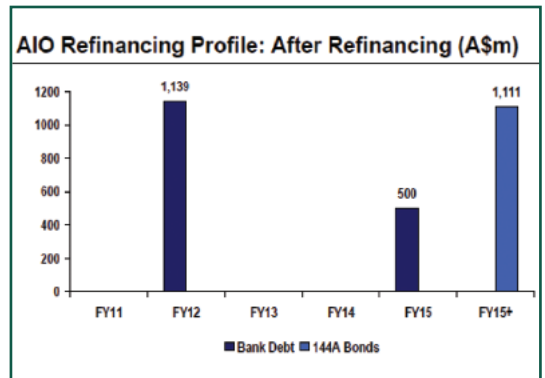
### Result FY10

Revenues declined 2% to \$682m with EBIT down 9% to \$73m.

Vehicle movements were up 10% pcp as at Sept Quarter 2010, as inventories are re-stocked. Grain was also strong, but this was offset by weakness in other sectors.

### Balance Sheet

Asciano has issued Senior Guaranteed Notes in the US to the value of USD1bn (400m 5year and 600m 10 year). The proceeds will be used to pay down existing bank debt, diversify funding and lengthen average maturity. AIO has ~A\$2.75bn of drawn debt facilities, with ~A\$0.7bn of undrawn facilities. Bank debt of A\$2.25bn matures in May 2012 and a further A\$0.5bn in December, 2014.



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## Asciano Group cont'd

### Drivers of value for Asciano shareholders

The key drivers of value for Asciano shareholders is the leverage to the coal export market. AIO enjoy a market leading position in an industry with high barriers to entry.

Domestic and global GDP numbers will impact demand for rail and port infrastructure. Ports and rail volumes are cyclical, and any 'double-dip' in the global economy will impact throughput.

The ability to continue to deliver cost savings is a risk, with capex requirements onerous. A third operator at major ports will provide increased competition.

## Panoramic Resources Ltd

Panoramic Resources Ltd is an established Western Australian nickel sulphide producer operating two mines. The Company has two underground mines; the Savannah Project in the Kimberley and the Lanfranchi Project south of Kambalda, along with the Copernicus Project open pit mine, currently on care and maintenance, near Savannah. Panoramic employs approximately 500 people, is an ASX top 200

Company with a market capitalisation of \$530 million and has a growing resource base and production profile.

The company is rather unique in the mid-cap resources space due to the fact that it has no debt, \$158 million in cash/ liquid assets/ receivables, an undemanding P/E Ratio of 10X and paid a very robust 6.9% fully franked dividend for 2010.

### Quarterly production summary – by operation

		Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	q/q %	y/y %	Q2 11E	% Var
<b>Savannah</b>										
Ore mined	kt	164.3	161.4	174.3	157.6	144.5	-8.3%	-12.0%	170.0	-15%
Ore treated	kt	170.3	156.1	176.4	159.5	138.7	-13.0%	-18.6%	170.0	-18%
Grade	%	1.3%	1.2%	1.2%	1.4%	1.2%	-15.2%	-10.7%	1.4%	-13%
Nicke-in-conc	kt	1.9	1.6	1.8	1.9	1.39	-26.5%	-27.4%	1.97	-29%
Copper-in-conc	kt	1.18	0.84	0.98	1.01	0.80	-21.5%	-32.8%	1.06	-25%
Payable cash cost	US\$/lb	4.37	5.42	4.91	5.41	7.51	38.8%	71.9%	5.11	47%
<b>Lanfranchi</b>										
Ore mined	kt	89.0	108.5	112.7	97.9	105.4	7.6%	18.5%	90.0	17%
Ore treated	kt	89.0	110.9	112.0	104.5	98.8	-5.4%	11.1%	90.0	10%
Grade	%	2.4%	2.5%	2.4%	2.3%	2.5%	7.7%	3.3%	2.4%	3%
Nickel-in-ore	kt	2.2	2.7	2.7	2.3	2.65	16.2%	22.8%	2.20	21%
Copper-in-ore	kt	0.20	0.26	0.21	0.19	0.20	8.6%	3.1%	0.17	18%
Payable cash cost	US\$/lb	5.77	5.03	5.12	5.71	6.02	5.4%	4.3%	5.66	6%

