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BERKSHIRE HATHAWAY INC.

1981
ANNUAL REPORT TO THE STOCKHOLDERS

Berkshire Hathaway Inc.

1981 ANNUAL REPORT

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A compilation of the letters from the principal executives of Berkshire Hathaway Inc. and Blue Chip Stamps taken from the Annual Reports for the years from 1977 to and including this 1981 Report is available upon request. Direct your request to the Company at 1440 Kiewit Plaza, Omaha, Nebraska 68131.

Berkshire Hathaway Inc.

February 26, 1982

To the Shareholders of Berkshire Hathaway Inc.:

Operating earnings of $39.7 million in 1981 amounted to 15.2% of beginning equity capital (valuing securities at cost) compared to 17.8% in 1980. Our new plan that allows stockholders to designate corporate charitable contributions (detailed later) reduced earnings by about $900,000 in 1981. This program, which we expect to continue subject to annual evaluation of our corporate tax position, had not been initiated in 1980.

Non-Controlled Ownership Earnings

In the 1980 annual report we discussed extensively the concept of non-controlled ownership earnings, i.e., Berkshire's share of the undistributed earnings of companies we don't control or significantly influence but in which we, nevertheless, have important investments. (We will be glad to make available to new or prospective shareholders copies of that discussion or others from earlier reports to which we refer in this report.) No portion of those undistributed earnings is included in the operating earnings of Berkshire.

However, our belief is that, in aggregate, those undistributed and, therefore, unrecorded earnings will be translated into tangible value for Berkshire shareholders just as surely as if subsidiaries we control had earned, retained — and reported — similar earnings.

We know that this translation of non-controlled ownership earnings into corresponding realized and unrealized capital gains for Berkshire will be extremely irregular as to time of occurrence. While market values track business values quite well over long periods, in any given year the relationship can gyrate capriciously. Market recognition of retained earnings also will be unevenly realized among companies. It will be disappointingly low or negative in cases where earnings are employed non-productively, and far greater than dollar-for-dollar of retained earnings in cases of companies that achieve high returns with their augmented capital. Overall, if a group of non-controlled companies is selected with reasonable skill, the group result should be quite satisfactory.

In aggregate, our non-controlled business interests have more favorable underlying economic characteristics than our controlled businesses. That's understandable; the area of choice has been far wider. Small portions of exceptionally good businesses are usually available in the securities markets at reasonable prices. But such businesses are available for purchase in their entirety only rarely, and then almost always at high prices.

General Acquisition Behavior

As our history indicates, we are comfortable both with total ownership of businesses and with marketable securities representing small portions of businesses. We continually look for ways to employ large sums in each area. (But we try to avoid small commitments — "If something's not worth doing at all, it's not worth doing well".) Indeed, the liquidity requirements of our insurance and trading stamp businesses mandate major investments in marketable securities.

Our acquisition decisions will be aimed at maximizing real economic benefits, not at maximizing either managerial domain or reported numbers for accounting purposes. (In the long run, managements stressing accounting appearance over economic substance usually achieve little of either.)

Regardless of the impact upon immediately reportable earnings, we would rather buy 10% of Wonderful Business T at X per share than 100% of T at 2X per share. Most corporate managers prefer just the reverse, and have no shortage of stated rationales for their behavior.

However, we suspect three motivations — usually unspoken — to be, singly or in combination, the important ones in most high-premium takeovers:

(1) Leaders, business or otherwise, seldom are deficient in animal spirits and often relish increased activity and challenge. At Berkshire, the corporate pulse never beats faster than when an acquisition is in prospect.

(2) Most organizations, business or otherwise, measure themselves, are measured by others, and compensate their managers far more by the yardstick of size than by any other yardstick. (Ask a *Fortune 500* manager where his corporation stands on that famous list and, invariably, the number responded will be from the list ranked by size of sales; he may well not even know where his corporation places on the list *Fortune* just as faithfully compiles ranking the same 500 corporations by profitability.)

(3) Many managements apparently were overexposed in impressionable childhood years to the story in which the imprisoned handsome prince is released from a toad's body by a kiss from a beautiful princess. Consequently, they are certain their managerial kiss will do wonders for the profitability of Company T(arget).

Such optimism is essential. Absent that rosy view, why else should the shareholders of Company A(cquisitor) want to own an interest in T at the 2X takeover cost rather than at the X market price they would pay if they made direct purchases on their own?

In other words, investors can always buy toads at the going price for toads. If investors instead bankroll princesses who wish to pay double for the right to kiss the toad, those kisses had better pack some real dynamite. We've observed many kisses but very few miracles. Nevertheless, many managerial princesses remain serenely confident about the future potency of their kisses — even after their corporate backyards are knee-deep in unresponsive toads.

In fairness, we should acknowledge that some acquisition records have been dazzling. Two major categories stand out.

The first involves companies that, through design or accident, have purchased only businesses that are particularly well adapted to an inflationary environment. Such favored business must have two characteristics: (1) an ability to increase prices rather easily (even when product demand is flat and capacity is not fully utilized) without fear of significant loss of either market share or unit volume, and (2) an ability to accommodate large dollar volume increases in business (often produced more by inflation than by real growth) with only minor additional investment of capital. Managers of ordinary ability, focusing solely on acquisition possibilities meeting these tests, have achieved excellent results in recent decades. However, very few enterprises possess both characteristics, and competition to buy those that do has now become fierce to the point of being self-defeating.

The second category involves the managerial superstars — men who can recognize that rare prince who is disguised as a toad, and who have managerial abilities that enable them to peel away the disguise. We salute such managers as Ben Heineman at Northwest Industries, Henry Singleton at Teledyne, Erwin Zaban at National Service Industries, and especially Tom Murphy at Capital Cities Communications (a real managerial "twofer", whose acquisition efforts have been properly focused in Category 1 and whose operating talents also make him a leader of Category 2). From both direct and vicarious experience, we recognize the difficulty and rarity of these executives' achievements. (So do they: these champs have made very few deals in recent years, and often have found repurchase of their own shares to be the most sensible employment of corporate capital.)

Your Chairman, unfortunately, does not qualify for Category 2. And, despite a reasonably good understanding of the economic factors compelling concentration in Category 1, our actual acquisition activity in that category has been sporadic and inadequate. Our preaching was better than our performance. (We neglected the Noah principle: predicting rain doesn't count, building arks does.)

We have tried occasionally to buy toads at bargain prices with results that have been chronicled in past reports. Clearly our kisses fell flat. We have done well with a couple of princes — but they were princes when purchased. At least our kisses didn't turn them into toads. And, finally, we have occasionally been quite successful in purchasing fractional interests in easily-identifiable princes at toad-like prices.

Berkshire Acquisition Objectives

We will continue to seek the acquisition of businesses in their entirety at prices that will make sense, even should the future of the acquired enterprise develop much along the lines of its past. We may very well pay a fairly fancy price for a Category 1 business if we are reasonably confident of what we are getting. But we will not normally pay a lot in any purchase for what we are supposed to bring to the party — for we find that we ordinarily don't bring a lot.

During 1981 we came quite close to a major purchase involving both a business and a manager we liked very much. However, the price finally demanded, considering alternative uses for the funds involved, would have left our owners worse off than before the purchase. The empire would have been larger, but the citizenry would have been poorer.

Although we had no success in 1981, from time to time in the future we will be able to purchase 100% of businesses meeting our standards. Additionally, we expect an occasional offering of a major "non-voting partnership" as discussed under the Pinkerton's heading on page 47 of this report. We welcome suggestions regarding such companies where we, as a substantial junior partner, can achieve good economic results while furthering the long-term objectives of present owners and managers.

Currently, we find values most easily obtained through the open-market purchase of fractional positions in companies with excellent business franchises and competent, honest managements. We never expect to run these companies, but we do expect to profit from them.

We expect that undistributed earnings from such companies will produce full value (subject to tax when realized) for Berkshire and its shareholders. If they don't, we have made mistakes as to either: (1) the management we have elected to join; (2) the future economics of the business; or (3) the price we have paid.

We have made plenty of such mistakes — both in the purchase of non-controlling and controlling interests in businesses. Category (2) miscalculations are the most common. Of course, it is necessary to dig deep into our history to find illustrations of such mistakes — sometimes as deep as two or three months back. For example, last year your Chairman volunteered his expert opinion on the rosy future of the aluminum business. Several minor adjustments to that opinion — now aggregating approximately 180 degrees — have since been required.

For personal as well as more objective reasons, however, we generally have been able to correct such mistakes far more quickly in the case of non-controlled businesses (marketable securities) than in the case of controlled subsidiaries. Lack of control, in effect, often has turned out to be an economic plus.

As we mentioned last year, the magnitude of our non-recorded "ownership" earnings has grown to the point where their total is greater than our reported operating earnings. We expect this situation will continue. In just four ownership positions in this category — GEICO Corporation, General Foods Corporation, R. J. Reynolds Industries, Inc. and The Washington Post Company — our share of undistributed and therefore unrecorded earnings probably will total well over $35 million in 1982. The accounting rules that entirely ignore these undistributed earnings diminish the utility of our annual return on equity calculation, or any other single year measure of economic performance.

Long-Term Corporate Performance

In measuring long-term economic performance, equities held by our insurance subsidiaries are valued at market subject to a charge reflecting the amount of taxes that would have to be paid if unrealized gains were actually realized. If we are correct in the premise stressed in the preceding section of this report, our unreported ownership earnings will find their way, irregularly but inevitably, into our net worth. To date, this has been the case.

An even purer calculation of performance would involve a valuation of bonds and non-insurance-held equities at market. However, GAAP accounting does not prescribe this procedure, and the added purity would change results only very slightly. Should any valuation difference widen to significant proportions, as it has at most major insurance companies, we will report its effect to you.

On a GAAP basis, during the present management's term of seventeen years, book value has increased from $19.46 per share to $526.02 per share, or 21.1% compounded annually. This rate of return number is highly likely to drift downward in future years. We hope, however, that it can be maintained significantly above the rate of return achieved by the average large American corporation.

Over half of the large gain in Berkshire's net worth during 1981 — it totaled $124 million, or about 31% — resulted from the market performance of a single investment, GEICO Corporation. In aggregate, our market gain from securities during the year considerably outstripped the gain in underlying business values. Such market variations will not always be on the pleasant side.

In past reports we have explained how inflation has caused our apparently satisfactory long-term corporate performance to be illusory as a measure of true investment results for our owners. We applaud the efforts of Federal Reserve Chairman Volcker and note the currently more moderate increases in various price indices. Nevertheless, our views regarding long-term inflationary trends are as negative as ever. Like virginity, a stable price level seems capable of maintenance, but not of restoration.

Despite the overriding importance of inflation in the investment equation, we will not punish you further with another full recital of our views; inflation itself will be punishment enough. (Copies of previous discussions are available for masochists.) But, because of the unrelenting destruction of currency values, our corporate efforts will continue to do a much better job of filling your wallet than of filling your stomach.

Equity Value-Added

An additional factor should further subdue any residual enthusiasm you may retain regarding our long-term rate of return. The economic case justifying equity investment is that, in aggregate, additional earnings above passive investment returns — interest on fixed-income securities — will be derived through the employment of managerial and entrepreneurial skills in conjunction with that equity capital. Furthermore, the case says that since the equity capital position is associated with greater risk than passive forms of investment, it is "entitled" to higher returns. A "value-added" bonus from equity capital seems natural and certain.

But is it? Several decades back, a return on equity of as little as 10% enabled a corporation to be classified as a "good" business — i.e., one in which a dollar reinvested in the business logically could be expected to be valued by the market at more than one hundred cents. For, with long-term taxable bonds yielding 5% and long-term tax-exempt bonds 3%, a business operation that could utilize equity capital at 10% clearly was worth some premium to investors over the equity capital employed. That was true even though a combination of taxes on dividends and on capital gains would reduce the 10% earned by the corporation to perhaps 6%-8% in the hands of the individual investor.

Investment markets recognized this truth. During that earlier period, American business earned an average of 11% or so on equity capital employed and stocks, in aggregate, sold at valuations far above that equity capital (book value), averaging over 150¢ on the dollar. Most businesses were "good" businesses because they earned far more than their keep (the return on long-term passive money). The value-added produced by equity investment, in aggregate, was substantial.

That day is gone. But the lessons learned during its existence are difficult to discard. While investors and managers must place their feet in the future, their memories and nervous systems often remain plugged into the past. It is much easier for investors to utilize historic p/e ratios or for managers to utilize historic business valuation yardsticks than it is for either group to rethink their premises daily. When change is slow, constant rethinking is actually undesirable: it achieves little and slows response time. But when change is great, yesterday's assumptions can be retained only at great cost. And the pace of economic change has become breathtaking.

During the past year, long-term taxable bond yields exceeded 16% and long-term tax-exempts 14%. The total return achieved from such tax-exempts, of course, goes directly into the pocket of the individual owner. Meanwhile, American business is producing earnings of only about 14% on equity. And this 14% will be substantially reduced by taxation before it can be banked by the individual owner. The extent of such shrinkage depends upon the dividend policy of the corporation and the tax rates applicable to the investor.

Thus, *with interest rates on passive investments at late 1981 levels*, a typical American business is no longer worth one hundred cents on the dollar to owners who are individuals. (If the business is owned by pension funds or other tax-exempt investors, the arithmetic, although still unenticing, changes substantially for the better.) Assume an investor in a 50% tax bracket; if our typical company pays out all earnings, the income return to the investor will be equivalent to that from a 7% tax-exempt bond. And, if conditions persist — if all earnings are paid out and return on equity stays at 14% — the 7% tax-exempt equivalent to the higher-bracket individual investor is just as frozen as is the coupon on a tax-exempt bond. Such a perpetual 7% tax-exempt bond might be worth fifty cents on the dollar as this is written.

If, on the other hand, all earnings of our typical American business are retained and return on equity again remains constant, earnings will grow at 14% per year. If the p/e ratio remains constant, the price of our typical stock will also grow at 14% per year. But that 14% is not yet in the pocket of the shareholder. Putting it there will require the payment of a capital gains tax, presently assessed at a maximum rate of 20%. This net return, of course, works out to a poorer rate of return than the currently available passive after-tax rate.

Unless passive rates fall, companies achieving 14% per year gains in earnings per share while paying no cash dividend are an economic failure for their individual shareholders. The returns from passive capital outstrip the returns from active capital. This is an unpleasant fact for both investors and corporate managers and, therefore, one they may wish to ignore. But facts do not cease to exist, either because they are unpleasant or because they are ignored.

Most American businesses pay out a significant portion of their earnings and thus fall between the two examples. And most American businesses are currently "bad" businesses economically — producing less for their individual investors after-tax than the tax-exempt passive rate of return on money. Of course, some high-return businesses still remain attractive, even under present conditions. But American equity capital, in aggregate, produces no value-added for individual investors.

It should be stressed that this depressing situation does not occur because corporations are jumping, economically, less high than previously. In fact, they are jumping somewhat higher: return on equity has improved a few points in the past decade. But the crossbar of passive return has been elevated much faster. Unhappily, most companies can do little but hope that the bar will be lowered significantly; there are few industries in which the prospects seem bright for substantial gains in return on equity.

Inflationary experience and expectations will be major (but not the only) factors affecting the height of the crossbar in future years. If the causes of long-term inflation can be tempered, passive returns are likely to fall and the intrinsic position of American equity capital should significantly improve. Many businesses that now must be classified as economically "bad" would be restored to the "good" category under such circumstances.

A further, particularly ironic, punishment is inflicted by an inflationary environment upon the owners of the "bad" business. To continue operating in its present mode, such a low-return business usually must retain much of its earnings — no matter what penalty such a policy produces for shareholders.

Reason, of course, would prescribe just the opposite policy. An individual, stuck with a 5% bond with many years to run before maturity, does not take the coupons from that bond and pay one hundred cents on the dollar for more 5% bonds while similar bonds are available at, say, forty cents on the dollar. Instead, he takes those coupons from his low-return bond and — if inclined to reinvest — looks for the highest return with safety currently available. Good money is not thrown after bad.

What makes sense for the bondholder makes sense for the shareholder. Logically, a company with historic and *prospective* high returns on equity should retain much or all of its earnings so that shareholders can earn premium returns on enhanced capital. Conversely, low returns on corporate equity would suggest a very high dividend payout so that owners could direct capital toward more attractive areas. (The Scriptures concur. In the parable of the talents, the two high-earning servants are rewarded with 100% retention of earnings and encouraged to expand their operations. However, the non-earning third servant is not only chastised — "wicked and slothful" — but also is required to redirect all of his capital to the top performer. *Matthew 25: 14-30*)

But inflation takes us through the looking glass into the upside-down world of *Alice in Wonderland*. When prices continuously rise, the "bad" business must retain every nickel that it can. Not because it is attractive as a repository for equity capital, but precisely because it is so unattractive, the low-return business must follow a high retention policy. If it wishes to continue operating in the future as it has in the past — and most entities, including businesses, do — it simply has no choice.

For inflation acts as a gigantic corporate tapeworm. That tapeworm preemptively consumes its requisite daily diet of investment dollars regardless of the health of the host organism. Whatever the level of reported profits (even if nil), more dollars for receivables, inventory and fixed assets are continuously required by the business in order to merely match the unit volume of the previous year. The less prosperous the enterprise, the greater the proportion of available sustenance claimed by the tapeworm.

Under present conditions, a business earning 8% or 10% on equity often has no leftovers for expansion, debt reduction or "real" dividends. The tapeworm of inflation simply cleans the plate. (The low-return company's inability to pay dividends, understandably, is often disguised. Corporate America increasingly is turning to dividend reinvestment plans, sometimes even embodying a discount arrangement that all but forces shareholders to reinvest. Other companies sell newly issued shares to Peter in order to pay dividends to Paul. Beware of "dividends" that can be paid out only if someone promises to replace the capital distributed.)

Berkshire continues to retain its earnings for offensive, not defensive or obligatory, reasons. But in no way are we immune from the pressures that escalating passive returns exert on equity capital. We continue to clear the crossbar of after-tax passive return — but barely. Our historic 21% return — not at all assured for the future — still provides, after the current capital gain tax rate (which we expect to rise considerably in future years), a modest margin over current after-tax rates on passive money. It would be a bit humiliating to have our corporate value-added turn negative. But it can happen here as it has elsewhere, either from events outside anyone's control or from poor relative adaptation on our part.

Sources of Reported Earnings

The table below shows the sources of Berkshire's reported earnings. Berkshire owns about 60% of Blue Chip Stamps which, in turn, owns 80% of Wesco Financial Corporation. The table displays aggregate operating earnings of the various business entities, as well as Berkshire's share of those earnings. All of the significant gains and losses attributable to unusual sales of assets by any of the business entities are aggregated with securities transactions in the line near the bottom of the table and are not included in operating earnings.

