



## Buffett Turns Gloomy: The “Incredible Period” For The US Economy Is Coming To An End

### Description

While Warren Buffett’s insights on the economy are traditionally cheerful and uplifting – usually hitting at time of peak pessimism in the form of self-serving NYT op-eds or CNBC vignettes (and usually around the time the Omaha billionaire knows that the government will backstop his TBTF investments, unlike those of pretty much anyone else), on Saturday the head of Berkshire Hathaway had a far more downbeat and gloomy prediction for his own businesses – and the broader economy in general – the good times may be over.

Speaking at Berkshire’s annual general meeting in Omaha, Nebraska, the billionaire investor said he expects **earnings at the majority of the conglomerate’s operations to fall this year** as the coming economic downturn slows corporate activity further. He made his pessimistic comments even as Berkshire posted an almost 13% gain in operating earnings to \$8.07 billion for the first quarter, up from \$7.04 billion a year ago.

“The majority of our businesses will report lower earnings this year than last year,” Buffett, 92, said, before crowds of thousands at the event on Saturday according to Bloomberg. During the last six months or so, the “incredible period” for the US economy has been coming to an end, he said.

As Bloomberg notes Berkshire is often viewed as a proxy for economic health owing to the expansive nature of its businesses ranging from railroad to electric utilities and retail. Buffett himself has said Berkshire owes its success to the incredible growth of the US economy over the decades, **but his prediction for a slowdown at his firms comes as upheaval at regional banks threatens to curtail lending as inflation and higher rates continue to bite.**

Buffett’s long-time business partner Charlie Munger, 99, who joined him on stage, said the more-difficult economic environment will also make it harder for value investors, who typically buy stocks that look cheap compared to the intrinsic value of the businesses.

“Get used to making less,” Munger said.

Despite the broader pessimism, Buffett said he expects earnings at its insurance underwriting operations — which are less correlated to business activity — to improve this year. Berkshire already reported higher earnings at those businesses including auto-insurer Geico, which swung to profitability following six quarters of losses.

Geico posted \$703 million in earnings as higher average premiums and lower advertising spending contributed to the gain even as claim frequencies fell, Berkshire said in a statement reporting its earnings Saturday. That revival follows a difficult period for the underwriting business as inflation took its toll on the cost of materials and labor.

Geico has been facing particular pressure from rivals including Progressive, which Buffett has called “well-run,” and Allstate which had long used telematics programs to track drivers and encourage better behavior before Geico introduced the offering. Geico’s profit also helped Berkshire’s insurance underwriting businesses deliver \$911 million in profit compared with \$167 million a year earlier.

Berkshire previously said it expected Geico to return to operating profitability in 2023, after securing premium rate increases. Still, Geico remains an issue for Berkshire, with top line growth in the quarter of less than 1% that “significantly lags peers,” CFRA analyst Cathy Seifert said.

*“I suspect rate hikes being put through to offset claim cost inflation is being met with policy cancellations,” she said. “While the loss of unprofitable policies is not always a bad thing—that’s not usually the policies — and policyholders — that leave.”*

Other parts of the conglomerate took a bigger hit, **with after-tax earnings from Berkshire Hathaway Energy falling 46.3% from the same time last year amid “lower earnings from the US regulated utilities, other energy businesses and real estate brokerage businesses.”** Railroad results were also weaker than expected due to a fall in freight volumes and higher operating expenses, according to Edward Jones analyst Jim Shanahan.

But at one of Berkshire’s best known businesses, Brooks Running Co., Chief Executive Officer Jim Weber was skeptical of a steep consumer downturn.

*“With unemployment being so low, it’s hard to be believing we’re going to fall off a cliff into a recession at the consumer level,” Weber said in an interview on Friday ahead of the meeting. “I wonder if this is going to be an asset-value recession.”*