## Operations Overview

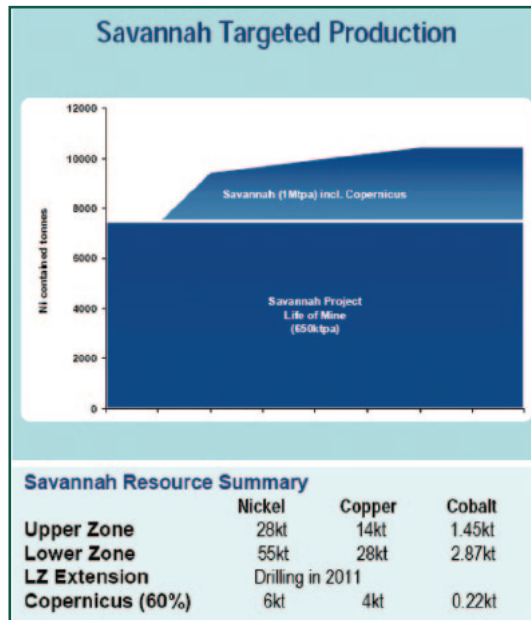
### Savannah

This project is located 240 kilometres south of Kununurra in the East Kimberley region of Western Australia and consists of a nickel sulphide ore body, underground mine, process plant and associated infrastructure. December quarterly production numbers were slightly disappointing due to the failure of an exhaust fan, which restricted underground access. Due to the restricted access, only lower grade

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## Panoramic Resources Ltd cont'd

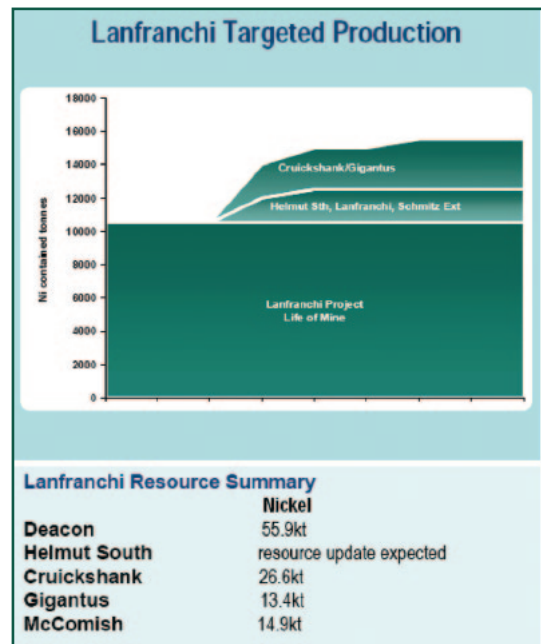
areas of the mine were available for extraction and processing. Ongoing, these issues will be resolved and the company intends to increase underground production rates and optimise cut-off grades and mining methods. Located just 50 kilometres south of the Savannah Project is the Copernicus Joint Venture (Panoramic 60%, Thunderlarra 40%) open pit which is currently on care and maintenance. Re-starting Copernicus is under constant review and when the time comes should provide further growth opportunities to the company.



### Lanfranchi

The Lanfranchi Operations are located 42 kilometres south of Kambalda, Western Australia. Panoramic acquired a 75% interest from BHP Billiton Nickel West (formerly WMC Resources) in June 2004, and in 2009 purchased the remaining 25% from its joint venture partner in the project, Brilliant Mining Corp. Recent discoveries of high-grade nickel Helmut South zone of the mine have further complemented the other three producing channels being Helmut/Deacon, Schmitz and Lanfranchi. The Company is very optimistic about further discoveries at other channels of Lanfranchi and an aggressive forward programme

has been planned for 2011/12. December 2010 quarterly production of 2.4kt nickel-in-concentrate at Lanfranchi was well above market consensus estimates and helped off-set the problems experienced at Savannah over the period.