	Earnings Before Income Taxes				*Net Earnings After Tax*	
	Total		*Berkshire Share*		*Berkshire Share*	
	1981	1980	1981	1980	1981	1980
	(000s omitted)					
Operating Earnings:						
Insurance Group:						
Underwriting	$ 1,478	$ 6,738	$ 1,478	$ 6,737	$ 798	$ 3,637
Net Investment Income	38,823	30,939	38,823	30,927	32,401	25,607
Berkshire-Waumbec Textiles	(2,669)	(508)	(2,669)	(508)	(1,493)	202
Associated Retail Stores	1,763	2,440	1,763	2,440	759	1,169
See's Candies	21,891	15,475	13,046	9,223	6,289	4,459
Buffalo Evening News	(1,057)	(2,7[illegible]7)	(630)	(1,655)	(276)	(800)
Blue Chip Stamps — Parent	3,642	7,699	2,171	4,588	2,134	3,060
Wesco Financial — Parent	4,495	2,916	2,145	1,392	1,590	1,044
Mutual Savings and Loan	1,605	5,814	766	2,775	1,536	1,974
Precision Steel	3,453	2,833	1,648	1,352	841	656
Interest on Debt	(14,656)	(12,230)	(12,649)	(9,390)	(6,671)	(4,809)
Other*	1,895	1,693	1,344	1,308	1,513	992
Sub-total — Continuing Operations	$60,663	$61,037	$47,236	$49,189	$39,421	$37,191
Illinois National Bank**	—	5,324	—	5,200	—	4,731
Operating Earnings	60,663	66,361	47,236	54,389	39,421	41,922
Sales of securities and unusual sales of assets	37,801	19,584	33,150	15,757	23,183	11,200
Total Earnings — all entities	$98,464	$85,945	$80,386	$70,146	$62,604	$53,122

**Amortization of intangibles arising in accounting for purchases of businesses (i.e. See's, Mutual and Buffalo Evening News) is reflected in the category designated as "Other".*

***Berkshire divested itself of its ownership of the Illinois National Bank on December 31, 1980.*

Blue Chip Stamps and Wesco are public companies with reporting requirements of their own. On pages 38-50 of this report we have reproduced the narrative reports of the principal executives of both companies, in which they describe 1981 operations. A copy of the full annual report of either company will be mailed to any Berkshire shareholder upon request to Mr. Robert H. Bird for Blue Chip Stamps, 5801 South Eastern Avenue, Los Angeles, California 90040, or to Mrs. Jeanne Leach for Wesco Financial Corporation, 315 East Colorado Boulevard, Pasadena, California 91109.

As we indicated earlier, undistributed earnings in companies we do not control are now fully as important as the reported operating earnings detailed in the preceding table. The distributed portion of earnings, of course, finds its way into the table primarily through the net investment income segment of Insurance Group earnings.

We show below Berkshire's proportional holdings in those non-controlled businesses for which only distributed earnings (dividends) are included in our earnings.

No. of Shares			Cost	Market
			(000s omitted)	
451,650	(a)	Affiliated Publications, Inc.	$ 3,297	$ 14,114
703,634	(a)	Aluminum Company of America	19,359	18,031
420,441	(a)	Arcata Corporation (including common equivalents)	14,076	15,136
475,217	(b)	Cleveland-Cliffs Iron Company	12,942	1[illegible],362
441,522	(a)	GATX Corporation	17,147	13,466
2,101,244	(b)	General Foods, Inc.	66,277	66,714
7,200,000	(a)	GEICO Corporation	47,138	199,800
2,015,000	(a)	Handy & Harman	21,825	36,270
711,180	(a)	Interpublic Group of Companies, Inc.	4,531	23,202
282,500	(a)	Media General	4,545	11,088
391,400	(a)	Ogilvy & Mather International Inc.	3,709	12,329
370,088	(b)	Pinkerton's, Inc.	12,14	19,675
1,764,824	(b)	R. J. Reynolds Industries, Inc.	76,668	83,127
785,225	(b)	SAFECO Corporation	21,329	31,016
1,868,600	(a)	The Washington Post Company	10,628	58,160
			$335,615	$616,490
		All Other Common Stockholdings	16,131	22,739
		Total Common Stocks	$351,746	$639,229

(a) All owned by Berkshire or its insurance subsidiaries.

(b) Blue Chip and/or Wesco own shares of these companies. All numbers represent Berkshire's net interest in the larger gross holdings of the group.

Our controlled and non-controlled businesses operate over such a wide spectrum of activities that detailed commentary here would prove too lengthy. Much additional financial information is included in Management's Discussion on pages 34-37 and in the narrative reports on pages 38-50. However, our largest area of both controlled and non-controlled activity has been, and almost certainly will continue to be, the property-casualty insurance area, and commentary on important developments in that industry is appropriate.

Insurance Industry Conditions

"Forecasts", said Sam Goldwyn, "are dangerous, particularly those about the future." (Berkshire shareholders may have reached a similar conclusion after rereading our past annual reports featuring your Chairman's prescient analysis of textile prospects.)

There is no danger, however, in forecasting that 1982 will be the worst year in recent history for insurance underwriting. That result already has been guaranteed by present pricing behavior, coupled with the term nature of the insurance contract.

While many auto policies are priced and sold at six-month intervals — and many property policies are sold for a three-year term — a weighted average of the duration of all property-casualty insurance policies probably runs a little under twelve months. And prices for the insurance coverage, of course, are frozen for the life of the contract. Thus, this year's sales contracts ("premium written" in the parlance of the industry) determine about one-half of next year's level of revenue ("premiums earned"). The remaining half will be determined by sales contracts written next year that will be about 50% earned in that year. The profitability consequences are automatic: if you make a mistake in pricing, you have to live with it for an uncomfortable period of time.

Note in the table below the year-over-year gain in industry-wide premiums written and the impact that it has on the current and following year's level of underwriting profitability. The result is exactly as you would expect in an inflationary world. When the volume gain is well up in double digits, it bodes well for profitability trends in the current and following year. When the industry volume gain is small, underwriting experience very shortly will get worse, no matter how unsatisfactory the current level.

The Best's data in the table reflect the experience of practically the entire industry, including stock, mutual and reciprocal companies. The combined ratio indicates total operating and loss costs as compared to premiums: a ratio below 100 indicates an underwriting profit, and one above 100 indicates a loss.

	Yearly Change in Premium Written (%)	*Yearly Change in Premium Earned (%)*	*Combined Ratio after Policyholder Dividends*
1972	10.2	10.9	96.2
1973	8.0	8.8	99.2
1974	6.2	6.9	105.4
1975	11.0	9.6	107.9
1976	21.9	19.4	102.4
1977	19.8	20.5	97.2
1978	12.8	14.3	97.5
1979	10.3	10.4	100.6
1980	6.0	7.8	103.1
1981	3.6	4.1	105.7

Source: *Best's Aggregates and Averages.*

As Pogo would say, "The future isn't what it used to be." Current pricing practices promise devastating results, particularly if the respite from major natural disasters that the industry has enjoyed in recent years should end. *For underwriting experience has been getting worse in spite of good luck, not because of bad luck.* In recent years hurricanes have stayed at sea and motorists have reduced their driving. They won't always be so obliging.

And, of course the twin inflations, monetary and "social" (the tendency of courts and juries to stretch the coverage of policies beyond what insurers, relying upon contract terminology and precedent, had expected), are unstoppable. Costs of repairing both property and people — and the extent to which these repairs are deemed to be the responsibility of the insurer — will advance relentlessly.

Absent any bad luck (catastrophes, increased driving, etc.), an immediate industry volume gain of at least 10% per year probably is necessary to *stabilize* the record level of underwriting losses that will automatically prevail in mid-1982. (Most underwriters expect incurred losses in aggregate to rise at least 10% annually; each, of course, counts on getting less than his share.) Every percentage point of annual premium growth below the 10% equilibrium figure quickens the pace of deterioration. Quarterly data in 1981 underscore the conclusion that a terrible underwriting picture is worsening at an accelerating rate.

In the 1980 annual report we discussed the investment policies that have destroyed the integrity of many insurers' balance sheets, forcing them to abandon underwriting discipline and write business at any price in order to avoid negative cash flow. It was clear that insurers with large holdings of bonds valued, for accounting purposes, at nonsensically high prices would have little choice but to keep the money revolving by selling large numbers of policies at nonsensically low prices. Such insurers necessarily fear a major decrease in volume more than they fear a major underwriting loss.

But, unfortunately, all insurers are affected; it's difficult to price much differently than your most threatened competitor. This pressure continues unabated and adds a new motivation to the others that drive many insurance managers to push for business; worship of size over profitability, and the fear that market share surrendered never can be regained.

Whatever the reasons, we believe it is true that virtually no major property-casualty insurer — despite protests by the entire industry that rates are inadequate and great selectivity should be exercised — has been willing to turn down business to the point where cash flow has turned significantly negative. Absent such a willingness, prices will remain under severe pressure.

Commentators continue to talk of the underwriting cycle, usually implying a regularity of rhythm and a relatively constant midpoint of profitability. Our own view is different. We believe that very large, although obviously varying, underwriting losses will be the norm for the industry, and that the best underwriting years in the future decade may appear substandard against the average year of the past decade.

We have no magic formula to insulate our controlled insurance companies against this deteriorating future. Our managers, particularly Phil Liesche, Bill Lyons, Roland Miller, Floyd Taylor and Milt Thornton, have done a magnificent job of swimming against the tide. We have sacrificed much volume, but have maintained a substantial underwriting superiority in relation to industry-wide results. The outlook at Berkshire is for continued low volume. Our financial position offers us maximum flexibility, a very rare condition in the property-casualty insurance industry. And, at some point, should fear ever prevail throughout the industry, our financial strength could become an operational asset of immense value.

We believe that GEICO Corporation, our major non-controlled business operating in this field, is, by virtue of its extreme and improving operating efficiency, in a considerably more protected position than almost any other major insurer. GEICO is a brilliantly run implementation of a very important business idea.

Shareholder Designated Contributions

Our new program enabling shareholders to designate the recipients of corporate charitable contributions was greeted with extraordinary enthusiasm. A copy of the letter sent October 14, 1981 describing this program appears on pages 51-53. Of 932,206 shares eligible for participation (shares where the name of the actual owner appeared on our stockholder record), 95.6% responded. Even excluding Buffet-related shares, the response topped 90%.

In addition, more than 3% of our shareholders voluntarily wrote letters or notes, all but one approving of the program. Both the level of participation and of commentary surpass any shareholder response we have witnessed, even when such response has been intensively solicited by corporate staff and highly-paid professional proxy organizations. In contrast, your extraordinary level of response occurred without even the nudge of a company-provided return envelope. This self-propelled behavior speaks well for the program, and speaks well for our shareholders.

Apparently the owners of our corporation like both possessing and exercising the ability to determine where gifts of their funds shall be made. The "father-knows-best" school of corporate governance will be surprised to find that none of our shareholders sent in a designation sheet with instructions that the officers of Berkshire -- in their superior wisdom, of course — make the decision on charitable funds applicable to his shares. Nor did anyone suggest that his share of our charitable funds be used to match contributions made by our corporate directors to charities of the directors' choice (a popular, proliferating and non-publicized policy at many large corporations).

All told, $1,783,655 of shareholder-designed contributions were distributed to about 675 charities. In addition, Berkshire and subsidiaries continue to make certain contributions pursuant to local level decisions made by our operating managers.

There will be some years, perhaps two or three out of ten, when contributions by Berkshire will produce substandard tax deductions — or none at all. In those years we will not effect our shareholder-designated charitable program. In all other years we expect to inform you about October 10th of the amount per share that you may designate. A reply form will accompany the notice, and you will be given about three weeks to respond with your designation. *To qualify, your shares must be registered in your own name or the name of an owning trust, corporation, partnership or estate, if applicable, on our stockholder list of September 30th, or the Friday preceding if such date falls on a Saturday or Sunday.*

Our only disappointment with this program in 1981 was that some of our shareholders, through no fault of their own, missed the opportunity to participate. The Treasury Department ruling allowing us to proceed without tax uncertainty was received early in October. The ruling did not cover participation by shareholders whose stock was registered in the name of nominees, such as brokers, and additionally required that the owners of all designating shares make certain assurances to Berkshire. These assurances could not be given us in effective form by nominee holders.

Under these circumstances, we attempted to communicate with all of our owners promptly (via the October 14th letter) so that, if they wished, they could prepare themselves to participate by the November 13th record date. It was particularly important that this information be communicated promptly to stockholders whose holdings were in nominee name, since they would not be eligible unless they took action to re-register their shares before the record date.

Unfortunately, communication to such non-record shareholders could take place only through the nominees. We therefore strongly urged those nominees, mostly brokerage houses, to promptly transmit our letter to the real owners. We explained that their failure to do so could deprive such owners of an important benefit.

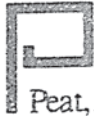
The results from our urgings would not strengthen the case for private ownership of the U.S. Postal Service. Many of our shareholders never heard from their brokers (as some shareholders told us after reading news accounts of the program). Others were forwarded our letter too late for action.

One of the largest brokerage houses claiming to hold stock for sixty of its clients (about 4% of our shareholder population), apparently transmitted our letter about three weeks after receipt — too late for any of the sixty to participate. (Such lassitude did not pervade all departments of that firm; it billed Berkshire for mailing services within six days of that belated and ineffectual action.)

We recite such horror stories for two reasons: (1) if you wish to participate in future designated-contribution programs, be sure to have your stock registered in your name well before September 30th; and (2) even if you don't care to participate and prefer to leave your stock in nominee form, it would be wise to have at least one share registered in your own name. By so doing, you can be sure that you will be notified of any important corporate news at the same time as all other shareholders.

The designated-contributions idea, along with many other ideas that have turned out well for us, was conceived by Charlie Munger, Vice Chairman of Berkshire and Chairman of Blue Chip. Irrespective of titles, Charlie and I work as partners in managing all controlled companies. To almost a sinful degree, we enjoy our work as managing partners. And we enjoy having you as our financial partners.

Warren E. Buffett
Chairman of the Board



Peat, Marwick, Mitchell & Co.

Certified Public Accountants

Kiewit Plaza Building
Thirty-Sixth and Farnam Streets
Omaha, Nebraska 68131
(402) 348-1450

The Board of Directors and Stockholders
Berkshire Hathaway Inc.:

We have examined the consolidated balance sheets of Berkshire Hathaway Inc. and consolidated subsidiaries as of January 2, 1982 and January 3, 1981 and the related consolidated statements of earnings, stockholders' equity and changes in financial position for each of the years in the three year period ended January 2, 1982. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We did not examine the consolidated financial statements of Blue Chip Stamps and Wesco Financial Corporation, the assets relating to such as reflected in the accompanying consolidated financial statements constitute 23 percent and 24 percent of the consolidated totals for 1981 and 1980, and total revenues constituting 43 percent, 37 percent and 35 percent of the consolidated totals for 1981, 1980 and 1979, respectively. These consolidated financial statements were examined by other auditors whose report thereon has been furnished to us and our opinion expressed herein, insofar as it relates to the amounts included for Blue Chip Stamps and Wesco Financial Corporation, is based solely upon the report of the other auditors.

In our opinion, based upon our examinations and the report of other auditors, the aforementioned consolidated financial statements present fairly the financial position of Berkshire Hathaway Inc. and consolidated subsidiaries at January 2, 1982 and January 3, 1981 and the results of their operations and the changes in their financial position for each of the years in the three year period ended January 2, 1982, in conformity with generally accepted accounting principles applied on a consistent basis.

Peat, Marwick, Mitchell & Co.

March 5, 1982

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(dollars in thousands)

ASSETS	*Jan. 2, 1982*	*Jan. 3, 1981*
Cash	$ 7,232	$ 9,993
Investments, other than investments in affiliates:		
Fixed maturities, principally bonds (market value: Jan. 2, 1982 — $164,075; Jan. 3, 1981 — $159,512)	206,078	187,802
Marketable equity securities (Notes 2 and 3)	641,269	525,947
Invested cash, U.S. Treasury bills and other short-term investments at cost which approximates market	63,529	50,546
Total investments, other than affiliates	910,876	764,295
Investment in Wesco Financial Corporation (Note 5)	68,874	63,040
Accounts receivable from customers, agents and others (Note 6)	49,901	49,861
Inventories (Note 7)	22,120	23,802
Real estate, equipment, furniture and leasehold improvements, at cost less allowance for depreciation and amortization (Note 8)	51,472	51,484
Deferred insurance premium acquisition costs	12,313	14,163
Other assets	35,123	33,945
	$1,157,911	$1,010,581

LIABILITIES AND STOCKHOLDERS' EQUITY		
Losses and loss adjustment expenses	$ 190,970	$ 199,128
Unearned premiums	62,269	73,281
Liability for unredeemed trading stamps	64,262	64,053
Accounts payable, accruals and other liabilities	51,915	43,462
Current income taxes	13,759	7,919
Deferred income taxes	87,089	63,329
Term debt payable (Notes 9 and 10)	97,768	104,344
Minority shareholders' interests	70,416	59,851
	638,448	615,367
Stockholders' equity:		
Common stock of $5 par value. Authorized 1,250,000 shares; issued 1,214,283 shares	6,071	6,071
Capital in excess of par value	3,517	3,517
Unrealized appreciation of marketable equity securities, net of provision for deemed applicable income taxes	196,475	135,010
Retained earnings (Notes 9 and 11)	354,058	291,454
	560,121	436,052
Less common stock in treasury, at cost (Jan. 2, 1982 — 227,774 shares; Jan. 3, 1981 — 228,224 shares)	40,658	40,838
Total stockholders' equity	519,463	395,214
Commitment and contingent liability (Notes 14 and 16)		
	$1,157,911	$1,010,581

See accompanying Notes to Consolidated Financial Statements.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(dollars in thousands except per share amounts)

	Fiscal Year Ended Saturday nearest December 31,		
	1981	1980	1979
Income Items:			
Insurance premiums earned	$159,013	$185,187	$181,949
Net sales and service revenues	263,374	259,200	247,952
Interest and dividend income	49,189	38,966	30,440
Equity in earnings excluding realized investment gain of Wesco Financial Corporation (Note 5)	7,120	8,804	8,784
	478,696	492,157	469,125
Cost and expense items:			
Insurance losses and loss adjustment expenses	103,417	118,230	120,337
Cost of products and services sold	155,661	160,261	158,710
Insurance underwriting expenses	54,119	60,219	57,870
Selling, general and administrative expenses	93,756	84,188	79,839
Interest and financing costs	11,486	9,185	5,729
	418,439	432,083	422,485
Earnings from continuing operations including minority interest in consolidated subsidiaries, before applicable income taxes and realized investment gain	60,257	60,074	46,540
Income taxes applicable to above	12,091	13,943	9,796
	48,166	46,131	36,844
Minority interest applicable to above	8,443	7,647	5,883
Earnings from continuing operations before realized investment gain	39,723	38,484	30,961
Equity in earnings before securities losses of unconsolidated banking subsidiary, divested as of Dec. 31, 1980 (Note 4)	—	4,731	4,960
Earnings before realized investment gain	39,723	43,215	35,921
Realized investment gain — continuing operations, net (Note 13)	22,881	10,790	6,896
Equity in securities losses of unconsolidated banking subsidiary, divested as of Dec. 31, 1980 (Note 4)	—	(883)	—
Net earnings	$ 62,604	$ 53,122	$ 42,817
Average shares outstanding	986,322	1,027,145	1,027,145
Per share:			
Earnings from continuing operations before realized investment gain	$ 40.27	$ 37.47	$ 30.14
Earnings before realized investment gain	40.27	42.07	34.97
Net earnings	63.47	51.72	41.68

See accompanying Notes to Consolidated Financial Statements.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(dollars in thousands)

	Common Stock*	Capital in Excess of Par Value	Net Unrealized Appreciation**	Treasury Stock***	Retained Earnings	Total Stockholders' Equity
Balance at December 30, 1978	$6,071	$3,517	$ 60,934	$(11,871)	$195,515	$254,166
Net earnings 1979					42,817	42,817
Change in 1979 in net unrealized appreciation			47,979			47,979
Balance at December 29, 1979	6,071	3,517	108,913	(11,871)	238,332	344,962
Net earnings 1980					53,122	53,122
Change in 1980 in net unrealized appreciation			26,097			26,097
Treasury shares reacquired in 1980				(28,967)		(28,967)
Balance at January 3, 1981	6,071	3,517	135,010	(40,838)	291,454	395,214
Net earnings 1981					62,604	62,604
Change in 1981 in net unrealized appreciation			61,465			61,465
Treasury shares reissued in 1981				180		180
Balance at January 2, 1982	$6,071	$3,517	$196,475	$(40,658)	$354,058	$519,463

* Common stock represents the aggregate par value of 1,214,283 issued shares of the Company's common stock, $5 par value per share. Issued shares include shares held as Treasury stock.

** Net unrealized appreciation represents the excess of carrying value of marketable equity securities over their cost, less deemed applicable income taxes, adjusted for applicable minority interest, if any.