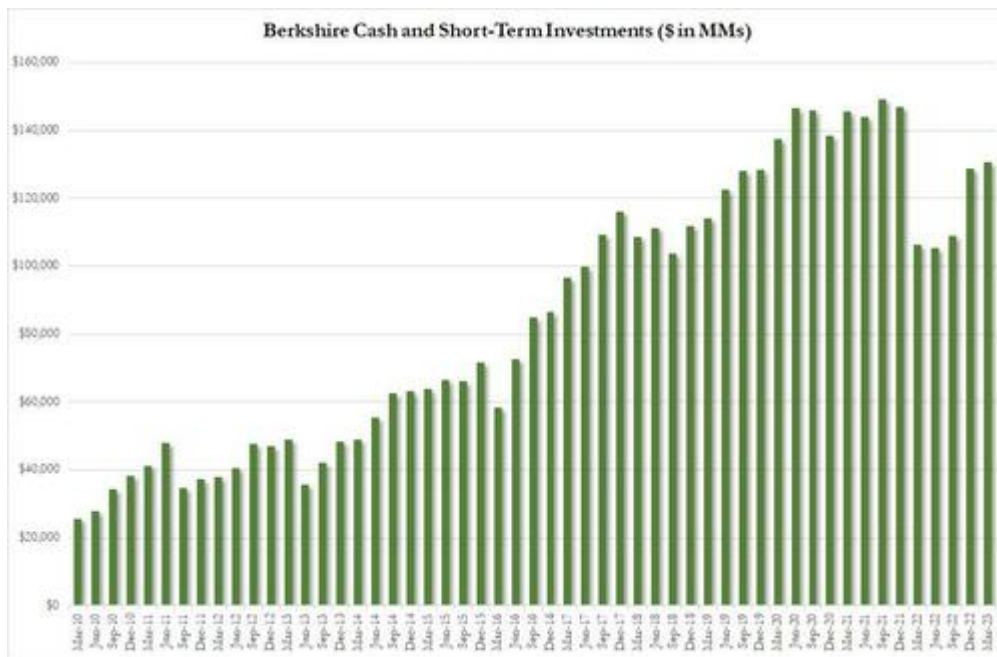
Among other topics discussed on Saturday were Buffett’s succession, the banking crisis, the US debt ceiling crisis, the company’s investment in Occidental, China’s upcoming invasion of Taiwan and more:

- **Succession planning:** Buffett named Greg Abel, 60, as heir apparent in 2021, and the vice chair for non-insurance operations has had a more pronounced presence ever since. On Saturday, Buffett reaffirmed he was “100% comfortable” with the decision and even indicated a largely business-as-usual transition, for whenever that could be. “Greg understands capital allocation as

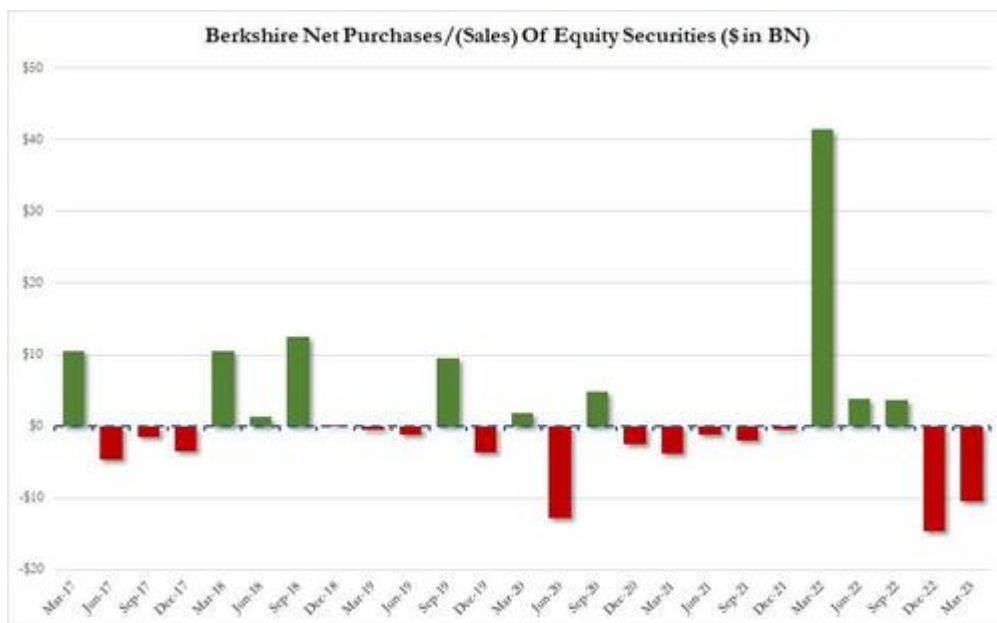
well as I do. That's lucky for us," Buffett said at the meeting in Omaha, Nebraska. "He will make those decisions, I think, very much in the same framework as I would make them. We have laid out that framework now for 30 years."