### Further Exploration Activity

The Company has committed to spend at least \$12 million on exploration in 2010/11, up from \$7 million in 2009/10. Half these funds will be allocated to the Savannah and Lanfranchi Projects with the balance to go to diversified growth investments through joint ventures described below.

### Northern Territory

In July 2009, Panoramic entered into a Farm-in Agreement with Territory Uranium Limited to earn up to 80% in the Bluebush copper-gold Project in the Tenant Creek region. The project is located between the Tennant Creek mineral field and the Rover mineral field where recent exploration success has provided renewed interest in an area which has historically produced over five million ounces of gold and 500,000 tonnes of copper. Panoramic will spend \$500,000 in the

MARKET UPDATE

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## Panoramic Resources Ltd cont'd

first 12 months, while Territory will manage the Project until Panoramic has earned 51% equity by spending \$3 million over three years.

### Sweden

In September 2008, the Company entered into a joint venture with Norrland Resources Ltd to explore for nickel sulphide mineralisation in the Vasterbotten Nickel-Copper-Cobalt-Platinum Group Metals district, Sweden. Norrland has secured 1,000 square kilometres of exploration licences within the Vasterbotten District which is geographically similar to the East Kimberley, where the Savannah project is located.

### Alaska

In July 2010, Panoramic negotiated a farm in agreement with Triton Gold Limited and Tushtena Resources Inc to explore for high grade gold on the Tushtena Gold Project in Alaska. The Project covers an area of 41.4 square kilometres in the 1200 kilometres long Tintina Gold Belt province which is host to several world class gold deposits.

### Scandinavia

In July 2010, the Company formed an alliance with the highly experienced Drake Resources Ltd to explore and develop base and precious metal opportunities in Scandinavia. Current focus is primarily copper-zinc targets in various parts of Finland.

### Investments

Panoramic also has interests in the following ASX listed Companies as follows;

- Magma Metals: 18.4 million shares for a market value of \$10.58 million

- Thundelarra Exploration: 2.5 million shares for a market value of \$1.51 million
- Ampella Mining: 500,000 shares for a market value of 1.39 million. We note that the Company sold 1.8 million shares in the last quarter generating \$6.5 million pre-tax trading profit
- Liontown Resources: 2.8 million shares for a market value of \$280,000

### View

As with all resource companies, the main risk Panoramic faces is downward movement in commodity prices (predominantly nickel) and the sector as a whole is subject to political, financial and operational risks.

The highly experienced management team has stated they intend to continue rewarding shareholders with regular dividends and considering the healthy cashflows (\$131.8 million in 2010), zero debt and cash/ liquid assets of \$158 million suggest this statement to be very achievable. Combine this with strong growth potential both organically from Lanfranchi/ Savannah and externally via exploration and investment in other provinces/ base metals should see this company further prosper.

PAN \$2.30	2009 A	2010 A	2011 E	2012 E	2013 E
EPS (cps)	7.30	25.57	21.77	22.53	20.80
PE (x)	31.51	9.00	10.57	10.21	11.06
DPS (cps)	3.00	16.50	9.67	9.80	8.60
Yield (%)	1.30%	6.90%	4.20%	4.26%	3.74%
Franking (%)	100%	100%	100%	100%	100%

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## Warren Buffett – Letter to Partners January 1969

### Our Performance in 1968

*Everyone makes mistakes.*

At the beginning of 1968, I felt prospects for BPL performance looked poorer than at any time in our history. However, due in considerable measure to one simple but sound idea whose time had come (investment ideas, like women, are often more exciting than punctual), we recorded an overall gain of \$40,032,691.

Naturally, you all possess sufficient intellectual purity to dismiss the dollar result and demand an accounting of performance relative to the Dow-Jones Industrial Average. We established a new mark at plus 58.8% versus an overall plus 7.7% for the Dow, including dividends which would have been received through ownership of the Average throughout the year. This result should be treated as a freak - like picking up thirteen spades in a bridge game. You bid the slam, make it, look modest, pocket the money and then get back to work on the part scores. We will also have our share of hands when we go set.