*** Treasury stock reflects the cost of reacquired shares of the Company's issued common stock. At December 30, 1978, 187,138 shares of the Company's issued common stock were held as Treasury stock, of which the Company held 136,637 shares, and insurance subsidiaries of the Company held 50,501 shares. On December 31, 1980 the Company acquired 41,086 shares in an exchange transaction whereby the Company divested of its banking subsidiary, see Note (4). At January 2, 1982, 227,774 shares of the Company's issued common stock were held as Treasury stock, of which 225,988 shares were held by the Company and 1,786 shares were held by an insurance subsidiary of the Company.

See accompanying Notes to Consolidated Financial Statements.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

(dollars in thousands)

	Fiscal Year Ended Saturday nearest December 31,		
	1981	1980	1979
Funds provided:			
From operations:			
Net earnings	$ 62,604	$ 53,122	$ 42,817
Minority interest in earnings	11,162	8,256	6,403
Earnings including minority interest	73,766	61,378	49,220
Charges (credits) to earnings not requiring (providing) funds:			
Equity in undistributed earnings of unconsolidated subsidiaries	(5,834)	(6,473)	(9,019)
Increase (decrease) in unpaid insurance losses and loss adjustment expenses	(8,158)	1,431	16,827
Increase (decrease) in unearned insurance premiums	(11,012)	(323)	4,236
Depreciation and amortization of property, plant and equipment, including leaseholds	5,753	5,144	4,631
Decrease (increase) in deferred insurance premium acquisition costs	1,850	(511)	194
Decrease (increase) in accounts receivable	(40)	2,370	(6,948)
Decrease (increase) in inventories	1,682	1,902	(2,675)
Increase (decrease) in liability for income taxes applicable to earnings	5,697	(861)	(518)
Increase (decrease) in liability for unredeemed trading stamps	209	(3,471)	692
Increase in accounts payable, accruals and other liabilities	8,453	3,952	4,809
Other	(1,050)	895	(574)
	(2,450)	4,055	11,675
Funds provided from operations	71,316	65,433	60,895
Proceeds from issuance of debt, net of expense	—	59,992	—
Decrease in cash	2,761	4,931	—
	$ 74,077	$130,356	$ 60,895
Funds used:			
Additions to property, plant and equipment, net of disposals	$ 5,741	$ 6,835	$ 6,567
Repayment of debt	6,576	10,857	1,972
Dividends paid to minority stockholders	502	502	520
Purchase of shares of Blue Chip Stamps from minority	—	—	2,233
Cost of net purchases (sales) of investments:			
U.S. Treasury bills and short-term obligations	12,983	32,374	(42,884)
Bonds and other fixed maturity securities	18,276	705	26,735
Marketable equity securities	29,954	78,343	63,929
Unconsolidated subsidiaries	45	740	(100)
Net purchase of investments	61,258	112,162	47,680
Increase in cash	—	—	1,923
	$ 74,077	$130,356	$ 60,895

See accompanying Notes to Consolidated Financial Statements.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

January 2, 1982
(dollars in thousands)

(1) Summary of Significant Accounting Policies and Practices

(a) Basis of Presentation

The accompanying Consolidated Financial Statements include the accounts of Berkshire Hathaway Inc. (the "Company" or "Berkshire") consolidated with accounts of its subsidiaries which were majority owned at January 2, 1982. Wholly-owned subsidiaries, the accounts of which are consolidated, include companies engaged in the property/casualty insurance business (the "Insurance Group"), textile products manufacturing, and apparel retailing. Additionally included in consolidation are the accounts of Blue Chip Stamps ("Blue Chip"), a California corporation, approximately 60% owned by the Company, and Blue Chip's wholly-owned subsidiaries. Blue Chip is engaged in the promotional services business, its wholly-owned subsidiaries include See's Candy Shops, Incorporated ("See's") engaged in the candy business, and the Buffalo Evening News (the "News") which publishes a newspaper.

Blue Chip owns approximately 80% of the outstanding capital stock of Wesco Financial Corporation ("Wesco"). Berkshire's economic interest in Wesco represents slightly less than 50% of that company; accordingly, the investment in Wesco is accounted for in the accompanying Consolidated Financial Statements pursuant to the equity method of accounting.

Accounts of subsidiaries engaged in the property and casualty insurance business are maintained on the basis of a calendar year. Accounts of Berkshire, its textile and retailing subsidiaries, Blue Chip and See's are maintained on the basis of a 52-53 week fiscal year ending with respect to December 31. The 1981 operations of the textile and apparel retailing businesses covered the 52 weeks ended January 2, 1982. The 1981 operations of Blue Chip and See's covered the 52 week period ended December 26, 1981. Accounts of the News are maintained on the basis of a calendar year.

(b) Investments in Securities, Other Than Affiliates

Investments in obligations with fixed dates of maturity, including convertible bonds and redeemable preferred stocks, are stated at cost, adjusted where appropriate for accretion of discount or amortization of premium.

Investments in marketable equity securities held by members of the Insurance Group are carried at market value. Investments in marketable equity securities held by Berkshire and by subsidiaries of Berkshire which are not members of the Insurance Group are carried at the lower of aggregate cost or market.

Blue Chip, at both December 26, 1981, and at December 27, 1980 held an investment in non-voting stock of Pinkerton Holding Corporation ("PHC") which is reflected in other assets at its cost of $4,163. There is no trading market for this stock. PHC's principal assets are equity securities of Pinkerton's, Inc. ("PI"). Blue Chip also holds non-voting securities of PI, the cost of which ($19,201) is included in marketable equity securities. Blue Chip's interest in PI, both direct and indirect (through PHC), represents a beneficial ownership in the equity of PI of approximately 37% at December 26, 1981, (35% at December 27, 1980), but because this interest is represented by non-voting stock, Blue Chip does not account for this interest pursuant to the equity method of accounting. Berkshire's economic interest in the equity of PI is reduced to approximately 22% at January 2, 1982, taking into account the minority interest of Blue Chip which is outstanding.

(c) Insurance Premiums

Insurance premiums are recognized as revenues ratably over the terms of the policies. Unearned premiums are computed on a monthly or daily pro rata basis and are stated after deduction for reinsurance placed with reinsurers in the amount of $1,617 at December 31, 1981 and $2,264 at December 31, 1980. Premium acquisition costs such as commissions, premium taxes and a portion of certain other underwriting expenses, for financial reporting purposes, are deferred and charged against income as the related premiums are earned. For statutory insurance accounting and income tax reporting purposes, premium acquisition costs are charged against income when incurred.

Dividends to policyholders, primarily relating to workers' compensation coverages, are reflected in the accompanying statements of earnings as a deduction from earned premiums; this reduction amounted to $3,534 for 1981, $2,405 for 1980 and $3,221 for 1979.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

January 2, 1982

(dollars in thousands)

(1) Summary of Significant Accounting Policies and Practices *(Continued)*

(d) Losses and Loss Adjustment Expenses

The Insurance Group provides for losses and loss adjustment expenses based on (1) aggregate case basis estimates for losses reported, relating to direct premiums written, (2) estimates of incurred but not reported losses, and (3) estimates received from primary insurers with respect to assumed reinsurance. The resulting liability provision is reduced for amounts recoverable on account of reinsurance amounting to $6,162 at December 31, 1981 and $4,742 at December 31, 1980. Incurred losses and loss adjustment expenses are net of recoveries of salvage and subrogation collected or in process of collection in accordance with statutory requirements; additional amounts recoverable as salvage or on account of subrogation, relating principally to automobile physical damage coverages, are not recognized as they are considered immaterial in the aggregate.

(e) Stamp Service Accounting

Blue Chip recognizes stamp revenues and related redemption costs upon issuance of its trading stamps. A liability account for unredeemed trading stamps is maintained consisting of management's estimates of the future cost of redemption merchandise and service; the estimates are periodically evaluated. At the end of 1980, such an evaluation resulted in revision to both the estimated rate of redemption — which was decreased, and the estimated redemption service cost — which was increased, with the effect of increasing Berkshire's 1980 net earnings by approximately $970 (94 cents per share). There were no comparable revisions of the estimate in 1979 or 1981.

(f) Real Estate, Equipment, Furniture and Leasehold Improvements

These items of property (including significant betterments and renewals) are carried at cost, depreciated, principally on a straight line basis, over their useful lives estimated at the date of acquisition. Maintenance, repairs and renewals of a minor nature are generally charged to operations as incurred.

(g) Inventories

Inventories are stated at cost, determined for Berkshire and for the News under the last-in, first-out ("LIFO") method. Inventories of other members consolidated are stated at the lower of cost or market, with cost determined under the first-in, first-out or average cost methods.

(h) Income Taxes

Berkshire and its eligible (over 80% owned domestic) subsidiaries file a consolidated Federal income tax return. Blue Chip and its subsidiaries also file a consolidated Federal income tax return. Amounts included in the consolidated balance sheets for current Federal income taxes payable or recoverable include the direct or apportioned Federal taxes of the companies whose accounts are consolidated.

Provision has been made for deferred taxes with respect to Berkshire's equity in undistributed earnings of Blue Chip, on the assumption that such earnings will eventually be distributed, taxable as dividend income. The cumulative amount so provided was $4,645 at January 2, 1982 and $3,560 at January 3, 1981.

Deferred or prepaid income taxes are recognized in the accompanying Consolidated Financial Statements with respect to certain items of income and deductions which are recognized in the financial statements in time periods that differ from those in which they are included in the income tax returns filed for the companies. The principal such "timing difference," for which deferred income taxes of $5,664 at January 2, 1982 and $6,515 at January 3, 1981 are recognized, is deferred insurance premium acquisition costs (see note 1(c) above). Other assets include prepaid income taxes of Blue Chip amounting to $12,178 at December 26, 1981 and $11,211 at December 27, 1980 primarily in recognition of timing differences with respect to stamp redemption expenses.

The liability for deferred income taxes reflected in the consolidated balance sheets also includes $76,407 at January 2, 198[illegible] and $52,504 at January 3, 1981 representing amounts computed at capital gain rates on the net excess of market value over cost of marketable equity securities held by members of the Insurance Group.

Berkshire Hathaway Inc.
AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*
January 2, 1982
(dollars in thousands)

(2) Investments in Marketable Equity Securities

A summary of the aggregate cost and aggregate approximate market value of investments in marketable equity securities is as follows:

	January 2, 1982		
Held by	Cost	Market	Carrying Value
Insurance Group	$263,866	$536,748	$536,748
Berkshire	25,471	27,934	25,471
Blue Chip Stamps and its wholly-owned subsidiaries	79,050	96,306	79,050
	$368,387	$660,988	$641,269

	January 3, 1981		
Held by	Cost	Market	Carrying Value
Insurance Group	$237,016	$424,530	$424,530
Berkshire	21,526	22,407	21,526
Blue Chip Stamps and its wholly-owned subsidiaries	79,891	95,017	79,891
	$338,433	$541,954	$525,947

The net excess of aggregate market value over aggregate cost of marketable equity securities held at January 2, 1982 represented unrealized gains less unrealized losses as follows:

	Insurance Group	Berkshire, Blue Chip and its wholly-owned subsidiaries	Combined Total
Unrealized gains	$278,997	$ 20,327	$299,324
Unrealized losses	6,115	608	6,723
Net excess of gains	$272,882	$ 19,719	$292,601

(3) Investment in GEICO Corporation

Included in marketable equity securities held by the Insurance Group at December 31, 1981 are 7,200,000 common shares of GEICO Corporation, the approximate market value of which was $199,800 and the approximate cost of which was $47,000. The shares possessed approximately 35% of the voting rights of all GEICO shares outstanding at December 31, 1981. With respect to these shares of GEICO held by members of the Insurance Group, Berkshire is required, pursuant to Order of the Superintendent of Insurance of the District of Columbia, the corporate domicile of GEICO, to maintain an independent proxy arrangement. It is prohibited from seeking or causing to change the independent proxy. Also, under the Order, no officer or director of Berkshire, or any affiliate or subsidiary of Berkshire, is permitted to serve as a director of GEICO. As a result of the Order Berkshire is divested of its voting rights with respect to its holdings of GEICO and, accordingly, does not use the equity method of accounting for this investment.

(4) Investment in the Illinois National Bank and Trust Co. of Rockford

From April 1, 1969 to December 31, 1980, the Company owned approximately 98% of the outstanding capital stock of the Illinois National Bank and Trust Co. of Rockford, a national bank conducting a commercial banking operation in Rockford, Illinois. The Federal Bank Holding Company Act, as amended, required the Company to divest of control of the bank prior to January 1, 1981. Accordingly, as of December 31, 1980, the Company reacquired from its shareholders 41,086 shares of its issued common stock in exchange for its interest in the bank, thereby accomplishing the required divestiture.

That portion of the Company's earnings in 1979 and 1980 representing equity in earnings of the bank is reflected as earnings from "discontinued operations" in the accompanying statements of earnings for those years.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

January 2, 1982

(dollars in thousands)

(5) Investment in Wesco Financial Corporation

Wesco Financial Corporation is approximately 80% owned by Blue Chip. The investment in Wesco is stated at Blue Chip's cost plus Blue Chip's equity in Wesco's undistributed earnings since date of acquisition. The unamortized excess of Blue Chip's equity in net assets of Wesco over its carrying value was $18,806 at the end of 1981 and $19,430 at the end of 1980. This excess is being amortized by Blue Chip over 40 years: annual amortization ($624) is reflected under the caption "Equity in earnings excluding realized investment gain of Wesco Financial Corporation" in the Statement of Earnings for each of the past three years. Wesco owns Mutual Savings and Loan Association, Pasadena, California and has subsidiaries engaged in the steel products service business. Wesco and its consolidated subsidiaries hold investments in marketable securities which at December 31, 1981 had a cost of $91,307 and a market value of $99,472. Summarized consolidated financial information of Wesco and its subsidiaries appears elsewhere in this report.

In 1980, Wesco's savings and loan subsidiary sold its fifteen branches and recorded a gain from the sale transaction. Net earnings of Berkshire for 1980 benefited approximately $1,293 ($1.26 per share) from the transaction.

(6) Receivables

Accounts receivable from customers, agents and others was made up of the following:

	Jan. 2, 1982	Jan. 3, 1981
Insurance Group:		
Agents' balances and premiums in course of collection	$ 21,596	$ 21,759
Investment income due and accrued	5,907	5,273
Reinsurance recoverable on loss payments	5,653	5,665
Amounts due from sales of securities	321	603
	33,477	33,300
Trade accounts receivable of other businesses, net of allowances for doubtful accounts	16,424	16,561
Total receivables	$ 49,901	$ 49,861

(7) Inventories

A summary of inventories follows:

	Jan. 2, 1982	Jan. 3, 1981
Textile business	$ 5,643	$ 7,700
Retailing business	6,077	5,642
Candy business	5,635	6,260
Other	4,765	4,200
	$ 22,120	$ 23,802

The carrying amounts for inventories determined under the LIFO method were approximately $3,566 and $2,426 less than their aggregate replacement cost at year-end 1981 and 1980, respectively.

(8) Real Estate, Equipment, Furniture and Leasehold Improvements

The composition of property, plant and equipment at the end of the past two years is shown below:

	Jan. 2 1982	Jan. 3, 1981
Land	$ 3,889	$ 3,957
Buildings	19,318	19,248
Machinery and equipment	56,152	59,840
Furniture, fixtures and leasehold improvements	19,269	11,391
	98,628	94,436
Less accumulated depreciation and amortization	47,156	42,952
	$ 51,472	$ 51,484

(9) Term Debt Payable

At the end of the past two years Berkshire's consolidated term debt payable was as follows:

	Jan. 2, 1982	Jan 3, 1981
Berkshire:		
8% Senior Notes maturing through March 1, 1993 at $1,143 annually	$ 16,571	$ 17,714
9¼% Senior Notes maturing March 1, 1985 to March 1, 1993 at $777 annually	7,000	7,000
12¾% debentures maturing from August 1, 1991 through August 1, 2005 at $4,004 annually	60,000	60,000
8% debentures due 1985, with 1% additional participating interest contingently payable	6,600	6,600
Other notes and debentures maturing through 1992 in varying annual installments, with interest at rates varying from 7½% to 9%	2,718	3,035
	92,889	94,349
Consolidated Subsidiaries:		
Term loan payable to bank by Blue Chip Stamps	—	5,000
Other notes maturing through 2006 in varying installments, with interest at rates varying from 6% to 15%	4,879	4,995
	$ 97,768	$104,344

Berkshire's Senior Note Agreements include limiting terms relating to sales of assets, mergers and consolidations, and allow the noteholders to demand prepayment at par within 60 days of notice that, during the lifetime of Warren E. Buffett, his ownership of stock of the Company, together with that of certain family affiliates, has decreased to less than 15% of the Company's outstanding capital stock. The Senior Note Agreements also impose a limitation upon "restricted payments" by Berkshire. That term includes investments by Berkshire in subsidiaries not bound by the terms of the Agreements, dividends and other equity distributions. Berkshire's investment in Blue Chip Stamps is a "restricted payment" under the terms of the Agreements. Retained earnings of approximately $98,000 as of January 2, 1982 were free of restriction by this provision, the balance is restricted.

Principal payments on term debt outstanding at January 2, 1982 are required as follows:

1982	$ 2,150
1983	1,536
1984	1,479
1985	8,863
1986	2,447
Thereafter	81,293
	$97,768

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

January 2, 1982
(dollars in thousands)

(10) Lines of Credit — Subsequent Loan Agreement

Blue Chip has a bank line of credit of $10,000 expiring June 30, 1983 requiring maintenance of $500 compensating balances. Borrowings under the line require collateral in the form of marketable securities with a value of at least 150% of the amounts borrowed. Interest rates on borrowings under the line are at the bank's prime rate or below. Additionally, Blue Chip and certain of its subsidiaries maintain stockbrokerage margin accounts. Margin account borrowings (none at Dec. 26, 1981) which may be outstanding from time to time bear interest based on broker call rates.

During 1980 and 1981, the Company had a $10,000 line of credit arrangement with The First National Bank of Boston, for which it agreed to maintain average balances with the Bank of 5% of the line plus 5% of any borrowings under the line. The line was not used in 1980 nor in 1981.

In March, 1982, the Company entered into a Revolving Credit and Term Loan Agreement with the First National Bank of Boston (the "Bank"). The Agreement provides for loans of up to $50 million by the Bank to the Company during a revolving term period which extends to February 28, 1985. The outstanding balance of the loans on February 28, 1985 will be repayable in sixteen equal quarterly installments. During the revolving term period of the Agreement, the Company will pay the Bank a committment fee on the unused portion of the committment at the per annum rate of ¼ of 1%. Loans during the revolving term period will bear interest at the Bank's Base (prime) rate for domestic money borrowings under the Agreement, or if the Company elects a form of loan involving Eurodollars, at ½ of 1% above the London Inter-Bank Offering Rate (LIBOR) for Eurodollar deposits. After the revolving term period, the interest rates payable on the loans will be ¼ of 1% over Base rate for outstanding domestic borrowings or ¾ of 1% over LIBOR for Eurodollar borrowings. The Agreement includes provisions for termination by the Bank of its committment and the repayment of borrowings in twelve equal quarterly installments if Warren E. Buffett ceases to act as chairman and chief executive officer of the Company or if total borrowings by the Company and its consolidated subsidiaries exceed a formula amount, generally 35% of Capitalization as defined.

(11) Dividend Restrictions — Insurance Subsidiaries

Payments of dividends by Insurance Group members are restricted by insurance statutes and regulations, to the extent that not more than approximately $70 million of dividends could be paid in 1982 by insurance subsidiaries to the Company, without prior regulatory approvals.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

January 2, 1982

(dollars in thousands)

(12) Income Taxes

The consolidated statements of earnings reflects charges for income taxes applicable to:

	1981	1980	1979
Operating earnings	$12,091	$13,943	$ 9,796
Realized investment gain — continuing operations	10,421	4,401	2,703
Security losses of bank	—	(345)	—
	$22,512	$17,999	$12,499
These taxes are comprised of:			
Federal	$19,948	$15,348	$10,786
State	2,428	2,489	1,583
Foreign	136	162	130
	$22,512	$17,999	$12,499

Income taxes applicable to operating earnings ,as set forth above, are reconciled in the table which follows to hypothetical amounts computed at the Federal statutory rate.

