Berkshire DIVIDEND STRATEGY

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"Casual Friday" Commentary

Casual Friday: Casual Friday: April Optimism + New Purchase: Bank Of America –
May 01, 2020

Good morning,
April provided much needed relief for equity investors. After the worst first quarter in decades, the S&P rebounded nearly 13% for the month. It's a welcome sign investors are willing to "bet on" beating the virus. There were a number of critical developments which justify optimism and potential higher stock prices:

- Coronavirus drug treatments have been showing positive results
- Treatment protocols are improving
- US policy makers have injected $5+ Trillion of stimulus into the economy
- The curve has "flattened", state restrictions are being methodically lifted
- Antibody tests are suggesting 10s of millions in US may have already been exposed
    - Stanford Study access: https://www.medrxiv.org/content/10.1101/2020.04.14.20062463v2

(Source: Bloomberg)

Q2 2020 - Dividend Increases:
Year to date, ten of our companies announced dividend increases. Several companies have reaffirmed their dividend commitments. Berkshire continues to conduct on-going analysis on dividend sustainability. While current visibility is low, we are comforted the majority of our companies have their current dividends well covered not only by earnings but by free cash flow.

Since the pandemic began, we've even had 3 companies raise dividends.

- Kinder Morgan Increases Dividend 5% - https://www.nasdaq.com/press-release/kinder-morgan-increases-dividend-five-percent-and-announces-results-for-first-quarter
- P&G Declares Dividend Increase 6% - https://www.nasdaq.com/press-release/pg-declares-dividend-increase-accelerates-third-quarter-2019-20-earnings-release-to
- Johnson & Johnson Increases Dividend 6.3% - https://www.nasdaq.com/press-release/johnson-johnson-announces-dividend-increase-of-6.3-2020-04-14

Portfolio Change:
We recently added **Bank of America (BAC)** to the portfolio. We believe the company offers a relatively safe dividend yield of 3%, attractive dividend growth potential (long term) and low valuation thanks in part to the Covid-19 pandemic. We believe this upgrades our bank portfolio as we purchased BAC with the proceeds from the sale of **Bank of Montreal (BMO)**

CEO Brian Moynihan took over arguably the biggest mess following the 2008 financial crisis and quietly, but steadily reshaped the bank. His strategies have worked, as evidenced by solid financial metrics even as the bank has a lower risk profile.

BAC is now a simpler, more efficient organization. Non-essential, higher risk businesses

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Dividend Highlights

- Dividend growth can often provide transparent insight into a company's fundamentals and vitality.
- Dividend growth can provide an attractive stream of increasing cash flow to satisfy many financial objectives.

have been shed. BAC's focus is now on basic banking services: deposit gathering, business and consumer loans, mortgages, credit cards, wealth management, and capital markets. Unlike the "bad old days" of Ken Lewis, the bank doesn't feel it needs to chase returns in every hot business line. Fewer business lines mean better scale, focus and a lower cost structure. The bank has invested in technology, using big data and AI tools to run the bank and enhance the customer experience. Loan underwriting standards are higher. Leverage is down and the bank's capital position is as strong as its ever been.

Yet despite a more conservative profile, shareholders have been rewarded under Moynihan's management of the bank and its balance sheet. The stock price climbed substantially out of the financial crisis. Return on tangible common equity slowly climbed from negative in 2012, to a peak of around 13% in 2019, outpacing many of its peers, and not too far behind even JPMorgan. And it has done so with excess capital on the balance sheet. But, in recent years BAC has returned a massive amount of capital to shareholders, buying back nearly $30 billion of stock in 2019. The dividend is important for our strategy. Coming into 2020, the company grew the dividend 31% over the past three years. We don't expect a dividend increase this year, but we believe the relative safety of the dividend has potentially increased as a result of the pandemic. Like other banks, it suspended its buy-back program which represented 75% of the capital plan, with dividends making up the other 25%.

Currently, the bank and the industry face the challenge of low interest rates. BAC is hurt more relative to peers from lower rates, but does have other levers (fee income, capital and wealth management) to offset lower spreads. Loan losses from Covid-19 are also an industry wide challenge. This time around, banks are part of the solution, having strong balance sheets, and the ability to extend credit to their customers when it's needed most. Provisioning may be very high, but manageable, in our opinion thanks to prudent reserve policies. Energy loans represent only 2% of BAC's loan book, which is relatively low among the big U.S. banks.

We believe BAC was extremely well positioned to grow its dividend heading into the pandemic and the recent decline presents opportunity. Dividend growth will likely pause the next 6-12 months, but as the pandemic eases, we believe BAC will return to growing earnings and dividends for years to come.

Have a great weekend!
Gerry,

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major industries. Russell 1000 Growth Index measures the performance of those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values. The index was developed with a base value of 200 as of August 31, 1992. Russell 1000 Value Index measures the performance of those Russell 1000 companies with lower price-to-book ratios and lower forecasted growth values. The index was developed with a base value of 200 as of August 31, 1992. You cannot invest directly in an index. BEst (Bloomberg Estimates) Earnings Per Share (EPS Adjusted) estimate returns Earnings Per Share from Continuing Operations, which may exclude the effects of one-time and extraordinary gains/losses. Beta is a measure of volatility vs. an index. Upside/Downside capture ratios refer to a portfolios performance as a percentage of either positive returns (upside) or negative returns (downside) vs. an index. Standard Deviation is a measure of total risk. Alpha, Beta and capture ratios are represented as calculated by Morningstar.

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