The following summarizes the year-by-year performance of the Dow, the Partnership before allocation (one quarter of the excess over 6%) 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
1966	-15.6	+20.4	+16.8
1967	+19.0	+35.9	+28.4
1968	+ 7.7	+58.8	+45.6

- (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.

On a cumulative or compounded basis, the results are:

Year	Overall Results From Dow (1)	Partnership Results (2)	Limited Partners' Results (3)
1957	- 8.4%	+10.4%	+ 9.3%
1957-58	+ 26.9	+ 55.6	+ 44.5
1957-59	+ 52.3	+ 95.9	+ 74.7
1957-60	+ 42.9	+ 140.6	+107.2
1957-61	+ 74.9	+ 251.0	+181.6
1957-62	+ 61.6	+ 299.8	+215.1
1957-63	+ 94.9	+ 454.5	+311.2
1957-64	+131.3	+ 608.7	+402.9
1957-65	+164.1	+ 943.2	+588.5
1957-66	+122.9	+1156.0	+704.2
1957-67	+165.3	+1606.9	+932.6
1957-69	+185.7	+2610.6	+1403.5
Annual Compounded Rate	+ 9.1	+31.6	+45.6

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## Warren Buffett – Letter to Partners January 1969 cont'd

### Investment Companies

On the following page is the usual tabulation showing the results of what were the two largest mutual funds (they stood at the top in size from 1957 through 1966 - they are still number two and three) 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
1966	- 7.7	- 10.0	- 2.5	- 6.2	- 15.6	+ 16.8
1967	+20.0	+22.8	+27.6	+25.2	+19.0	+28.9
1968	+ 10.3	+ 8.1	+ 6.7	+ 6.8	+ 7.7	+ 45.6
Cumulative results	+189.3	+167.7	+225.6	+200.2	+185.7	+1403.5
Annual compounded rate	9.3	8.6	10.3	9.6	9.1	25.3

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

(2) From 1968 Moody's Bank & Finance Manual for 1957-1967. Estimated for 1968.

It is interesting that after twelve years these four funds (which presently aggregate well over \$5 billion and account for over 10% of the investment company industry) have averaged only a fraction of one percentage point annually better than the Dow.

Some of the so-called "go-go" funds have recently been re-christened "no-go" funds. For example, Gerald Tsai's Manhattan Fund, perhaps the world's best-known aggressive investment vehicle, came in at minus 6.9% for 1968. Many smaller investment entities continued to substantially out-perform the general market in

1968, but in nothing like the quantities of 1966 and 1967.

The investment management business, which I used to severely chastise in this section for excessive lethargy, has now swung in many quarters to acute hypertension. One investment manager, representing an organization (with an old established name you would recognize) handling mutual funds aggregating well over \$1 billion, said upon launching a new advisory service in 1968:

*"The complexities of national and international economics make money management a full-time job. A good money manager cannot maintain a study of securities on a week-by-week or even a day-by-day basis. Securities must be studied in a minute-by-minute program. "*

Wow!

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## Warren Buffett – Letter to Partners January 1969 cont'd

This sort of stuff makes me feel guilty when I go out for a Pepsi. When practiced by large and increasing numbers of highly motivated people with huge amounts of money on a limited quantity of suitable securities, the result becomes highly unpredictable. In some ways it is fascinating to watch - and in other ways it is appalling.

### Analysis of 1968 Results

All four main categories of our investment operation worked out well in 1968. Our total overall gain of \$40,032,691 was divided as follows:

Category	Average Investment	Overall Gain
Controls	\$24,996,998	\$ 5,886,109
Generals - Private Owner	16,363,100	21,994,736
Generals - Relatively Undervalued	8,766,878	4,271,825
Workouts	18,980,602	7,317,128
Miscellaneous, primarily U.S. Treasury Bills	12,744,973	839,496
Total Income		\$ 40,309,294
Less - General Expense including Interest		276,603
Overall Gain		\$ 40,032,691

A few caveats, as mentioned in my letter two years ago, are again in order (non-doctoral candidates may proceed to next section):