	1981	1980	1979
Earnings from continuing operations including minority interests, before applicable income taxes and realized investment gain	$60,257	$64,805	$51,600
Hypothetical amounts applicable to above computed at Federal statutory rate (46%)	$27,718	$29,810	$23,736
Decreases, resulting from:			
Tax-exempt interest income	(3,190)	(3,042)	(2,747)
85% dividends received credit	(11,146)	(8,640)	(6,012)
100% exclusion relating to equity in net earnings of:			
Illinois National Bank	—	(2,176)	(2,282)
Wesco	(3,275)	(4,050)	(4,041)
Benefits from unconsolidated subsidiaries	—	(530)	—
Increases, resulting from:			
State income taxes, less Federal income tax benefit	1,413	1,216	821
Berkshire provision, at rate applicable to dividends, with respect to its equity in Blue Chip's operating earnings	859	777	580
Net other differences	(288)	578	(259)
Total income taxes applicable to operating earnings	$12,091	$13,943	$ 9,796

The above Federal income tax expense represents amounts assessed currently, adjusted for changes in amounts previously considered prepaid or deferred as follows:

	1981	1980	1979
Currently assessed applicable to operating income	$13,482	$11,638	$ 9,480
Change in prepaid	(972)	1,147	431
Change in deferred liability arising from operations	(419)	1,158	(115)
	$12,091	$13,943	$ 9,796

(12) Income Taxes (continued)

The change in prepaid income taxes relates to timing differences primarily in reporting Blue Chip's stamp redemption expenses. The change in the deferred liability arising from operations relates to the following:

	1981	1980	1979
Undistributed income of Blue Chip Stamps	$ 808	$ 730	$ 536
Deferred insurance premium acquisition costs	(851)	235	(366)
Other timing differences	(376)	193	(285)
	$ (419)	$ 1,158	$ (115)

Income taxes deemed applicable to realized investment gain are essentially equal to amounts computed at the Federal statutory rate of 28% applicable to long-term capital gains.

(13) Realized Investment Gain — Continuing Operations

A summary of net realized investment gain — continuing operations — for each of the past three years is presented in the following table.

	1981	1980	1979
Pre-tax net gain realized by the Company and consolidated subsidiaries	$34,739	$15,934	$ 9,385
Applicable income taxes	(10,421)	(4,401)	(2,702)
Applicable minority interest	(2,179)	(609)	(196)
	22,139	10,924	6,487
Equity in net realized gain (loss) of Wesco Financial Corporation, an unconsolidated subsidiary	742	(134)	409
Realized investment gain — continuing operations, net	$22,881	$10,790	$ 6,896

The cost of securities sold is usually determined on a first-in, first-out basis; occasionally, when specific identification of securities sold results in lower applicable income tax, identified cost is used.

(14) Lease Commitments

Associated, Blue Chip, and subsidiaries of Blue Chip had significant lease commitments outstanding, the minimum rentals under which were as follows at January 2, 1982:

Year	*Associated*	*Blue Chip*	*Total*
1982	$1,626	$ 3,957	$ 5,583
1983	1,279	3,611	4,890
1984	1,018	3,134	4,152
1985	734	2,498	3,232
1986	555	2,226	2,781
Thereafter	1,753	10,889	12,642

Leases of Berkshire and its consolidated subsidiaries in effect at January 2, 1982 are classified as operating leases; there were no capital lease commitments pertaining to real property; any such commitments with respect to equipment leases entered into are considered immaterial. Total rental expense charged to consolidated net earnings was $9,797 for 1981, $10,145 for 1980, and $9,026 for 1979, including contingent real estate rentals in excess of stated minimum amounting to $3,071 for 1981, $2,726 for 1980, and $2,699 for 1979.

Berkshire Hathaway Inc.

AND CONSOLIDATED SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(Continued)*

January 2, 1982

(dollars in thousands)

(15) Pension Plans

Employees of Berkshire and its consolidated subsidiaries who meet certain eligibility requirements are covered under either employer-sponsored or union-sponsored pension plans. Total pension expense charged to consolidated earnings was $3,118 for 1981, $1,917 for 1980, and $2,454 for 1979, which includes, as to certain of the plans, amortization of prior service costs over a 30-year period. Berkshire and its subsidiaries generally fund pension costs as accrued.

The latest actuarial evaluations of employer-sponsored defined benefit plans of the Company and its consolidated subsidiaries were last performed generally as of December 31, 1980 or 1981. The actuarial present values determined for accumulated benefits, using interest assumptions ranging from 6% to 10%, segregated as between overfunded and underfunded plans, together with assets available for benefits as of that date, are presented in the following table.

	Overfunded plans	*Underfunded plans*
Actuarial present value of accumulated benefits:		
Vested	$ 5,987	$18,639
Not vested	349	1,442
Total	$ 6,336	$20,081
Assets available for benefits	$12,255	$18,903

(16) Litigation

On October 28, 1977 the Buffalo Courier-Express, Inc., a principal competitor of Blue Chip's subsidiary, Buffalo Evening News, Inc., filed an action against such subsidiary in the United States District Court under Federal antitrust laws seeking to enjoin certain practices allegedly engaged in by the News in connection with the proposed initiation of the Sunday edition in place of its Saturday weekend edition and publication of Saturday and holiday editions, thus providing competition for the existing Sunday edition of the Courier-Express. In addition to seeking an injunction, the complaint seeks treble damages in an unspecified amount, attorneys' fees and costs. The News has filed an answer and counterclaim denying all liability and seeking affirmative relief of treble damages in an unspecified amount, injunction, attorneys' fees and costs against the Courier-Express on the ground, among others, that the Courier-Express seeks to monopolize the Sunday newspaper business in the Buffalo metropolitan area in violation of the Federal antitrust laws. The Courier-Express was sold to the Minneapolis Star and Tribune Co. in 1979 and the litigation has been relatively dormant since that time. The company is presently unable to predict what effect, if any, this transaction will have on the lawsuit. If the Courier-Express is successful in obtaining the kinds of permanent injunctions it is seeking, the Company has stated the News probably will be forced to cease operations and liquidate; however, with discovery incomplete, the outcome of the action and the News' potential exposure, if any, is uncertain.

It is the opinion of management of Berkshire that the ultimate outcome of this litigation will not have a materially adverse effect on the consolidated financial position of Berkshire, notwithstanding its potentially severe impact upon the News.

(17) Quarterly Data

Results of operations for the four quarters of 1981 and 1980 appearing on the following page is incorporated in these Financial Statements by this reference.

(18) Business Segment Data

Information as to business segments is shown on page 32 and is incorporated in these Financial Statements by this reference.

Berkshire Hathaway Inc.

QUARTERLY DATA

(dollars in thousands except per share amounts)

This information is unaudited.

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter**
1981				
Income items	$113,388	$115,184	$103,592	$146,532
Earnings before realized investment gain	9,133	10,972	7,801	11,817
Realized investment gain	5,713	12,580	2,407	2,181
Net earnings	$ 14,846	$ 23,552	$ 10,208	$ 13,998
Per share:				
Earnings before realized investment gain	$ 9.26	$ 11.13	$ 7.91	$ 11.98
Net earnings	15.06	23.88	10.35	14.19
1980				
Income items	$116,914	$119,662	$104,788	$150,793
Earnings from continuing operations before realized investment gain	8,966	9,001	6,193	14,324
Equity in earnings — before securities losses — Illinois National Bank*	1,289	1,078	1,055	1,309
Earnings before realized investment gain	10,255	10,079	7,248	15,633
Realized investment gain	7,271	1,110	1,255	271
Net earnings	$ 17,526	$ 11,189	$ 8,503	$ 15,904
Per share:				
Earnings from continuing operations before realized investment gain	$ 8.73	$ 8.76	$ 6.03	$ 13.95
Earnings before realized investment gain	9.98	9.81	7.06	15.22
Net earnings	17.06	10.89	8.28	15.48

*Berkshire divested itself of its interest in the Illinois National Bank on December 31, 1980.

**Candy business revenues and earnings are normally seasonally higher in the fourth quarter, compared to earlier quarters of the year. Additionally, 4th quarter of 1980 earnings include (1) a benefit of approximately $970 (94 cents per share) resulting from revisions to estimation factors applied in computing Blue Chip's liability for unredeemed trading stamps (See note 1(e) to Consolidated Financial Statements), and (2) the Company's equity of approximately $1,293 ($1.26 per share) attributable to sale by Wesco's savings and loan subsidiary of its fifteen branches (See Note (5) to Consolidated Financial Statements).

Berkshire Hathaway Inc.

SUPPLEMENTAL INFORMATION ON THE EFFECTS OF CHANGING PRICES

(dollars in thousands except per share amounts)

This information is unaudited.

The Financial Accounting Standards Board ("FASB") requires disclosure of supplementary data intended to reflect the effects of inflation on portions of the financial statements.

The method of measuring the impact from inflation is in the development stage and conceivably subject to future changes. Therefore, evaluation of the data presented should be made with caution and only with reference to other financial data.

Selected Financial Data As Reported And As Adjusted For General Inflation

This table presents certain prescribed data as reported and then as adjusted to average 1981 constant dollars. The latter is determined by the Consumer Price Index.

	Fiscal Year Ended Saturday nearest December 31.				
	1981	*1980*	*1979*	*1978*	*1977*
Total revenues:					
As reported	$478,696	$492,157	$469,125	$453,359	$369,350
As adjusted	478,696	543,008	587,593	631,779	554,127
Income from continuing operations before realized investment gain:					
Total as reported	$ 39,723	$ 38,484	$ 30,961	$ 25,742	$ 19,922
Total as adjusted	39,723	42,460	38,780	35,873	29,888
Per share as reported	$ 40.27	$ 37.47	$ 30.14	$ 25.02	$ 19.20
Per share as adjusted	40.27	41.34	37.75	34.87	28.81
Stockholders equity:					
As reported	$519,463	$395,214	$344,962	$254,166	$206,738
As adjusted	519,463	436,049	432,075	354,193	310,164
Market price per common share at year end:					
Historical amount	$ 560.00	$ 425.00	$ 320.00	$ 158.00	$ 138.00
As adjusted	560.00	468.91	400.81	220.18	207.04
Average consumer price index (1967 = 100)	272.3	246.8	217.4	195.4	181.5

Gain in Purchasing Power From Holding Net Monetary Items

In general, assets or liabilities which are fixed in terms of the amount of cash held, receivable or payable are "monetary items." At the end of each of the last six years, Berkshire held, on a consolidated basis, net monetary liabilities, i.e., consolidated monetary items which were liabilities exceeded consolidated monetary items which were assets. In an inflationary period, a gain in purchasing power results from holding net monetary liabilities, since this calculation presumes that the net liabilities can be redeemed with dollars of declining value. The calculated purchasing power gain resulting from this calculation, as to Berkshire and its consolidated subsidiaries for each of the past five years — stated in average 1981 dollars — is as follows:

1981	$10,041
1980	12,052
1979	9,062
1978	5,492
1977	3,322

Additional FASB Requirements

Another FASB requirement is for restating at "current cost" inventories, assets used in production and depreciation thereon, and reporting the net effect on reported net income of these restatements. Since these items are not material to Berkshire's operating income or financial position, this information has been omitted.

Berkshire Hathaway Inc.

BUSINESS ACTIVITIES OF THE COMPANY AND ITS SUBSIDIARIES

January 2, 1982

(a) Underwriting of property and casualty insurance. The insurance business is conducted through several wholly-owned subsidiaries referred to throughout this report as the "Insurance Group." Principal insurance subsidiaries are National Indemnity Company and National Fire and Marine Insurance Company, companion carriers sharing a home office in Omaha, Nebraska, and specializing in non-standard automobile and general liability insurance. A reinsurance operation is also conducted through National Indemnity and through Columbia Insurance Company, a Nebraska domiciled insurer. "Home state" multiple line property and casualty insurance operations are conducted through subsidiaries formed for that purpose in Colorado, Kansas, Minnesota, Nebraska and Texas. Workers' compensation coverages are provided by other subsidiaries of the Company, principally: Cypress Insurance Company, Pasadena, California, Redwood Fire and Casualty Insurance Company, Los Angeles, California and Southern Casualty Insurance Company, Alexandria, Louisiana. (Redwood succeeded in 1980 to the business formerly conducted by a branch office of National Indemnity.) Home and Automobile Insurance Company, based in Chicago, is a subsidiary of the Company which underwrites non-standard automobile and general liability insurance.

The insurance business generates significant amounts of investment income, both from capital funds committed to the operations and from policyholders' funds derived from unearned premiums and loss reserves.

(b) Manufacturing and selling of woven textile products. The company owns a weaving mill in New Bedford, Massachusetts, operations of which by the Company or its predecessors dates back to 1889, and maintains sales offices in New York City and Los Angeles; a Canadian subsidiary maintains a textile products sales office and warehouse in Toronto, Canada. In 1980, operations of a subsidiary textile operation in Manchester, New Hampshire, purchased in 1975, were discontinued.

Products of the textile business include curtain and bedspread materials, apparel fabrics and industrial fabrics. Sales are through employees to home fabric jobbers and converters, menswear converters, industrial fabrics and apparel fabrics converters, custom and ready-made curtain manufacturers, bedspread manufacturers, retail chain and department stores and mail order houses.

(c) Retailing of popularly priced women's and children's apparel. The Company's retailing business is conducted through Associated Retail Stores, Inc., ("Associated"). Associated has been a wholly-owned subsidiary of the Company or a now-merged predecessor of the Company, since 1966. Associated's headquarters and central warehouse are in Long Island City, New York; it had 88 retail outlets at January 2, 1982, ranging in size from 2,000 square feet to 60,000 square feet of selling and non-selling floor area, located in eleven states, principally in the midwest (Chicago) and in northeastern states.

(d) Blue Chip Stamps. Blue Chip is an approximately 60% owned subsidiary of the Company. Blue Chip is engaged directly in the promotional services business, and wholly-owned subsidiaries of Blue Chip are engaged in the candy business — See's Candy Shops, Incorporated, and the newspaper business — Buffalo Evening News, Inc.

(i) The promotional services business. Blue Chip offers two principal types of promotional services: (1) those used by business organizations to attract or retain customers (mainly a conventional trading stamp program), and (2) those used by businesses or other entities for internal purposes (motivation programs).

Blue Chip's trading stamp service, started in 1956, continues to be the pre-eminent trading stamp operation in the California-Nevada area. Revenues of the trading stamp service component declined dramatically in the early 1970's after peaking at $124 million in the fiscal year ended February 28, 1970, but have been relatively stable over the past several years. Such revenues were $15.6 million in 1981 compared to $16.7 million in 1980 and $15.9 million in 1979. However, such revenues are expected to drop materially in 1982. One Southern California supermarket chain which accounted for about 51% of the 1981 trading stamp service revenues has told Blue Chip that it will discontinue giving trading stamps effective April 1, 1982. Blue Chip intends to stay in the trading stamp business; its management believes trading stamps are an effective point-of-purchase sales promotion device for certain retailers. Blue Chip currently has 37 redemption outlets, compared to 41 one year ago and a peak number of 90.

Blue Chip Motivation, a separate division, tailors programs for businesses using awards of merchandise and travel in order to stimulate sales or productivity, promote attendance or safety, or perform other employee motivational functions. The division concentrates its sales efforts generally in Western United States. Motivation programs vary greatly as to size and duration with the result that revenues of this division fluctuate from year to year.

Berkshire Hathaway Inc.

BUSINESS ACTIVITIES OF THE COMPANY AND ITS SUBSIDIARIES *(Continued)*

(ii) See's Candy Shops, Incorporated. Blue Chip purchased See's in 1972. See's produced boxed chocolates and other confectionary products of high quality in two large kitchen facilities in California. See's is believed to be one of the largest candy manufacturers distributing through its own chain of retail shops: it now has 199 in twelve western and midwestern states including Hawaii.

A significant degree of seasonality exists in this business: about 50% of each year's candy sales is generated during the Thanksgiving-Christmas season, when high shop volume is augmented by quantity sales to organizations at reduced prices.

(iii) Buffalo Evening News, Inc. The assets of this entity, subject to certain liabilities, were purchased by Blue Chip in 1977. It publishes a daily newspaper in Buffalo, New York. Advertising revenues of the News, representing most of its revenues, peak during the fourth quarter of the year due to holiday advertising. The News is involved in litigation proceedings. See Note (16) to the accompanying Consolidated Financial Statements.

In addition to the above businesses, the Company has approximately 48% economic interest in **Wesco Financial Corporation**, through Blue Chip's ownership of approximately 80% of the outstanding stock of Wesco. In the Company's Consolidated Financial Statements included in this report, the equity method of accounting is reflected for Blue Chip's investment in Wesco. Wesco invests in marketable securities and real estate, and owns all of the outstanding stock of Mutual Savings and Loan Association, Pasadena, California ("Mutual"). Wesco also owns 100% of Precision Steel Warehouse, Inc. ("Precision"). Further discussion of the business of Mutual and Precision is included at pages 40 to 41 of this report.

Berkshire Hathaway Inc.

BUSINESS SEGMENT DATA

(dollars in thousands)

Revenues	1981	1980	1979
Insurance	$ 198,032	$ 216,298	$206,356
Textiles	30,389	44,432	49,862
Retailing	44,239	44,374	42,709
Candy	113,724	98,600	88,189
Promotional services	23,842	25,637	23,628
Newspaper	54,829	49,977	46,414
Revenues not identified with major segments	13,641	12,839	11,967
	$ 478,696	$ 492,157	$469,125

Capital Expenditures	1981	1980	1979
Insurance	$ 645	$ 653	$ 1,133
Textiles	859	1,019	1,116
Retailing	398	199	279
Candy	3,526	5,116	3,250
Promotional services	569	338	355
Newspaper	335	346	642
Other	3	45	18
	$ 6,337	$ 7,716	$ 6,793

Identifiable Assets at Year-End	1981	1980	1979
Identified with segments:			
Insurance	$ 825,635	$ 693,859	$585,103
Textiles	15,521	19,388	25,139
Retailing	12,830	13,295	14,520
Candy	63,595	53,178	47,923
Promotional services	105,409	94,761	93,646
Newspaper	34,852	34,215	35,653
Other	2,270	2,215	2,246
	1,060,112	910,911	804,240
Not identified with segments:			
Investment in Illinois National Bank	—	—	28,785
Investment in Wesco	68,874	63,040	56,750
Investment in unconsolidated subsidiaries	896	1,187	1,377
Corporate cash and marketable securities	28,029	35,443	1,113
	$1,157,911	$1,010,581	$892,265

Operating Profit Before Taxes — Continuing Operations	1981	1980	1979
Insurance	$ 40,301	$ 37,677	$ 27,966
Textiles	(2,669)	(508)	1,723
Retailing	1,763	2,440	2,775
Candy	21,447	15,031	12,785
Promotional services	3,642	7,699	2,397
Newspaper	(1,086)	(2,805)	(4,617)
Pre-tax operating profits not identified with major segments	11,259	10,618	9,987
Corporate expenses	(2,913)	(893)	(647)
Interest expense	(11,487)	(9,185)	(5,729)
	$ 60,257	$ 60,074	$ 46,640

Amounts are stated before deduction of minority interest. Realized investment gains are not reflected.

Depreciation and Amortization of Tangible Assets	1981	1980	1979
Insurance	$ 644	$ 535	$ 459
Textiles	556	500	486
Retailing	203	164	151
Candy	1,804	1,486	1,199
Promotional services	231	174	146
Newspaper	2,263	2,230	2,159
Other	52	55	51
	$ 5,753	$ 5,144	$ 4,651

Revenues of the Insurance Segment	1981	1980	1979
Premiums written	$ 148,000	$ 184,864	$186,185
Premiums earned:			
Specialized auto and general liability	73,177	88,404	90,646
Workers' Compensation*	18,193	19,890	19,350
Reinsurance	29,446	33,804	30,864
Home State multiple lines	38,197	43,089	41,089
Total premiums earned	159,013	185,187	181,949
Investment income	39,019	31,111	24,407
	$ 198,032	$ 216,298	$206,356

*Workers' Compensation coverage written by the Home States Companies, as part of their multiple line business, is not disaggregated from their total earned premiums.