- **Occidental control:** One analyst called it the biggest announcement of the day: Berkshire won't make an offer for full control of Occidental Petroleum Corp., the energy firm it has spent months boosting its wagers on. The comment by Buffett likely helped temper speculation that Berkshire is seeking to own Occidental after winning approval from US regulators last year to acquire as much as 50% of the firm. Buffett didn't rule out buying more stock of the Houston-based firm, adding it may — or may not — seek further purchases.
- **Banking Turmoil:** Buffett and Munger were so sure they'd be questions about the recent banking turmoil that they jokily brought placards bearing the accounting classifications spotlighted during the upheaval. One was labeled "available for sale," while the other read "held to maturity." Striking a more serious note, Buffett faulted the executives in charge of the failed banks, arguing they should be held accountable for mistakes that were hiding in "plain sight." He also called out "messed up" incentives in banking regulation, as well as poor messaging by regulators, politicians and the press to the American public about the upheaval. Buffett pointed to First Republic Bank, the insolvent bank which last weekend was acquired by JPMorgan after it collapsed after offering jumbo, non-government-backed mortgages at fixed rates that were interest-only for 10 years in some cases — which Buffett called "a crazy proposition."... "It was doing it in plain sight and the world ignored it 'til it blew up," Buffett said.
- **Debt Ceiling:** As lawmakers race to resolve a standoff around the US debt ceiling, Buffett said he couldn't see how Washington would allow the US to default on its debt, an outcome that would tip the financial system into turmoil. Investors and politicians are zeroing in on whether or not the US government can avoid crashing into its statutory debt ceiling and a potentially catastrophic technical default that could follow. Despite the impasse, Buffett reiterated his belief in America as an "incredible society" with "everything going for us." Given the choice, he would still want to be born in the US, he said.
- **Geopolitics, Taiwan:** In Q4 Buffett slashed his holding of Taiwan Semi just months after disclosing a major stake in a quick reversal that spooked investors. Buffett said Saturday the company was one of the best managed and most important in the world, but that he didn't like the location — a reference to Taiwan amid rising tensions between the island and China. Buffett and Munger emphasized the need for smooth relations between the US and China and urged increased trade. While the two will be competitive, they will always need to judge "how far you can push the other guy without them reacting wrong," Buffett said.

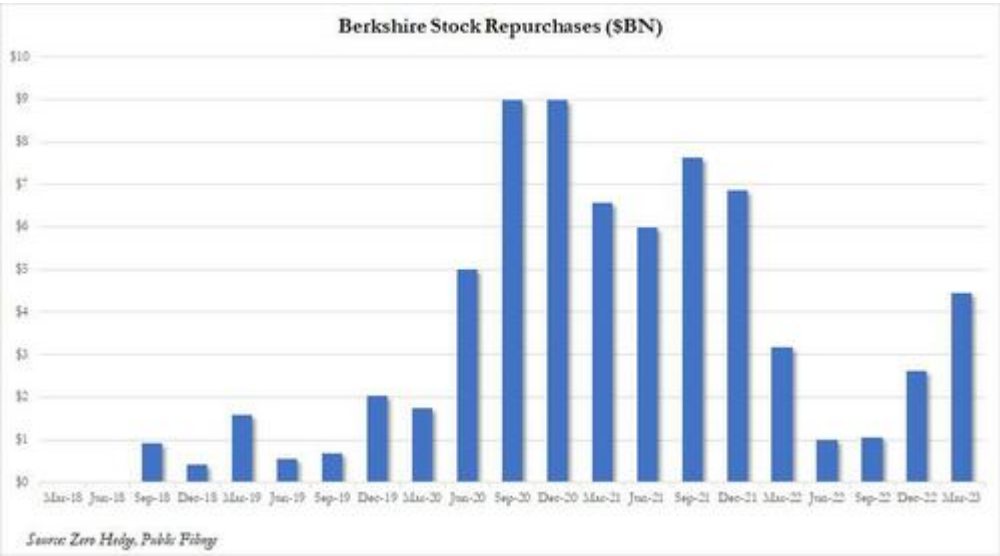
Separately, Berkshire topped up its cash pile, ending the quarter with \$130.6 billion, a \$2 billion increase from the \$128.6 billion at the end of the year. This means that Berkshire stands to make a bonanza from interest income as the Fed keeps hiking rates: *"Our investment income is going to be a lot larger this year than last year, and that's built in," Buffett said at the annual meeting.*



The company was also a net seller of equities for the second quarter in a row, pocketing \$10.4 billion in net stock sales (\$13.3 billion gross) after deducting purchases of \$2.9 billion.



Finally, Berkshire bought back \$4.4 billion of stock, an increase from the same period last year, as Bekrshire confronted turbulent markets that offered fewer of the blockbuster deals he's renowned for. Berkshire has turned toward buybacks more often as valuations in public markets had made it more challenging for Buffett to identify promising acquisitions.



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