1. An explanation of the various categories listed above was made in the January 18, 1965 letter. If your memory needs refreshing and your favourite newsstand does not have the pocketbook edition, we'll be glad to give you a copy.
2. The classifications are not iron clad. Nothing is changed retroactively, but the initial decision as to category is sometimes arbitrary. Sometimes later classification proves difficult; e.g., a workout that falls through but that I continue to hold for reasons unrelated or only partially related to the original decision (like stubbornness).
3. Percentage returns calculated on the average investment base by category would be significantly understated relative to Partnership percentage returns which are calculated on a beginning investment base. In the foregoing figures, a security purchased by us at 100 on January 1 which appreciated at an even rate to 200 on December 31 would have an average investment of 150 producing a 66.66% result contrasted to a 100% result by the customary approach. In other words, the foregoing figures use a monthly average of market values in calculating the average investment.
4. All results are based on a 100% ownership, non-leverage basis. Interest and other general expenses are deducted from total performance and not segregated by category. Expenses directly related to specific investment operations, such as dividends paid on short stock, are deducted by category. When securities are borrowed directly and sold short, the net investment (longs minus shorts) is shown for the applicable category's average investment.
5. The foregoing table has only limited use. The results applicable to each category are dominated by one or two investments. They do not represent a collection of great quantities of stable data (mortality rates of all American males or something of the sort) from which conclusion's can be drawn and projections made. Instead, they represent infrequent, non-homogeneous phenomena leading to very tentative suggestions regarding various courses of action and are so used by us.
6. Finally, these calculations are not made with the same loving care we apply to counting the money and are subject to possible clerical or mathematical error, since they are not entirely self-checking.

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## Warren Buffett – Letter to Partners January 1969 cont'd

### Controls

Overall, the controlled companies turned in a decent performance during 1968. Diversified Retailing Company, Inc. (80% owned) and Berkshire Hathaway, Inc. (70% owned) had combined after-tax earnings of over \$5 million.

Particularly outstanding performances were turned in by Associated Cotton Shops, a subsidiary of DRC run by Ben Rosner, and National Indemnity Company, a subsidiary of B-H run by Jack Ringwalt. Both of these companies earned about 20% on capital employed in their businesses. Among Fortune's "500" (the largest manufacturing entities in the country, starting with General Motors), only 37 companies achieved this figure in 1967, and our boys outshone such mildly better-known (but not better appreciated) companies as IBM, General Electric, General Motors, Procter & Gamble, DuPont, Control Data, Hewlett-Packard, etc.

I still sometimes get comments from partners like: "Say, Berkshire is up four points - that's great!"; or "What's happening to us, Berkshire was down three last week?" Market price is irrelevant to us in the valuation of our controlling interests. We valued B-H at 25 at yearend 1967 when the market was about 20, and 31 at yearend 1968 when the market was about 37. We would have done the same thing if the markets had been 15 and 50, respectively. ("Price is what you pay, value is what you get"). We will prosper or suffer in controlled investments in relation to the operating performances of our businesses - we will not attempt to profit by playing various games in the securities markets.

### Generals - Private Owner

Over the years this has been our best category, measured by average return, and has also maintained by far the best percentage of profitable transactions. This approach was the way I was taught the business, and it formerly accounted for a large proportion of all our investment ideas. Our total individual profits in this category during the twelve year BPL history

*"It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."*

are probably fifty times or more our total losses. The cash register really rang on one simple industry idea (implemented in several ways) in this area in 1968. We even received a substantial fee (included in Other Income in the audit) for some work in this field.

Our total investment in this category (which is where I feel by far the greatest certainty regarding consistently decent results) is presently under \$2 million, and I have nothing at all in the hopper to bolster this. What came through like the Johnstown flood in 1968 looks more like a leaky faucet in Altoona for 1969.

### Generals - Relatively Undervalued

This category produced about two-thirds of the overall gain in 1966 and 1967 combined. I mentioned last year that the great two-year performance here had largely come from one idea. I also said, "We have nothing in this group remotely approaching the size or potential which formerly existed in this investment." It gives me great pleasure to announce that this statement was absolutely correct. It gives me somewhat less pleasure to announce that it must be repeated this year.