Insurance Segment Operating Profit Before Taxes	1981	1980	1979
Underwriting gain (loss):			
Specialized auto and general liability	$ 3,020	$ 7,395	$ 7,845
Workers' Compensation	2,822	4,870	5,130
Reinsurance	(3,720)	(233)	(4,338)
Home State multiple lines	(644)	(5,294)	(4,895)
Total underwriting gain	1,478	6,738	3,742
Net investment income	38,823	30,939	24,224
	$ 40,301	$ 37,677	$ 27,966

Berkshire Hathaway Inc.

PARENT COMPANY ONLY — CONDENSED FINANCIAL STATEMENTS

(dollars in thousands)

Balance Sheets

	Jan. 2, 1982	Jan. 3, 1981
Assets:		
Investment in wholly-owned subsidiaries (includes unrealized appreciation of marketable equity securities held by insurance subsidiaries)	$477,300	$389,013
Investment in Blue Chip Stamps	103,827	56,050
Cash and invested cash	2,558	13,917
Investment in marketable equity securities at cost	25,471	21,526
Accounts receivable and inventories of parent company's textile business	9,917	13,196
Other assets	4,579	4,042
	$623,652	$497,744
Liabilities and stockholders' equity:		
Accounts payable and accrued expenses	$ 6,044	$ 7,553
Term debt payable	92,889	94,349
Current and deferred income taxes	5,257	628
	104,190	102,530
Stockholders' equity (See Consolidated Balance Sheet)	519,462	395,214
	$623,652	$497,744

Statements of Earnings

	1981	1980	1979
Income:			
From subsidiaries:			
Interest	$ 474	$ 695	$ 703
Dividends — Cash	539	5,146	7,692
Dividends — Property*	33,325	21,955	—
Undistributed earnings	41,290	32,071	36,267
	75,628	59,867	44,662
Interest and dividends — other investments	2,677	1,083	70
Gross profit (loss) from textile product sales	(253)	3,157	4,838
Other income (loss)	565	(807)	37
	78,617	63,300	49,607
Costs and expenses:			
Administrative and selling expenses of textile business	2,689	3,194	2,944
Corpor[illegible] administration**	2,579	893	647
Interest expense	10,745	6,078	3,172
Income taxes	—	13	27
	16,013	10,178	6,790
Net earnings	$62,604	$53,122	$42,817

* *Dividends received in property were in the form of shares of Blue Chip Stamps stock.*

** *Corporate administration costs in 1981 reflect contributions pursuant to shareholder designated contributions program.*

Wesco Financial Corporation

Wesco Financial Corporation is an approximately 80% owned subsidiary of Blue Chip Stamps; Blue Chip Stamps is approximately 60% owned by Berkshire. Berkshire's economic interest in Wesco, therefor, is about 48%

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(dollars in thousands)

Balance Sheets

	December 31, 1981	December 31, 1980
Assets:		
Financial:		
Cash and temporary cash investments	$ 28,100	$ 54,972
Investments, at cost	123,755	105,875
Loans receivable	149,656	164,648
Other assets	14,137	16,843
	315,648	342,338
Steel service:		
Cash and temporary cash investments	3,328	1,695
Accounts receivable and inventories	11,788	11,151
Property, plant and equipment, net	6,112	6,175
Other assets	158	166
	21,386	19,187
	$337,034	$361,525
Liabilities and stockholders' equity:		
Financial liabilities:		
Savings deposit	$149,168	$168,366
Notes payable	68,424	73,719
Other liabilities, including income taxes	5,810	12,048
	223,402	254,133
Steel service liabilities:		
Note payable	2,138	2,188
Other liabilities, including income taxes	2,033	2,247
	4,171	4,435
Total liabilities	227,573	258,568
Stockholders' equity	109,461	102,957
	$337,034	$361,525

Statements of Earnings

	1981	1980	1979
Financial revenues:			
Interest on loans, loan fees and service charges	$12,357	$45,244	$45,190
Interest and dividends from investments	16,966	15,200	14,056
Gain on sales of branches	—	5,873	—
Other	1,098	797	2,798
	30,421	67,114	62,044
Financial expenses:			
Interest on savings deposits	15,970	41,283	37,028
Interest on notes payable	6,778	7,180	7,106
General and administrative	3,901	6,586	6,136
Income taxes	(2,391)	3,354	2,414
	24,258	58,403	52,684
Net income from financial operations	6,163	8,711	9,360
Steel service:			
Revenues	46,986	41,074	37,883
Costs and expense, including income taxes	45,039	39,570	36,176
Net income from steel service operations	1,947	1,504	1,707
Net income before securites gains	8,110	10,215	11,067
Realized securities gains (losses)	1,669	(170)	73
Net income	$ 9,779	$10,045	$11,140

Berkshire Hathaway Inc.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Results of Operations

This discussion should be read in conjunction with the Selected Financial Data, the Business Segment Data and with the Consolidated Financial Statements and notes thereto appearing elsewhere in this report. Operating profit before taxes is shown in the Business Segment Data. The impact of income taxes is not proportional to the pre-tax income of the Company's business segments because of the tax-free nature of municipal bond interest income and the virtually tax-free nature of dividend income earned by certain segments. Also, the minority interest in Blue Chip's segments is significant. Therefore, presented below is a summary of net earnings — after giving effect to income taxes and after deduction of the applicable minority interest — for the past three years.

	Berkshire's Net Earnings After Taxes (000s omitted)		
	1981	1980	1979
Insurance:			
Underwriting gain	$ 798	$ 3,637	$ 2,214
Net investment income	32,401	607	20,106
Sub-total — Insurance	33,199	[illegible],244	22,320
Equity in operating earnings[1] of:			
Blue Chip Stamps and its wholly-owned subsidiaries	7,884	6,456	3,739
Wesco Financial Corporation[2]	3,95[illegible]	4,885	4,793
Textiles and retailing	(734)	1,371	2,128
	44,299	41,956	32,980
Net unallocated costs — principally interest[3]	(4,576)	(3,472)	(2,019)
Earnings from continuing operations before realized investment gain	39,723	38,484	30,961
Equity in earnings (before securities losses in 1980) of Illinois National Bank	—	4,731	4,960
Earnings before realized investment gain	39,723	43,215	35,921
Realized investment gain, net[4]	22,881	9,907	6,896
Net earnings	$62,604	$53,122	$42,817

[1] "Operating earnings" of Blue Chip has been computed before deduction of its interest expense, net of tax effect. Any significant realized gain or loss from sale of securities by Blue Chip and Wesco is excluded from the computation of "operating earnings" of these subsidiaries.

[2] "Operating earnings" of Wesco for 1980 include gain from sale of Mutual Savings and Loan Association's fifteen branches. Berkshire's share of such gain included in the above table was $1,293,000 in 1980.

[3] Net unallocated costs include Berkshire's proportionate share of Blue Chip's interest expense, net of tax effect.

[4] Realized investment gain includes Berkshire's proportionate share of any significant net securities gains or losses of Blue Chip, Wesco and the Illinois National Bank.

Income taxes have been assigned in the above tabulation to the income or deduction items which created the tax or generated the benefit; amounts so assigned may differ from amounts allocated to the various legal entities in accordance with tax sharing agreements effective as between the entities.

Berkshire Hathaway Inc.

MANAGEMENT'S DISCUSSION *(Continued)*

Insurance

Premium volume of the Insurance Group declined significantly in 1981. The underwriting gain also declined. A summary of underwriting results of the Insurance Group for the past three years is as follows:

	(Dollars in thousands)					
	1981		1980		1979	
	Amount	%	*Amount*	%	*Amount*	%
Premiums written	$148,000	XX	$184,864	XX	$186,185	XX
Premiums earned	159,013	100.0	185,187	100.0	181,949	100.0
Losses and loss expenses	103,417	65.1	118,230	63.9	120,337	66.1
Underwriting expenses	54,118	34.0	60,219	32.5	57,870	31.8
	157,535	99.1	178,449	96.4	178,207	97.9
Underwriting gain (pre-tax)	$ 1,478	0.9	$ 6,738	3.6	$ 3,742	2.1

A major portion of the total business of our Insurance Group is represented by the traditional specialized automobile and general liability lines underwritten through National Indemnity Company and National Fire and Marine Insurance Company. The volume of this business is subject to significant fluctuation: when industry price competition is fairly intense (as it was in 1981), the number of "specialty" risks offered at acceptable prices to our companies declines significantly. About 55% of the Insurance Groups 1981 decline in premiums earned was recorded in this price-sensitive business. Reinsurance premiums earned also declined; this was, similarly, the result of competitors willing to write business at rates lower than we were willing to match. Decline in Homestate premium volume reflects principally the discontinuance in late 1980 of our Iowa corporation.

While underwriting profits of the specialized businesses declined, these operations remained profitable. Workers'compensation underwriting gains declined; some favorable loss reserve developments are reflected in 1981 results for this business, but in lesser amounts than in the prior two years.

The statutory combined ratio for our Insurance Group was 100.3% for 1981, compared to 96.6% for 1980 and 97.1% for 1979. That ratio is the sum of the ratio of losses and loss adjustment expenses to premiums earned plus the ratio of statutory underwriting expenses incurred to premiums written. Both premium figures are reduced, in our calculation, for dividends to policyholders. In the property/casualty industry, this ratio is an indicator, where a ratio of 100% indicates break-even (i.e., costs and expenses are equal to the related premiums), higher than 100% indicates an underwriting loss, and less than 100% indicates an underwriting gain. The computation of the statutory combined ratio takes into account written premiums without regard to when those premiums may be earned. Generally accepted accounting principles as applied to premium acquisition costs (underwriting expenses) do not provide deferral of such of those costs as are deemed "period costs," i.e., those deemed as continuing without regard to volume; statutory accounting practice results in no deferral of premium acquisition costs. A common result for periods in which there is a sizeable difference between premiums written and premiums earned may be reflection of an underwriting gain for a period for which the combined ratio was slightly over 100% (such as occurred with respect to our Group for 1981), or, conversely, reflection of an underwriting loss for a period for which the combined ratio was slightly less than 100%.

Investment income of the Insurance Group increased fairly significantly in both 1980 and 1981, each as compared to the preceding year. The increases reflect both (1) an increased yield earned on total average investments (with the yield measured on cost), and (2) an increased total of investments; in each year, a greater portion of the increase in investment income was derived from the increased level of investments than was derived from increased yield. Berkshire contributed $28,750,000 additional equity capital to the Insurance Group in 1980; the funds contributed represented part of the proceeds of its public debt offering in August, 1980; additional funds for investment by the Insurance Group have been generated by their operations.

Berkshire Hathaway Inc.

Blue Chip and its Wholly-Owned Subsidiaries

Amounts contributed to Berkshire's earnings in each of the past three years by each of Blue Chip's three constituent businesses are shown in the table below. The figures are before deduction of interest expense, do not reflect any realized securities gains, and are net of applicable or deemed applicable income taxes.

	(000s omitted)		
	1981	1980	1979
See's Candies	$6,042	$4,212	$3,448
Promotional services	2,134	3,060	1,624
Buffalo Evening News	(292)	(816)	(1,333)
	$7,884	$6,456	$3,739

See's profits in 1981 rose sharply to an all-time record. Revenues were up about 15% from 1980, with respect to substantially unchanged unit volume, while ingredient costs increased only moderately. The Company's management considers See's earning performance in 1981 to be phenomenal. In 1980, See's earnings increased about 20% over 1979; the dollar volume of candy revenues in 1980 exceeded those of 1979 by approximately 12% due almost completely to price increases, and 1980 cost increases from 1979 were a lesser percentage increase.

The contribution to Berkshire's earnings in 1980 (the prior year) by the promotional services segment of Blue Chip includes approximately $970,000 from revisions to its estimated liability for redemption of its trading stamps. Revisions of the estimation factors used to determine that liability are required periodically, with the last prior revisions occurring in 1976. The contribution to Berkshire's earnings in 1981 from Blue Chip's promotional services business was substantially unchanged from 1980 except for the benefit to the prior year of those revisions. The 1980 profit contribution, other than that reflecting the revisions, was slightly higher than in 1979 principally as the result of higher investment earnings in 1980 than in 1979.

The Buffalo Evening News has recorded an operating loss in each of the past three years, steadily reduced in amount from year-to-year. The steady reduction in the loss reflects a combination of aggressive price increases, intense efforts at general cost containment, and reduction or elimination of expenses or losses in specific areas including litigation expenses and labor contract provision "buy-out" expenses, the latter incurred in order to allow the News to benefit from equipment modernization.

Wesco Financial Corporation

As shown in the table presented at the beginning of this discussion of results of operations, the Company's equity in earnings of Wesco Financial Corporation, 80% owned by Blue Chip, declined in 1981 after remaining approximately the same in 1980 as it was in 1979. However, the 1980 figure of $4,885,000 includes our equity of $1,293,000 in a gain recorded by Wesco's savings and loan subsidiary from sale of its branches, so that Berkshire's 1981 equity in Wesco's earnings, amounting to $3,950,000, should more appropriately be compared to a 1980 figure of $3,592,000 from sources other than the sale of branches, and to a figure of $4,793,000 for 1979. The profits of Mutual Savings, the principal Wesco operation, are under pressure from both high interest rates — reducing its net interest margin — and from competitive pressures created by removal, in part, of the distinctions between banks and savings and loan associations.

Textiles and Retailing

A significant operating loss — $2,669,000 before credit for tax benefit — was recorded from our textile business in 1981. Competitive pressures were severe, and operations were significantly curtailed to avoid building of inventories. The shut-down of the Manchester, New Hampshire operation in late 1980 appears to have precluded the 1981 loss from being even greater. Retailing profits were also under pressure in 1981, resulting in some decline from 1980 in pre-tax profits of Associated Retail Stores. In 1981, Associated increased the number of stores it operates, enabling its revenues to remain at nearly the same level as in 1980, but its total costs increased.

Berkshire Hathaway Inc.

MANAGEMENT'S DISCUSSION *(Continued)*

Net Unallocated Costs

Interest expense increased in 1981 from 1980, and increased in 1980 from 1979 as a result of Berkshire's issuance in August, 1980 of its $60 million 12¾% debentures due 2005. The debt was outstanding for all of 1981, but only during the last five months of 1980.

Liquidity and Capital Resources

Berkshire's consolidated balance sheet at January 2, 1982 reflects continuing significant liquidity. In management's opinion, the fiduciary nature of obligations to policyholders of Berkshire's insurance subsidiaries and to savers of Blue Chip's trading stamps requires maintenance of high liquidity, and management expects to meet this requirement with a significant margin of safety. Maintenance of liquidity considerably above industry norms in Berkshire's insurance subsidiaries allows those operations to perform their underwriting function with a sole view towards underwriting profitability; they are not forced to accept premiums to maintain positive cash flow.

Berkshire's businesses are not capital-intensive; i.e., they do not require significant investment or reinvestment in property, plant and equipment. Generally, management tends to avoid deployment of assets in businesses of such a nature; on the contrary, Berkshire desires to own companies engaged in businesses that produce positive cash flow.

Berkshire's total equity capital has more than doubled over the past three years, from approximately $254 million at the end of 1978 to $519 million at the end of 1981, the net increase amounting to $265 million. Realized and unrealized securities gains during the three years represent approximately $175 million of the increase. Debt is used by Berkshire in relatively modest amounts, and management does not expect the Company to rely upon a high degree of leverage in its financing at any time in the foreseeable future. Management is averse to reliance on any significant amount of short-term debt. In August, 1980, Berkshire issued, in a public offering, $60 million 12¾% debentures, the principal amount of which is repayable through operation of a sinking fund in the years 1991 through 2005. No significant debt financing occurred in 1981. In March, 1982, the Company obtained a $50 million revolving loan committment from the First National Bank of Boston. Berkshire did not undertake the 1980 debenture financing nor obtain the 1982 revolving loan committment because of any specific needs, but rather to have the funds in place when attractive opportunities arise to profitably use the funds. Management believes that such opportunities may present themselves when credit is extremely expensive or even unavailable.

The Parent company is largely dependent upon dividends received from its subsidiaries to provide its own cash requirements including debt service requirements. Dividend payments by insurance subsidiaries are subject to regulatory restrictions; the possibility that such restrictions may significantly restrict dividend payments to the Parent is provided for (1) by retaining direct ownership by the Parent of five of its insurance subsidiaries (so that a limitation as to one company would not be a limitation as to all), (2) by direct ownership by the Parent of shares of Blue Chip Stamps, and (3) by retention of significant liquid assets at the Parent company level.

Inflation

Berkshire's management does not believe that, to date, inflation has seriously affected Berkshire's businesses. Generally, Berkshire receives current revenues in any year which have substantially the same purchasing power as the dollars which represent its current costs. Very few of Berkshire's costs are stated in dollars which are other than current dollars.

Very large changes in the rate of inflation that were not anticipated could seriously impact Berkshire's insurance businesses, particularly since premium rates are established well in advance of incurrence of the related costs. Management believes that to date, however, underwriting results have not been impacted materially by inflation or changes in inflation rates.

The 1981 Annual Report of Blue Chip Stamps included the following letter to Blue Chip stockholders from the Chairman and the President of that Company.

To Our Shareholders

Consolidated operating income (i.e., before all net gains from sales of securities, mortgages and important fixed assets) for the calendar year 1981 increased to $20,895,000 ($4.03 per share) from $16,564,000 ($3.20 per share) in the previous year.

Consolidated net income (i.e., after net gains from sale of securities, mortgages and important fixed assets) increased to $27,626,000 ($5.33 per share) from $20,389,000 ($3.94 per share) in the previous year.

We have four major subsidiaries, See's Candy Shops, Incorporated (100%-owned), Mutual Savings (80%-owned), Precision Steel (80%-owned), and Buffalo Evening News, Inc. (100%-owned), in addition to the basic business (primarily trading stamps) operated by the parent company. Our consolidated income for our two reporting years just ended breaks down as follows (in 000s except for per-share amounts):

	Blue Chip's equity in						
	Net operating income (loss) of						
Year ended about	See's*1	Mutual Savings*2	Steel Business	Buffalo Evening News*3	All other net operating income*4	Net gains on sales of securities, mortgages and important fixed assets*5	Blue Chip consolidated net income
December 31, 1981	$10,647	$3,393	$1,560	$ (531)	$5,826	$6,731	$27,626
Per Blue Chip share	2.06	.65	.30	(.10)	1.12	1.30	5.33
December 31, 1980	7,270	4,181	1,205	(1,472)	5,380	3,825	20,389
Per Blue Chip share	1.40	.81	.23	(.28)	1.04	.74	3.94

*1 After reducing income by amortization of intangibles arising from purchase of See's at a large premium over its book value

*2 After increasing income by amortization of the discount from Mutual Savings' book value at which the interest was acquired and eliminating gains and losses from sale by Mutual Savings of securities, mortgages and important fixed assets

*3 After reducing income by amortization of relatively minor intangibles arising at acquisition of the newspaper

*4 After deduction of interest and other corporate expenses. In each yea[illegible] there was an operating loss from promotional services activities before residual consolidated net income was credited with (i) dividends and interest resulting primarily from investment of the funds available through "float" caused by trading stamps issued bu[illegible] not yet redeemed, plus (ii) income tax benefit caused by 85% exclusion of dividends in computing federal income taxes, plus (iii) Blue Chip's share of dividends, interest and rent from securities and real estate held by the Wesco Financial Corporation group outside its savings and loan and steel service activities, plus (iv) in 1980 a net adjustment of Blue Chip's stamp liability account in the amount of $1,747 or $.34 per Blue Chip share, net of taxes, as explained below under "Promotional Services Business and Miscellaneous Sources of Operating Income."

*5 The 1980 figures comprise $2,332 or $.45 per Blue Chip share attributable to Mutual Savings' sale of 15 branch offices, as explained below under "Mutual Savings and Loan Association," and $1,493 or $.29 per Blue Chip share of net securities gains realized by the various entities including Mutual Savings, net of taxes and minority interest. The 1981 figures relate solely to such net securities gains.

The foregoing breakdown (of the same aggregate earnings) differs somewhat from that used in our audited financial statements.

We take the pains to prepare our unconventional breakdown of earnings and to furnish it in this letter because we believe it better explains what is really happening than does our accompanying consolidated income statement in conventional form. Generally, we are trying to improve our annual letter to shareholders each year so as better to disclose the things we would want to be told if the roles were reversed and we were passive investors. However, we make no effort to provide fresh or novel descriptions. Repetition seems appropriate to us where facts remain both true and analytically important over many years and where certain ideas are part of our fixed business catechism. Accordingly, where previously used words, sentences or paragraphs appear adequate we simply repeat them, inserting up-to-date numbers.

SEE'S CANDY SHOPS, INCORPORATED

The earnings of our 100%-owned subsidiary, See's Candy Shops, Incorporated, increased 43.7% last year, a phenomenal performance considering the general state of retailing in the current recession. We have now owned See's for exactly ten years. Comparative figures for See's for the entire ten-year period of our ownership are set forth below:

Reproduced from 1981 Annual Report of Blue Chip Stamps.

Year ended about	Sales	Profits after taxes*	Number of pounds of candy sold	Number of stores open at year end
December 31, 1981	$112,578,000	$11,130,000	24,052,000	199
December 31, 1980	97,715,000	7,747,000	24,065,000	191
December 31, 1979	87,314,000	6,473,000	23,985,000	188
December 31, 1978	73,653,000	6,289,000	22,407,000	182
December 31, 1977	62,886,000	6,262,000	20,921,000	179
December 31, 1976	56,333,000	5,618,000	20,553,000	173
December 31, 1975	50,492,000	5,308,000	19,134,000	172
December 31, 1974	41,248,000	3,229,000	17,883,000	170
December 31, 1973	35,050,000	2,069,000	17,813,000	169
December 31, 1972	31,337,000	2,?32,000	16,954,000	167

*These earnings figures are a little higher than Blue Chip Stamps' share of See's earnings shown in the table on page 1 because Blue Chip's share reflects (i) amortization of intangibles ar[illegible] from purchase of See's stock at a large premium over book value and (ii) state income taxes on See's dividends received by Blue C[illegible].

See's aggregate sales in pounds held up well last year, being essentially unchanged from the previous year even though prices were increased at a rate which turned out to be somewhat higher than the inflation rate. Shop sales increased, but only because of the impact of additional stores. Shops operating throughout both years registered an aggregate decrease in poundage of 1.6%. Christmas season quantity order sales to businesses declined for the first time since the 1974 recession. Ingredient costs in 1981 increased only moderately and, with revenues up about 15%, See's profits rose sharply to an all-time record.

See's is by far the finest business we have ever purchased, exceeding our expectations, which were quite conservative. Our record as foretellers of the future is often poor, even with respect to businesses we have owned for many years, and we so greatly underestimated See's future that we were lucky to acquire it at all.

However, we have at least had the good sense all these last ten years to want See's chief executive, Chuck Huggins, who has spent his working life in its business, to run the company in his and its traditional way. Chuck Huggins is a splendid man and a splendid manager. It is no minor privilege to be associated with him and the kind of quality enterprise he and his predecessors and co-workers have created.

Boxed chocolate consumption per capita in the United States continues to be essentially static, and the candy-store business remains subject to extraordinary cost pressures, offset to some extent in 1981 by subnormal increases in ingredient costs. When See's increases prices each year to reflect cost pressures, it never knows whether consumer resistance will cause net profits to fall instead of rise. Thus far, consumers have been willing to keep buying in the amounts required to keep See's profits rising irregularly at an average rate which, aided by large recent gains, has turned out to be quite satisfactory. This state [illegible]fairs logically cannot continue forever if, on average, See's costs keep increasing faster than the general rate of inflation. Moreover, in some future years commodity and ingredient prices will rise sharply and unexpectedly, causing unanticipated decreases in profits.

Perhaps because price increases deter purchases for personal consumption more than purchases for gifts, See's seasonal sales peak becomes more extreme each year, causing many operating problems and a growing concentration of See's net income in the single month of December.

See's success to date becomes even more remarkable when its industry background is examined in more detail. So far as we know the candy-store business continues to be terrible to mediocre for all other companies, which tend to suffer from a combination of (1) low sales per square foot of retailing space plus (2) the great seasonality of the business which requires staffing and maintenance of stores at minimum levels grossly unjustified by sales during about 90% of each year.

We believe that See's exceptional profits occur, despite all the problems, mainly because both new and old customers prefer the taste and texture of See's candy, as well as the extremely high level of retailing service which characterizes its distribution. This customer enthusiasm is caused by a virtually fanatic insistence on expensive natural candy ingredients plus expensive manufacturing and distributing methods that ensure rigorous quality control and cheerful retail service. These qualities are rewarded by extraordinary sales per square foot in the stores, frequently two to three times those of competitors, and by a strong preference by gift recipients for See's chocolates, even when measured against much more expensive brands.

At the end of 1981, the portion of Blue Chip's consolidated net worth represented by its interest in See's amounted to $38.3 million and included liquid assets adequate to finance See's substantial annual build-up of pre-Christmas inventories. Obviously, based on See's 1981 earnings of $11.1 million, this investment in See's is worth considerably more than its carrying value in Blue Chip's consolidated balance sheet.

Reproduced from 1981 Annual Report of Blue Chip Stamps.

Last year we made "a guarded forecast that See's earnings would increase at least moderately in 1981." In 1982 See's will try again to increase earnings and a modest increase is quite conceivable.

MUTUAL SAVINGS AND LOAN ASSOCIATION

Our equity in Mutual Savings' operating income declined sharply in 1981 to $3,393,000 from $4,181,000 in the previous year.

Earning these reduced profits was an achievement of some note, because in 1981 almost all other savings and loan associations suffered large operating losses and some failed and were absorbed by stronger companies under pressure from governmental regulatory authorities. The financial pressure has continued into 1982. The troubles are caused by a borrowed-short, lent-long position, combined with high current interest rates associated with past and anticipated inflation and removal of much former regulation limiting rate competition for savings accounts. Associations have been forced to pay interest rates to hold savings accounts which are higher than can be covered by locked-in yields from long-term, fixed-rate mortgages acquired years ago in what now seems like a different world.

The sorry state of the savings and loan industry is one more example of the operation of Garrett Hardin's principle for soft sciences (like business, politics, economics and law) that bad ideas are born good. A well-intentioned idea of some kind works fine for a while, then stops working and goes into reverse, as did the basic savings and loan idea of borrowing short and lending long to an extreme degree while depending on governmental regulation to force savers to take an inadequate return in an inflationary period. If, as seems likely, Hardin's principle is part of an inevitable human legacy, tragedy can be averted, partially, only by reversing course when the danger flags start flying as the cherished ideas of the past are faithfully followed. Unfortunately, another perverse phenomenon interferes here — the tendency of the mind to reject the message from a danger signal which is inconsistent with a cherished idea.

At Mutual Savings we were too blind for too long, exactly as Hardin would have predicted, but like the rest of the savings and loan industry we started coping better with reality when it stopped waving the danger flags at us and started using them to poke us in the head and stomach.

The eventual result of our efforts to cope with reality has been that Mutual Savings has continued to make modest profits despite having a substantial borrowed-short, lent-long position, including a fixed-rate mortgage portfolio bearing what is probably the very lowest average interest rate among all U.S. associations (7.6% per annum at the end of 1981). The 1981 profits occurred, notwithstanding this handicap, because Mutual Savings has had:

(1) so far as we know, a higher ratio of shareholders' equity to total interest-bearing liabilities than any other mature U.S. association;
(2) a higher-than-normal proportion of assets in short-term, interest-bearing cash equivalents; and
(3) a far-higher-than-normal proportion of assets in intermediate-term, tax-exempt bonds and utility preferred stocks producing a tax-equivalent yield of about double that prevailing on the mortgage portfolio of the typical association.

Mutual Savings' balance sheet at the end of 1981 is set forth in summary form in Note 1 to our accompanying financial statements.

Mutual Savings' unusual asset-liability structure was caused in part by the sale in 1980 of all its branch offices, one incident of which was retention of only the lowest-yielding mortgages, albeit those with the shortest remaining terms. In selling all branch offices in 1980 the institution shortened sail to allow for hurricane conditions, not because a hurricane was clearly foreseen, but because of the effect that being poked with danger flags had on our generally cautious nature. A hurricane came in 1981, the end of which is yet to be seen. There is, of course, a price to be paid when caution purchases safety. If interest rates decline sharply and more or less permanently, Mutual Savings will have greatly penalized future earnings through sale of its branch offices.

Moreover, what Mutual Savings has left is no jewel of a business. As it keeps its books it had $48.5 million in shareholders' equity at the end of 1980, on which its operating income was only $3.5 million in 1981, or at the inadequate rate of 7.2% per annum. However, as Blue Chip reports earnings from its equity in this less-than-mediocre business, the results are somewhat better because Blue Chip's equity was originally purchased at a large discount from its book value on the books of Mutual Savings. At the end of 1980 Blue Chip's equity in Mutual Savings was carried in Blue Chip's consolidated balance sheet, net of minority interest, at $19.4 million, and this equity contributed $3.4 million to Blue Chip's consolidated earnings in 1981, or at the rate of 17.5% per annum, including $.6 million of amortization into income, at the rate of 1/40th per year, of the discount from book value at which the equity originally was purchased.

Reproduced from 1981 Annual Report of Blue Chip Stamps.

Some additional perspective on the current situation may be obtained by examining the following table:

Calendar year	Blue Chip's average equity in Mutual Savings as carried in Blue Chip's consolidated balance sheet	Blue Chip's share of the cash dividend paid by Mutual Savings during the year	Annual percentage return on Blue Chip's equity from the Mutual Savings dividend
1975	$11,975,000	$1,932,000	16.1%
1976	20,570,000	3,226,000	15.7
1977	23,928,000	3,845,000	16.1
1978	25,285,000	5,287,000	20.9
1979	25,630,000	6,728,000	26.3
1980	22,381,000	9,852,000	44.0
1981	18,778,000	1,922,000	10.2

In 1982 for sure, and perhaps in 1983, Mutual Savings will realize reportable, tax-deductible losses by making sales and reinvestments involving mortgages which will have the effects of bringing the market value of its assets closer to their book value and causing recognition for accounting and income-tax purposes of a portion of the real economic deterioration already in place, caused by interest rates at current levels. Such sales and reinvestments will almost surely cause suspension of dividends from Mutual Savings to its parent corporation, Wesco, in 1982, ending for at least a year or two the important cash flow shown in the immediately preceding table. However, the income and cash-flow effects of a portfolio restructuring at Mutual Savings, after partially offsetting favorable income-tax effects, could quite conceivably increase in a very material way the dividends Mutual Savings will be able to pay at a later time, perhaps as early as 1984. All restructuring decisions will be made with a view to long-term benefit, ignoring considerations of image.

But, no matter what is done, it looks to us as if operating a savings and loan association in the future is going to present a challenge which, so far, we haven't fully figured out how to meet. We do have a lot of options, including expansion by acquisition, with or without additional investment in Mutual Savings, and we are trying to keep all options open as we ride out the storm.

We do not have any intention to sell Mutual Savings. We hope that it will ultimately find a way to earn higher profits, sufficient at least to permit payment of dividends causing realization of a satisfactory rate of return on the carrying value of Blue Chip's equity.

No savings and loan executive has had an easy time in the last few years. Louis Vincenti, chief executive of both Mutual Savings and Wesco, is no exception. In our view the record he has created is better than those of his peers, reflecting both unusual talent and a very high sense of stewardship for savers and shareholders.

PRECISION STEEL WAREHOUSE, INC.

Our 80%-owned Precision Steel subsidiary, located in the outskirts of Chicago at Franklin Park, Illinois, was acquired for approximately $15 million on February 28, 1979. It owns a long-established steel service center business and a subsidiary engaged in the manufacture and distribution of tool room supplies and other products sold under its own brand names. Precision Steel's operating businesses contributed $1,560,000 to our consolidated net income in 1981 compared with $1,205,000 in 1980.The increase in earnings was more than proportionately attributable to operations in the first three quarters of 1981. In the last quarter of 1981 and the first quarter of 1982, earnings have declined substantially, reflecting severe recessionary conditions in the steel industry.

Even under recessionary conditions operations remain profitable, and we anticipate no great change in earnings for the full year 1982.

The minimum shareholders' equity, at Blue Chip's carrying value, required to operate Precision Steel's business at its 1981 level is about $14 million, on which the business earned $1.9 million in 1981 or at a rate of 13.6% per annum.

We knew when we purchased Precision Steel that earning a return, satisfactory under inflationary conditions, on the unleveraged equity capital required to operate its business would be difficult, and we supplied some leverage by borrowing the purchase price, refinancing at a fixed rate as soon as practicable. We ordinarily have reservations concerning financial leverage but are willing, as in this case, to borrow money to purchase as part of our mix of businesses a clean and moderately profitable company like Precision Steel where inventories carried on the LIFO basis represent a substantial part of total assets and where reported earnings are expected usually to turn up in cash, absent optional expansion.

Both Mutual Savings and Precision Steel are owned by Blue Chip Stamps through 80% control of Wesco Financial Corporation, a public company with shares traded on the American Stock Exchange. For more complete information, we encourage Blue Chip shareholders to obtain a copy of Wesco's 1981 annual report.

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Simply make your request to:
Wesco Financial Corporation
315 East Colorado Boulevard
Pasadena, California 91109
Attention: Mrs. Jeanne Leach, Treasurer

BUFFALO EVENING NEWS, INC.

Our 100%-owned subsidiary, Buffalo Evening News, Inc., was acquired in April 1977 for approximately $34 million. It now constitutes only approximately $28.5 million of our consolidated net worth, as a result of about $5.5 million of aggregate after-tax operating losses after acquisition. This translates roughly into $11 million of aggregate operating losses before taxes.

However, the operating loss, before taxes, of the News in 1981 was lower than that of 1980, having declined to $1,091,000 from $2,805,000 in the previous year, which in turn had declined from $4,617,000 in 1979.

The steady reduction in operating loss has been made possible by a combination of aggressive price increases, intense efforts at general cost containment, and reduction or elimination of expenses or losses in three specific categories: (1) litigation expense, (2) expense of "buy-outs" from labor contract provisions made in order to allow the News to benefit from equipment modernization, and (3) the strike losses of 1980. A lot of effort has gone into reducing the overall operating loss — except that more "buy-outs" would have been preferred — and the 1981 results reflect some success.

We predicted accurately the financial improvement in 1980 and 1981. For 1982 we confidently predict a lack of improvement. We anticipate terrible market conditions for the News in 1982.

Buffalo has been hit harder than the average U.S. city by the current recession, and the attrition rate among retailers is sharply and permanently reducing the demand for the advertising service provided by the two main newspapers. In 1981 the News and the Buffalo Courier-Express, the News' main competitor, ran 4,000,000 lines of advertising (10% of their aggregate retail advertising linage) from retailers which by the end of 1982 either will not be in business at all or will be in business as mere remnants of their former selves. Although th Courier-Express is bearing a share of the retailing contraction, that will not stem the losses faced by the News.

It is particularly discouraging that continuing operating losses occur despite aggressive circulation and advertising price increases in the recent past. The News, for instance, increased circulation revenues by 15.2% in 1981, a figure exceeding that achieved in many cities less affected by the recession, helping cause a small but painful reduction in weekday subscribers, and will be forced to be conservative when it again increases circulation prices later in 1982. Based on the News' experience to date, it does not dare go faster in raising circulation prices. And, with a retailing contraction now in progress, the outlook for any above-normal increases in advertising prices also appears very dim. Greater, not smaller, operating losses for the News almost surely lie immediately ahead.

Not all of the difficulties come from purely regional trends. Since publication of our 1980 annual report there have also been a number of adverse developments in newspaper economics not limited to areas like Buffalo which are bearing more than their share of the current recession. Certain important print advertisers, once thought certain to rely almost 100% on newspapers, are experimenting with alternate forms of delivery. As the world has changed, the Washington Star, once by far the strongest daily newspaper in what remains a prosperous and growing Washington, D.C. metropolitan area, has ceased publication, as has the Philadelphia Bulletin, which once occupied a position of seemingly impregnable dominance in its city. The Bulletin was late in starting a Sunday edition, never caught up on Sunday, and eventually lost its weekday advantage as well, cascading to extinction. The ranking of the News among the nation's evening newspapers has been moving steadily upward, not because its circulation is growing but because large evening newspapers are disappearing.

In many of America's remaining two-or-more-metropolitan-newspaper cities, one or two of the newspapers have been reported to be losing money, including but by no means limited to the Boston Herald American, the Los Angeles Herald Examiner, the New York Post, the New York Daily News, the Seattle Post Intelligencer, the Trenton Times, the Cleveland Press, the Detroit Evening News and the Detroit Free Press. In fact, we know of only five metropolitan areas (above 250,000) in the U.S. where two separately owned and economically competing daily newspapers are both now profitable — Houston, Dallas, Denver, San Antonio and Chicago. Houston and Dallas are booming sunbelt cities aided by the OPEC energy cartel, and we suspect that profits in the weaker papers in Denver, San Antonio and Chicago are marginal.

Even more ominous, operating trends have been poor in a number of two-daily-newspaper cities, more prosperous than Buffalo, where both newspapers have the same owner. That operating trends can be poor even under such conditions tends to confirm that more aggressive pricing by the News and its main competitor in

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Buffalo — which might appear akin to the solution hoped for by airlines when they anticipate the end of price wars — is not likely to cause termination of the operating miseries of the News. Pricing in Buffalo, with some limited exceptions, is already quite aggressive, all factors considered. The economic demand for both reading material and advertising service is price-sensitive, and does not necessarily increase, or even remain static, when prices are increased only as much as necessary to cover inexorable increases in the energy-intensive and people-intensive operating costs of our newspaper. Economic forces are at work which are plainly beyond anyone's control, and we are catching at least our share of a widespread malaise. We know of no easy solution.

It is, of course, a temptation when writing an annual letter to shareholders to gloss over difficulties, like those in Buffalo, and comment extensively concerning successes. We recommend exactly the opposite emphasis to business managers who report to us, and we believe in practicing what we preach. Accordingly, year after year, we re-tell and extend the history of the News, creating the largest single section of our annual letter. This year we surpass all previous records.

The News had no Sunday edition when acquired. The principal competitor, the Buffalo Courier-Express, published without opposition on Sundays. As we explained in detail in our 1977 through 1980 annual reports, the long-term survival of the News clearly required that it inaugurate a Sunday edition. [Of that there was simply no question. Real trouble has been the invariable eventual outcome for every other daily newspaper in the United States, no matter how extreme its past record of prosperity and popularity, which relied overlong, in an important city, exclusively on weekday publication while a significant seven-day competitor enjoyed a Sunday monopoly. In fact, only three other "no-Sunday" papers, competing against such "with-Sunday" papers in important cities, survived as late as 1977, even though many such "no-Sunday" papers once had long histories of profitability derived from dramatic advantages in weekday circulation and advertising over their "with-Sunday" competitors. Moreover, the three other survivors all were in serious trouble in 1977. And since then one of the three survivors, the Cincinnati Post, has been preserved, after incurring huge losses, only through the grace of its competitor's absorbing it into a minority share of a joint operation with approval of the U.S. Attorney General as required by the Federal Newspaper Preservation Act of 1970. A second of these "no-Sunday" survivors of 1977, the Cleveland Press, after also incurring huge losses, was recently sold by its experienced Ohio-based newspaper-chain owner (Scripps-Howard), under distress conditions, to a wealthy Cleveland man who forthwith spent millions of dollars inaugurating a Sunday edition. Even after so recognizing the cause of its difficulties, and despite tying Sunday circulation to a very substantial daily circulation base, the Cleveland Press now appears almost surely doomed to continuing and apparently irreversible operating losses by its reluctance or inability to create a Sunday edition at a timely point in its history. The only other remaining "no-Sunday" survivor is the New York Post, controlled by the able Rupert Murdoch, which has been losing many millions of dollars per year and which has announced it must have a Sunday edition to survive. Prospects for its survival looked virtually nil until 1981 when the New York Post's principal competitor, the New York Daily News, by far the biggest newspaper in New York City, announced it was tired of losing money and was looking for a buyer. If the New York Daily News eventually closes, the New York Post may well survive, aided by the Sunday edition it would then surely have. In any event, one way or another, within a very few years the "no-Sunday" paper, competing in an important American city against a "with-Sunday" competitor, will be as extinct as the dodo bird.]