### Workouts

This category, which was a disaster in 1967, did well during 1968. Our relatively heavy concentration in just a few situations per year (some of the large arbitrage houses may become involved in fifty or more workouts per annum) gives more variation in yearly results than an across-the board approach. I feel the average profitability will be as good with our policy, and 1968 makes me feel better about that conclusion than 1967 did.

# Leyland Lines

## Warren Buffett – Letter to Partners January 1969 cont'd

It should again be stated that our results in the Workout area (as well as in other categories) are somewhat understated, compared to the more common method of determining results computed on an initial base figure and utilizing borrowed money (which is often a sensible part of the Workout business).

I can't emphasize too strongly that the quality and quantity of ideas is presently at an all time low - the product of the factors mentioned in my October 9th, 1967 letter, which have largely been intensified since then.

Sometimes I feel we should have a plaque in our office like the one at the headquarters of Texas Instruments in Dallas which reads: "We don't believe in miracles, we rely on them." It is possible for an old, overweight ball player, whose legs and batting eye are gone, to tag a fast ball on the nose for a pinch-hit home run, but you don't change your line-up because of it.

We have a number of important negatives operating on our future and, while they shouldn't add up to futility, they certainly don't add up to more than an average of quite moderate profitability.

### Memorabilia

As one of my older friends says, "Nostalgia just isn't what it used to be." Let's take a stab at it, anyway.

Buffett Associates, Ltd., the initial predecessor partnership, was formed May 5, 1956 with seven limited partners (four family, three close friends), contributing \$105,000, and the General Partner putting his money where his mouth was by investing \$100. Two additional single-family limited partnerships were formed during 1956, so that on January 1, 1957 combined net assets were \$303,726. During 1957, we had a gain of \$31,615.97, leading to the 10.4% figure shown on page one. During 1968 I would guess that the New York Stock Exchange was open around 1,200 hours, giving us a gain of about \$33,000 per

*"Only buy something that you'd be perfectly happy to hold if the market shut down for 10 years."*

hour (sort of makes you wish they had stayed with the 5-1/2 hour, 5 day week, doesn't it), or roughly the same as the full year gain in 1957.

On January 1, 1962 we consolidated the predecessor limited partnerships, moved out of the bedroom, and hired our first full-time employees. Net assets at that time were \$7,178,500. From that point to our present net assets of \$104,429,431, we have added one person to the payroll. Since 1963 (Assets \$9,405,400), rent has gone from \$3,947 to \$5,823 (Ben Rosner would never have forgiven me if I had signed a percentage lease), travel from \$3,206 to \$3,603, and dues and subscriptions from \$900 to \$994. If one of Parkinson's Laws is operating, at least the situation hasn't gotten completely out of control.

In making our retrospective survey of our financial assets, our conclusion need not parallel that of Gypsy Rose Lee who opined, when reviewing her physical assets on her fifty-fifth birthday: "I have everything I had twenty years ago - it's just that it's all lower."

### Miscellaneous

Although the investment environment is difficult, the office environment is superb. With Donna, Gladys, Bill and John, we have an organization that functions speedily, efficiently and pleasantly. They are the best.

The office group, along with spouses (one apiece - I still haven't figured out how I should handle that plural) and children have over \$27 million invested in BPL on January 1, 1969. Assorted sizes and shapes of aunts, uncles, parents, in-laws, brothers, sisters and cousins make the BPL

# Leyland Lines

## Warren Buffett – Letter to Partners January 1969 cont'd

membership list read like. "Our Crowd" - which, so far as I am concerned, is exactly what it is.

Within a few days, you will receive:

1. A tax letter giving you all BPL information needed for your 1968 federal income tax return. This letter is the only item that counts for tax purposes.
2. An audit from Peat, Marwick, Mitchell & Co. (they have again done an excellent job) for 1968, setting forth the operations and financial position of BPL, as well as your own capital account.
3. A letter signed by me setting forth the status of your BPL interest on January 1, 1969. This is identical with the figures developed in the audit.

Let me know if anything in this letter or that occurs during the year needs clarifying. My next letter will be about July 10th, summarizing the first half of this year.

Cordially,

Warren E. Buffett

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