Under such circumstances, the News commenced publishing Sundays late in 1977, as it plainly had to do if it cared at all about its long-term future. In response, an antitrust lawsuit was filed by the competing paper which for the first time faced the prospect of competition on Sundays as well as weekdays. The lawsuit, in turn, resulted in some interlocutory (i.e., temporary and not final) injunctions which, among other things, created severe disruptions in normal circulation procedures under midwinter conditions and restricted certain business promotion practices of the News, commonplace within the newspaper industry, while similar but more aggressive practices of the competing paper were not prohibited.

These interlocutory injunctions against the News were reversed on appeal in 1979. In its unanimous decision for reversal of the injunctions, the Federal Court of Appeals reasoned that the generally pro-competitive antitrust laws should not be used in an anti-competitive fashion by enjoining normal promotional practices, such as those used by the News, in the course of normal competition such as inauguration of a Sunday edition.

Of course, the elimination of the harmful interlocutory injunctions did not automatically improve the circulation and advertising linage of the News' Sunday edition. Success in the market had to be won slowly, if it could be won at all, through creating a desirable value for customers. Moreover, achieving success was made more difficult by the fact that it was beyond the power of the appellate court to reverse certain material damage suffered by the News as a result of the interlocutory injunctions and accompanying publicity. Damage inflicted on an infant at birth impairs its subsequent life even after the people in charge of the operating room have decided that different delivery procedures would have been appropriate.

Despite the damage at birth, there was a gradual trend toward success. The Sunday edition of the News has been recognized by subscribers for editorial merit and rewarded by steady circulation growth, needed

considering the substantial Sunday-circulation lead of its principal competitor. Great credit must be given to Murray Light, Editor of the News, and other editors and reporters, for consistent delivery of a product which deserves and has received increased acceptance by the Greater Buffalo community. The circulation of the News' Sunday edition was over 183,000 copies in February 1982, up from approximately 178,000 copies in February 1981 which, in turn, was up from 173,000 copies in February 1980. We expect Sunday gains to continue. Weekday circulation decreased slightly in 1981, after increases in both 1980 and 1979, and the weekday News continues to be greatly preferred to the weekday Courier-Express by both readers and advertisers. As this is written we believe that, measured against levels twelve months earlier and ignoring at both papers meaningless temporary fluctuations caused by special promotion, circulation at the Courier-Express is essentially unchanged on both weekdays and Sundays whereas at the News Sunday circulation is up about 3% and weekday circulation is down about 2%. The News' total weekday circulation is still more than twice that of the Courier-Express, and the weekday circulation split in the close-in areas most important to advertisers remains considerably more favorable to the News than the split in total circulation. Moreover, to this point the News has pretty well held its own on weekdays as a strictly afternoon newspaper without following the practice in most other major two-competing-newspaper cities (e.g., in Dallas, Houston, Seattle, Detroit and Denver) where the afternoon newspaper has gone "all-day" by commencing publication of a morning edition for limited distribution by street sales and home delivery in outlying areas.

On Sundays, the Courier-Express continues to have a little less than 60% of the two newspapers' combined circulation.

We do not know precisely the News' share of the combined advertising revenues of the two newspapers, but we believe it was essentially unchanged during the last two years at about 60%, or perhaps a bit higher. Presumably the Courier-Express lost at least as much money as the News last year.

Overall, this situation is not desirable for our employees or shareholders. And labor relations are affected in a none-too-predictable fashion when employers are unable to incur additional costs without bearing unacceptable losses.

Approximately 83% of the News' employees are members of its 13 different labor unions which through bargained settlements over many years have helped create collective bargaining agreements some of which contain provisions, designed to save jobs, which prevent technological change. With occasional exceptions, all in recent years, as each new collective bargaining agreement was negotiated the union involved sought to improve, from its own point of view, on the expiring collective bargaining agreement, with the net effect that (1) the newspaper was often left weaker on account of inefficient operations and (2) there was often some leapfrogging of benefits, giving a particular union more than its proportionate share of aggregate available economic advantage.

By the time Blue Chip Stamps purchased the News in 1977, this process, combined with a similar process at the Courier-Express and the general state of the newspaper business in Buffalo, had greatly reduced profits of both newspapers. In fact, profits were so minimal that unless more rapid technological progress were allowed and the leapfrogging process ended in favor of conservative pattern settlements, one of the two major newspapers eventually would be forced to cease publication, as has happened in response to similar pressures in major city after major city, on both sides of the Atlantic. In recognition of these facts, the Courier-Express in the years immediately preceding 1977 obtained needed union concessions and suffered no strikes.

There were also grounds for optimism concerning labor relations at the News. We believed in 1977 when we purchased the News that the enterprise-destroying pattern of labor relations which had killed so many metropolitan newspapers was unlikely to kill the News in Buffalo. For one thing, the News had an up-from-the-ranks labor-relations executive, Richard Feather, whom we instantly admired and trusted as fair-minded and constructive and perceived as likely to be so regarded by union members at the News. For another, we made a point, before closing the acquisition, of meeting some of the union leaders and their counsel, and they likewise impressed us favorably. Further, we noticed a great professionalism in employees at the News. Production people and reporters alike cared about the quality of their product, causing us to conclude that they would care similarly about the security and continuation of a common enterprise. Still further, we perceived a high level of friendship and communication among employees of the News, across craft-union lines. Indeed, the enterprise is so old and its jobs so well regarded that jobholders of all kinds have for decades urged their relatives and friends to join the News, often in different craft unions, creating as the years went by something more like a family business than might seem possible to anyone not familiar with it. Finally, we had enjoyed constructive relations with diverse and major labor unions elsewhere and did not enter Buffalo with any plan to seek destruction of long-established benefits, although we did hope to use negotiated voluntary "buy-outs" to make some particularly important reductions in future costs. All these factors, together with the News' long history of labor peace, contributed to our willingness to purchase the News, although at least two

other prospective buyers, perhaps more fearful of the risks from having an unusually large number of separate unions, had refused to pay the asking price for the paper.

Until 1980 the long no-strike history continued much as we expected, despite economic forces and troubles which frequently caused operating losses for the News and disappointing wage and salary increases for union members and other employees.

However, with 13 different unions and serious external pressures from competition and inflation, labor peace requires that 14 different groups (the News' management plus all 13 unions), without any exception, understand well the common danger, and, even if moving backward in inflation-adjusted economic terms, be wise and considerate of one another at all times. Even in the presence of the unusually favorable conditions for labor peace at the News, such unanimous wisdom and restraint are a lot to expect, given (1) the limitations of human nature, including that on management's side of the table, (2) the tradition, carried over from a different era, at each union that its main preoccupation should be vigorously to enhance and protect the interests of its own members, and (3) the fact that technological changes do not arrive at a steady pace and with effects allocated equally to each union.

The long labor peace ended in December 1980, when one small union group went on strike in an effort to insert new manning requirements, and new requirements of pay for work even if not performed, into its collective bargaining agreement. Most of the other unions' members, recognizing the pattern-breaking nature of the striking union group's demands, ignored a picket line and reported for work, but, finally, most of the News' pressmen refused to continue working, and the News was unable to continue publishing.

The gravity of the strike, its harmful effect on the potentiality for continued existence of the News, can hardly be overstated. An area-wide metropolitan newspaper which is closed down by a strike while a similar competitor continues publishing does not merely lose a lot of money while the strike goes on and then return to publishing at approximately the same annual profit (or loss) as before. Instead, because the competing paper gains circulation rapidly during the strike, the closed-down paper usually suffers such a loss of competitive position that it fairly soon reaches a point where it is unwise to reopen at all. For instance, in Montreal what had long been the overwhelmingly dominant English-language newspaper recently lost many millions of dollars, before its ultimate expiration, in a fruitless and foolish attempt to reopen after a strike of several months during which its main competitor continued to publish.

Such being the facts of life, the News had no practicable alternative, when its strike occurred in 1980, except to prepare to face rationally whatever degree of impaired position resulted from the strike. Clearly, if the strike was an extended one, the sensible decision would be not to renew publication. Nor was the News willing to settle its disagreement with the striking union group in any manner unfair to other unions involved, under conditions of common external hazard, in serial bargaining of union contracts. A resolution of the dispute unfair to unions which had settled earlier would lead to a ruinous resumption of leapfrogging to the ultimate detriment of the News and all its employees, including those attempting to take the first jump.

Fortunately, the amount of good will and good sense at the News was sufficient, as the matter worked out, to cause the strike to end in two days without, in the News' view, unfairness to unions which had settled earlier. However, the strike augmented the News' pre-tax losses by several hundred thousand dollars in 1980 and also caused a small loss of competitive position. Both economic results, of course, diminish the capacity of the News to compensate its employees in the future as well as its prospects for beginning to pull its economic weight for shareholders.

In 1981 there was no major labor crisis at the News although hardships were being shared instead of advances. With a very few exceptions the News' economic difficulties in recent years have come in spite of an overall attitude of understanding in its employees and not on account of a lack of such understanding. The ultimate survival of the News continues to depend not only on its competitive position but also on repetitive success on the part of management and all unions in dealing fairly and wisely with one another, under very difficult conditions, changing habits formed in a different era.

The litigation against the News, filed by former owners of the Courier-Express in 1977 when the News commenced publishing on Sundays, remains pending. However, the litigation has been dormant in 1981, following purchase of the Courier-Express by the Minneapolis Star and Tribune Company, which has a history of preferring the exercise of business and journalistic skills over court battles. On the other hand, possibly as a result of this preference, the Courier-Express is now a more effective competitor than it was under its former owners.

However, the improved Courier-Express is not making headway against the News, which is also improving. And even though we anticipate an unsatisfactory 1982 year, we anticipate better operating results in the more remote future. Because we own what we believe to be one of society's best service institutions and much the better of Buffalo's two major newspapers, we still hope and expect that the News in due course will earn annual profits consistent with its value to Buffalo and appropriate to our level of investment. This generally has been the

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outcome for the better of two competing seven-day newspapers, and despite some new economic variables affecting metropolitan newspapers, we believe that such outcome is likely for the News.

This is not to say that we will ever really get well, considering all effects of our initial decision to buy the News. Shareholders can easily calculate that the reported losses of the News are a small part of the economic detriment our decision created. While convention doesn't require reporting of "opportunity cost" losses to shareholders, we believe they are just as important as conventional reported losses and should be faced just as squarely. If we hadn't purchased the News in 1977 but had simply earned returns on the unspent purchase price comparable with the average earning power of the rest of our shareholders' equity, we would now have about $70 million in value of other assets, earning over $10 million per year, in place of the Buffalo Evening News and its current red ink. No matter what happens in the future in Buffalo we are about 100% sure to have an economic place lower than we would have occupied if we had not made our purchase. In a period like the present one, where passive returns on capital before inflation are high, an inadequate or negative return persisting for any extended period is almost impossible to make up through later success, after allowing for probable returns from alternative capital uses. When other capital is sprinting, remaining in the starting blocks for a long time prevents one from ever catching the field.

Of course, we can't now relive the past but must simply adopt the correct business strategy for the present situation. That strategy is clearly for the News to keep doing the very best job it can for its city, its employees, its readers and its advertisers, seven days a week, unless and until some combination of our principal competitor's relative strength, our intolerable losses, and our labor-trouble weakness makes the long-term future look hopeless. There is no such situation now and we think it extremely improbable that such a situation will occur in the future. If it ever does, we will face it. But we will first exert every effort to make certain it never occurs, believing as we do that the News has both the product and the acceptance that should make its efforts successful.

The News remains a salable property, even with its current troubles, so long as its share of circulation and advertising is stable-to-inching-ahead, and we could easily improve our consolidated operating earnings and the percentage return we earn on our shareholders' investment by selling the News and reinvesting the proceeds, after tax effects, in profit-earning assets. That we are not even slightly tempted to do so demonstrates our conviction that Buffalo will have a reasonably felicitous future as a city and that the fine people who work at the News will ultimately succeed in making it a sound business for its owners and employees, through continued provision of sound service to its customers. We still plan to stay with the News until it either expires, or, far more likely, becomes a solid earner and employer.

Despite our confidence in the probable long-term success of the News, caution is appropriate based on the record to date and the nature of the situation. We therefore repeat to shareholders our warning in previous years regarding what we now believe are unlikely contingencies: "If the litigation continues and if the competing paper succeeds in somehow changing the law as enunciated by the Federal Court of Appeals and in obtaining the kinds of injunctions it is seeking, or if any extended strike shuts down the Buffalo Evening News, it will probably be forced to cease operations and liquidate, at an after-tax cost which could exceed $10 million."

PROMOTIONAL SERVICES BUSINESS AND MISCELLANEOUS SOURCES OF OPERATING INCOME

The final components of our consolidated net operating income last year were provided by (1) operating earnings from our promotional services (mainly trading stamp and motivation) business, after deduction of interest and other general parent company expense, plus (2) our share of operating earnings, after deduction of interest and other Wesco general corporate expense, from securities and real estate held by Wesco outside the savings and loan and steel service activities of its subsidiaries.

The promotional services business operated at a sharply decreased profit, after parent company interest and other general expense and income taxes, last year, down to $3,659,000 from $4,293,000 after (properly) giving it credit for the entire income (dividends and interest, plus income tax benefits caused by dividends) from investment of the funds available through "float" caused by trading stamps issued but not yet redeemed. Our shareholders should not be discouraged by the decrease in after-tax profit, which was attributable to the fact that favorable revisions in our estimates of our liability to redeem outstanding trading stamps were made in 1980 but not in 1981. The revisions, which by their nature will not frequently recur, increased 1980 after-tax profit by $1,747,000, and, therefore, in the absence of such revisions after-tax profit would have improved last year.

Although trading stamp service revenues decreased by only a minor amount to $15,619,000 in 1981 compared with $16,672,000 in 1980, they are expected to drop materially in 1982. By the time this report is distributed, we understand that the Stater Bros. supermarket chain, which accounted for 51% of our trading stamp revenues in 1981 and which has recently been for sale, will have publicly announced that it will discontinue giving trading stamps on April 1, 1982. Loss of the Stater Bros. account will present us with a serious

challenge: We must not only continue our efforts in adding to our customer base (for example, in the retail gasoline trade, where we have recently had considerable success) but also try to replace the lost grocery business by signing up a competing grocery chain, which we have been unable to do in the past because of our commitment to Stater Bros. We are as convinced as ever that trading stamps are an effective point-of-purchase sales promotion device for supermarkets, service stations, bowling alleys and the like. We intend to remain in the trading stamp business.

In our trading stamp business our "float" — resulting from past issuance of trading stamps when volume was many times greater than the current level — is large in relation to current issuances. (Trading stamp revenues peaked at $124,180,000 in fiscal 1970, and our 1981 revenues of $15,619,000 therefore represented a decline of 87% from peak volume.) Eventually, unless stamp issuances improve, earnings from investing "float" will decline greatly. The decline in "float" in recent years, however, has proceeded at an extremely slow rate, and our reserved liability for trading stamp redemption was $64,262,000 at yearend 1981.

As discussed extensively in previous annual reports (particularly for fiscal 1976), which we urge shareholders to review, accounting for trading stamp redemption liability (which involves estimating the number of stamps that will ultimately be redeemed and the cost per stamp) is a difficult process under any circumstances, but particularly so in an inflationary economy and when stamp issuances decline by a large percentage. We periodically revise our estimated future redemption liability as conditions warrant. In 1980 we made revisions increasing operating income as above described, as explained in detail in Note 2 to our accompanying financial statements.

Motivation business revenues decreased to $1,446,000 from $2,771,000, but are expected to rise in 1982.

One final item augments our consolidated net operating income. Our share of operating earnings, after deduction of interest and other Wesco general corporate expense, from securities and real estate held by Wesco outside the savings and loan and steel service activities of its subsidiaries, amounted to $1,665,000 in 1981, compared with $695,000 in the previous year.

NET GAINS ON SALES OF CORPORATE SECURITIES, MORTGAGES AND IMPORTANT FIXED ASSETS

In our total assets, located among our five operating businesses, we hold considerably more corporate securities than might be expected in a consolidated enterprise of our size at the close of 1981, as we report consolidated revenues of $246 million and consolidated net worth of $169 million (see Note 3 to our accompanying consolidated financial statements).

Most of these holdings of corporate securities are held because of the very nature of the particular business in which they are owned. For instance, the trading stamp business owns liquid assets to provide for ultimate redemption of stamps, and the savings and loan business holds liquid assets to provide for repayment of savings account holders. The remaining security holdings exist temporarily, primarily in Wesco Financial Corporation, pending their disposition to provide funds for use in buying additional businesses.

Only Mutual Savings, which is barred by law from owning most common stocks, has significant holdings of preferred stocks. Most holdings, therefore, are of common stocks. Our reported operating earnings include only the dividends from our stockholdings, after taxes. And, because the corporations whose common stock we own also have and reinvest earnings not paid out as dividends, a process which ultimately raises market value of the stock we own, we also realize regularly net capital gains from sales of portions of our holdings.

In addition, our various businesses occasionally sell important buildings, machinery or other fixed assets, as such businesses adjust to changing conditions. In 1980 the sale of branch office facilities by Mutual Savings fell into this category. No significant sale of fixed assets occurred in 1981.

In 1980 our share of the gain from sale of Mutual Savings' branch office facilities was $2,332,000, and our total share of the net gains from sale of corporate securities was $1,493,000. Our aggregate share of all types of special gains combined was $3,825,000 in 1980, compared with $6,731,000 in 1981, all from the sale of securities.

PINKERTON'S, INC.

At yearend 1981 we owned non-voting stock representing 37% of the equity in Pinkerton's, Inc., the leading national security and investigation service company.

Our ownership of this non-voting interest demonstrates that, when all factors are considered, we often would rather buy stock we can't or won't vote than absolute control. We think the rationality of use-of-capital decisions is improved when the repertoire of a corporate manager includes purchases of business interests which do not augment the number of people to whom the manager can give orders. However, we have generally observed a low interest among corporate managers in passive investments, even when available at much better

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price/earnings and price/book value ratios than controlling positions. The strong preference for controlling positions is ordinarily justified by (1) expected improvements from a change in control based on a high appraisal of the business skills of the managers of the corporate investor compared to the managers of the corporate investee and (2) a low appraisal of the likelihood that the managers of the corporate investee, if free to act independently, will make decisions which best serve the interests of ultimate shareholders. Our view is different, and, although we expect always to concentrate our activities primarily in operating businesses, we also have an uncommon interest in passive positions for the following reasons:

(1) We know that our business skills are frequently inferior by a wide margin to those of others, as we can prove from comparative figures and our audited record reflecting gross errors;

(2) We believe that many corporate managers can be trusted to serve the shareholders' interests even when the shareholders have no practical power to control or replace management;

(3) We think the advantage of buying at a non-premium price, because control is absent, often counterbalances the disadvantage, if any, from lack of control;

(4) Our consolidated enterprise includes operating businesses required by their nature to own significant passive investments.

We hope to become better known for our uncommon willingness to own "non-voting-partnership" interests in businesses and to attract other offerings like that which produced our Pinkerton's holding. And we are sure, based on five years' observation from our non-voting position, that Pinkerton's wouldn't have been managed one whit better or one whit more in its shareholders' interests if we had purchased voting control.

Our total investment in Pinkerton's at cost was $23,364,000, which, with respect to the major portion thereof constituting marketable securities, is substantially below current market value. See Note 3 to our accompanying financial statements. Only the dividends we receive from Pinkerton's are included in our reported income. These dividends have increased regularly in recent years, creating part of the income reported above under the heading: "Promotional Services Business and Miscellaneous Sources of Operating Income." The part created by Pinkerton's dividends was $1,730,000 in 1981 and $1,429,000 in 1980.

CONSOLIDATED BALANCE SHEET AND OTHER DATA

Our consolidated balance sheet retains a strength befitting a company whose consolidated net worth supports large outstanding promises to others. As explained in Note 3 to the accompanying financial statements, the aggregate market value of our marketable securities was higher than their aggregate cost at December 26, 1981. In addition, an office building and related real estate owned by Wesco Financial Corporation has a market value substantially in excess of carrying value. We remain in a prudent position when total debt is compared to total net worth and total liquid assets.

Retaining the impeccable bank credit facilitated by a prudent balance sheet position is very important to us. When combined with our practice of doing a certain amount of long-term borrowing in advance of specific need, it gives us maximum financial flexibility to face both hazards and opportunities.

Sections entitled "Principal Business Activities," "Selected Financial Data" and "Management's Discussion and Analysis" are presented beginning on page 13. We invite your careful attention to these items and to our audited financial statements.

A LOOK BACK AND A LOOK AHEAD

We began the 1970s with a single business, trading stamps, which was destined to decline to a small fraction of its former size, and a portfolio of securities, offsetting stamp redemption liabilities, which had been selected by previous owners and would have led to a disastrous result if held through to the present time. (The portfolio, for instance, contained a substantial amount of very-long-term, low-coupon municipal bonds of issuers with declining credit ratings.)

We began the 1980s with five constituent businesses instead of one. In order of acquisition they are: (1) trading stamps and other promotional services, (2) See's Candy Shops, Incorporated, (3) Mutual Savings, (4) Buffalo Evening News, and (5) Precision Steel.

Our five constituent businesses have more in common than might be noted by a casual observer:

(1) They are all high-grade operations suffused to a considerable extent with the business ideas of Benjamin Franklin, manned by high-grade people operating within a long tradition emphasizing reliable and effective service, and

(2) When functioning properly each business will usually generate substantial amounts of cash not claimed by compulsory reinvestment in the same business and therefore available for purchases of new businesses or debt repayment.

Reproduced from 1981 Annual Report of Blue Chip Stamps.

The second of these two common characteristics gets more important every year as inflation continues. Many businesses, once good investments when inflation was low, are now, under inflationary conditions, unable to produce much, if any, cash even when physical volume is constant. Any such business, always cash-starved even while reporting apparently satisfactory profits, is not a candidate, absent some special factor, to become a new subsidiary of ours.

Our balance sheet net worth at March 4, 1972 was about $46 million. By the end of 1981 our balance sheet net worth had increased to approximately $169 million, up 267% in ten years, after payment of regular dividends. At March 4, 1972 our equity in aggregate securities was worth about $3 million less than balance sheet cost. At the end of 1981 this equity was worth about $26.7 million more than balance sheet cost. Our average annual total percentage return earned on shareholders' investment over the ten years ending December 26, 1981 was approximately 15% per annum, without counting the favorable swing from unrealized loss to unrealized profit in our equity in marketable securities. The percentage return earned was acceptable in a moderate-inflation environment, considering the headwinds in our initial trading stamp business.

In 1981, the year just ended, our total percentage return on the beginning investment of our shareholders was approximately 19%. This percentage return fluctuates from year to year, depending upon various factors including changes in amounts of capital gains realized. The percentage return figure for any one year is not very significant, although the average figure over a period of years, and the trend in such average figure, are of vital importance.

We hope to earn a higher average (though sharply fluctuating) annual total percentage return on shareholders' investment in the next ten years than we have in the ten years just past. Our total percentage return on shareholders' investment is now depressed by our substantial commitment to the Buffalo Evening News, producing losses instead of profits. We are trying to correct this condition. Moreover, we expect from time to time to acquire additional businesses which eventually will produce higher returns than the assets disposed of to fund their purchase. A better experience in the future is far from a sure thing, but it may well be achieved if future errors, headwinds, and reverses are no worse than the ample number characterizing our past.

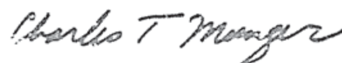
However, even if we succeed in increasing our average annual total percentage return on shareholders' investment, our performance as a company may not do very much for our shareholders as investors if inflation continues at the present rate. As we point out year after year, "A 16% return on equity obviously won't do much in real terms for shareholders if the inflation rate is 16%, or even 11% when we also allow for income taxes imposed on owners who must report taxable 'profits' while only maintaining their position on the purchasing-power treadmill."

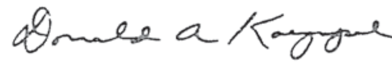
Inflation is a very effective form of indirect taxation on capital represented by holdings of common stock. We know of no adequate countermeasure, generally available to corporate managers who wish to protect shareholders, to this form of indirect taxation. But, even so, we think a habit of always thinking about shareholders' interests in real terms, instead of rationalizing growth of managed assets regardless of real effects on shareholders, is quite useful and may fairly be expected of corporate managements. We make a very conscious effort, perhaps with occasional inadvertent lapses, to have and reinforce this habit.

For one example, low stock prices, caused by inflation, together with our preoccupation with real shareholder interests, have intensified our resistance to most proposals that we issue new common stock. We haven't issued a new share, for any reason, for a long time. With rare exceptions American corporations now cannot get as much intrinsic value as they give when new common stock is issued. Our corporation is no exception. And, quite clearly, a corporation can't further its own shareholders' long-term interests by diluting, through new stock issuances, the value underlying each outstanding share. Our unwillingness to accept any such dilution explains our long-unchanged common stock capitalization.

We believe that our (1) heavy emphasis on the cash-generating characteristics of businesses, (2) reluctance to issue new stock and (3) strong balance sheet position are all likely to enjoy increased recognition in future years as qualities to be emphasized by selectors of common stocks for investment.

Cordially yours,





Charles T. Munger
Chairman of the Board

Donald A. Koeppel
President

March 18, 1982

The 1981 Annual Report of Wesco Financial Corporation included the following letter from Louis R. Vincetti, Chairman of the Board and President of Wesco.

TO THE STOCKHOLDERS OF WESCO FINANCIAL CORPORATION

Consolidated net income of Wesco Financial Corporation and its subsidiaries for 1981 amounted to $9,779,000 ($1.37 per share) compared to $10,045,000 ($1.41 per share) in 1981. Sources of net income are as follows:

	1981	1980
Wesco Financial Corporation (Parent Company)	$2,705,000	$ 1,358,000
Mutual Savings and Loan Association	3,458,000	7,353,000*
Precision Steel Warehouse, Inc.	1,947,000	1,504,000
Realized securities gains (losses)	1,669,000	(170,000)
	$9,779,000	$10,045,000

Our statement of income for this year differs from that of previous years. We now show separately the amount realized on securities gains (losses).

The continuance of positive earnings by Wesco and its subsidiaries for 1981 is in contrast with the substantial losses being reported by most other savings and loan associations and holding companies. The result is, in part, attributable to the disposition in 1980 of the branch offices of Mutual Savings and to the substantial stockholders' equity of $109,461,000 at December 31, 1981 which is 32% of assets.

The unprecedented poor performance of the savings and loan business generally, in 1981, is in large part attributable to the high and volatile interest rates in existence for that year. The outlook for 1982 is for more of the same.

This amount differs from $6,243,000 which was reported in our 1980 annual report. The difference represents realized securities losses of $1,110,000 by Mutual Savings which is now shown separately with other realized securities gains and losses.

During 1981, real estate loan disbursements by Mutual Savings were $304,000 compared with $13,618,000 in 1980. Mutual Savings, at the present time, is not active in real estate lending. We are unable to predict with any confidence the new environment that will exist for this industry in the future. We expect to adapt successfully to whatever that new environment will be.

Savings accounts at Mutual Savings totaled $149,168,000 at December 31, 1981 compared with $168,366,000 at 1980 year end. Savings accounts can be maintained by competing for deposits of $100,000 or more which are not subject to rate control. Mutual Savings could substantially increase the total amount of its savings accounts by the payment of a larger rate of return on such types of accounts. Mutual Savings has not done so. At December 31, 1981, approximately 6% of the total savings accounts of Mutual Savings were in this category.

This annual report contains Form 10-K, a report filed with the Securities and Exchange Commission. It provides much detailed information on the operations of Wesco and its subsidiaries. Of particular interest is the table on page 8 showing the rate spread between the combined yields on loans and investments and the combined cost of savings and borrowings.

On January 27, 1982, Wesco increased its regular quarterly cash dividend from $.11½ per share to $.12½ per share, payable March 16, 1982 to stockholders of record as of the close of business on February 23, 1982.

Louis R. Vincenti
Chairman of the Board and President

The letter reproduced on this and the following 2 pages, describing the Company's shareholder designated contributions program, was mailed on October 14, 1981 to all persons who were then record-owners of the Company's common stock.

BERKSHIRE HATHAWAY INC.
1440 KIEWIT PLAZA
OMAHA, NEBRASKA 68131
TELEPHONE (402) 342-4110

WARREN E. BUFFETT, CHAIRMAN

OCTOBER 14, 1981

To the Shareholders of Berkshire Hathaway Inc.:

On September 30, 1981 Berkshire received a tax ruling from the U.S. Treasury Department that, in most years, should produce a significant benefit for charities of your choice.

Each Berkshire shareholder — on a basis proportional to the number of shares of Berkshire that he owns — will be able to designate recipients of charitable contributions by our company. You'll name the charity; Berkshire will write the check. The ruling states that there will be no personal tax consequences to our shareholders from making such designations.

Thus, our approximately 1500 owners now can exercise a perquisite that, although routinely exercised by the owners in closely-held businesses, is almost exclusively exercised by the managers in more widely-held businesses.

In a widely-held corporation the executives ordinarily arrange all charitable donations, with no input at all from shareholders, in two main categories:

(1) Donations considered to benefit the corporation directly in an amount roughly commensurate with the cost of the donation; and

(2) Donations considered to benefit the corporation indirectly through hard-to-measure, long-delayed feedback effects of various kinds.

I and other Berkshire executives have arranged in the past, as we will arrange in the future, all charitable donations in the first category. However, the aggregate level of giving in such category has been quite low, and very likely will remain quite low, because not many gifts can be shown to produce roughly commensurate direct benefits to Berkshire.

In the second category, Berkshire's charitable gifts have been virtually nil, because I am not comfortable with ordinary corporate practice and had no better practice to substitute. What bothers me about ordinary corporate practice is the way gifts tend to be made based more on who does the asking and how corporate peers are responding than on an objective evaluation of the donee's activities. Conventionality often overpowers rationality.

A common result is the use of the stockholder's money to implement the charitable inclinations of the corporate manager, who usually is heavily influenced by specific social pressures on him. Frequently there is an added incongruity; many corporate managers deplore governmental allocation of the taxpayer's dollar but embrace enthusiastically their own allocation of the shareholder's dollar.

For Berkshire, a different model seems appropriate. Just as I wouldn't want you to implement your personal judgments by writing checks on my bank account for charities of your choice, I feel it inappropriate to write checks on your corporate "bank account" for charities of my choice. Your charitable preferences are as good as mine and, for both you and me, funds available to foster charitable interests in a tax-deductible manner reside largely at the corporate level rather than in our own hands.

Under such circumstances, I believe Berkshire should imitate more closely-held companies, not larger public companies. If you and I each owned 50% of a corporation, our charitable decision making would be simple. Charities very directly related to the operations of the business would have first claim on our available charitable funds. Any balance available after the "operations-related" contributions would be divided among various charitable interests of the two of us, on a basis roughly proportional to our ownership interest. If the manager of our company had some suggestions, we would listen carefully — but the final decision would be ours. Despite our corporate form, in this aspect of the business we probably would behave as if we were a partnership.

Wherever feasible, I believe in maintaining such a partnership frame of mind, even though we operate through a large, fairly widely-held corporation. Our Treasury ruling will allow such partnership-like behavior in this area.

Here's the procedure:

(1) About November 13th we will notify all beneficial owners, who also are owners of record, that "x" dollars per share are available for designated contributions. This year we are going to allocate $2 per share, or approximately $2 million if all shareholders participate. (If they do not, our total corporate contribution will decrease proportionately.) For example, if you own, and have registered in your name, 1,000 shares on November 13th you may direct us to make contributions totaling $2,000.

(2) Stockholders must let us know, in writing, by December 10th of not more than three charities to whom they wish contributions sent and the amount for each, if more than one charity is named. You will be asked to certify that such a contribution by Berkshire does not fulfill any outstanding personal obligation of yours or of your family. (This is necessary to conform with the Treasury ruling.) If any designated organization is not easily identifiable as a charity entitling Berkshire to a tax deduction, you must attach evidence that contributions to that organization are deductible under 170(c) of the Internal Revenue Code. Where such evidence is submitted any U.S. charity will qualify, including a private charitable foundation.

(3) During December Berkshire Hathaway will make the designated contributions in cash or appreciated securities. The recipient charities will be told, unless you request otherwise, that the contributions were made at your request.

Our decision as to "x" (or whether any contributions at all will be made) must be delayed until November each year so that we can make an informed estimate of our tax position and contributions base. In some years, though we may report substantial income and pay substantial income taxes, contributions would provide virtually no reduction in corporate tax. This apparent anomaly occurs because of intricacies in the tax law that I'm not sure I'm up to explaining. In those years we will not call for stockholder-designated contributions.

In the years when we do request such designations, amounts are likely to vary significantly. Your degree of participation in this plan and your comments about it will be important factors affecting whether and at what level we continue the program. We'll let you know in the annual report what the reaction has been.

Of course, even though this procedure is tax efficient, contributions still will result in cost to our shareholders (before considering hard-to-measure positive feedback effects benefiting Berkshire). Just because an item is tax-deductible doesn't mean that it's free. Very roughly, $2 million of contributions designated by shareholders will reduce our net income by about $1 million.

Here's some perspective on those numbers. If all shareholders participate in the 1981 program, our percentage gain in net worth for the year will be about ¼ of 1% less than otherwise would be the case. Historically, that gain has averaged over 20% per annum. This minor dent in our economic performance will allow us to make contributions totalling about 10% of those made in 1980 by Mobil Oil, the fifth largest American corporate donor.

Please particularly note that shareholders may participate only if shares are held in their own name on the November 13th mailing date. If your shares are held by a broker, a depository institution, or other nominee, you are urged to reregister these shares promptly in order to participate. If you are on the shareholder records on November 13th, you will hear from us about a week after that date with detailed instructions and a form to return. Holdings of all sizes will be eligible, right down to holdings of a single share (a species with which we are abundantly blessed).

I am pleased that Berkshire donations can become owner-directed. It is ironic, but understandable, that a large and growing number of major corporations have charitable policies pursuant to which they will match gifts made by their employees (and — brace yourself for this one — many even match gifts made by directors) but none, to my knowledge, has a plan matching charitable gifts by owners. I say "understandable" because much of the stock of many large corporations is owned on a "revolving door" basis by institutions that have short-term investment horizons, and that lack a long-term owner's perspective.

Large investing institutions and investment managers are required to file lists of their holdings quarterly with the SEC. The flip-flopping in positions revealed by many of these filings makes the adjective "investment" ludicrous as applied to these institutions and advisors. In such circumstances many corporate managers quite naturally will identify subconsciously more closely with employees' interests than with shareholders' interests. If a great many shareholders themselves do not think and behave like owners, it is understandable that managers will not think of them as owners.

Our own shareholders are a different breed. As I mentioned in the 1979 annual report, at the end of each year more than 98% of our shares are owned by people who were shareholders at the beginning of the year. This long-term commitment to the business reflects an owner mentality which, as your manager, I intend to acknowledge in all feasible ways. The designated contributions policy is an example of that intent.

Sincerely,

Warren E. Buffett

Berkshire Hathaway Inc.

DIRECTORS AND EXECUTIVE OFFICERS

WARREN E. BUFFETT, *Director and Chairman of the Board*
Chief Executive Officer of the Company

KENNETH V. CHACE, *Director*
President of the Company and Chief Operating Officer of the Textile Operations of the Company

MALCOLM G. CHACE, JR., *Director*
Retired, Former Chairman of the Board of Directors of the Company

J. VERNE MCKENZIE, *Director*
Vice President, Secretary and Treasurer of the Company

CHARLES T. MUNGER, *Director*
Vice Chairman of the Board of the Company
Chairman of the Board of Blue Chip Stamps

COMMON STOCK DATA

Shareholders
The Company had approximately 1,600 record holders of its common stock at March 5, 1982.

Market Prices
The common stock of Berkshire Hathaway Inc. is traded in the over the counter market and is regularly quoted in the NASDAQ System under the symbol BKHT. The high and low bid prices for stock in each quarter of 1981 and 1980 is set forth in the following table. The quotations represent prices between dealers and do not include retail markup, markdown or commission. They do not represent actual transactions.

1981	*High*	*Low*	*1980*	*High*	*Low*
First Quarter	485	425	First Quarter	340	260
Second Quarter	525	480	Second Quarter	320	245
Third Quarter	520	460	Third Quarter	400	300
Fourth Quarter	590	460	Fourth Quarter	475	375

Dividends
Berkshire has not declared a cash dividend since 1967. No change is contemplated in Berkshire's policy of investing its earnings in expansion of its businesses rather than paying cash dividends.

Berkshire Hathaway Inc.

SELECTED FINANCIAL DATA

(dollars in thousands – except per share amounts)

	Fiscal Year Ended Saturday Nearest December 31.				
	1977	1978	1979	1980	1981
Revenues of consolidated companies:					
Insurance premiums earned	$143,087	$186,073	$181,949	$ 185,187	$ 159,013
Interest and dividend income	16,796	24,293	30,440	38,966	49,189
Other revenues of consolidated companies	203,752	235,576	247,952	259,200	263,374
Equity in earnings excluding significant securities gains or losses of companies not consolidated:					
Wesco Financial Corporation	$ 5,715	$ 7,417	$ 8,784	$ 8,804	$ 7,120
Illinois National Bank*	3,550	4,242	4,960	4,731	—
Earnings:					
Earnings from continuing operations before realized investment gain	$ 19,922	$ 25,742	$ 30,961	$ 38,484	$ 39,723
Earnings from discontinued operations*	3,550	4,242	4,960	4,731	—
Earnings before realized investment gain	23,472	29,984	35,921	43,215	39,723
Realized investment gain, net — including equity in significant securities gains or losses of companies not consolidated	6,921	9,258	6,896	9,907	22,881
Net earnings	$ 30,393	$ 39,242	$ 42,817	$ 53,122	$ 62,604
Average shares of common stock outstanding — in thousands	1,038	1,029	1,027	1,027	986
Earnings per share:					
Earnings from continuing operations before realized investment gain	$ 19.20	$ 25.02	$ 30.14	$ 37.47	$ 40.27
Earnings before realized investment gain	22.62	29.15	34.97	42.07	40.27
Net earnings	29.29	38.15	41.68	51.72	63.47
Balance Sheet items (at end of Fiscal Year):					
Total assets	$646,678	$757,612	$892,265	$1,010,581	$1,157,911
Term debt	55,104	57,071	55,099	104,344	97,768
Minority shareholders' interest	47,926	48,520	52,097	59,851	70,416
Shareholders' equity — total	206,735	254,166	344,962	395,214	519,463
Shareholders' equity — per outstanding share	199.17	247.00	335.85	400.80	526.57

*The Company divested of its interest in the Illinois National Bank as of December 31, 1980. The Company's equity in earnings of that former subsidiary for years prior to 1981 is reflected above as earnings from discontinued operations.

1981

BERKSHIRE HATHAWAY INC.
Executive Offices – 1440 Kiewit Plaza, Omaha, Nebraska, 68131

1981