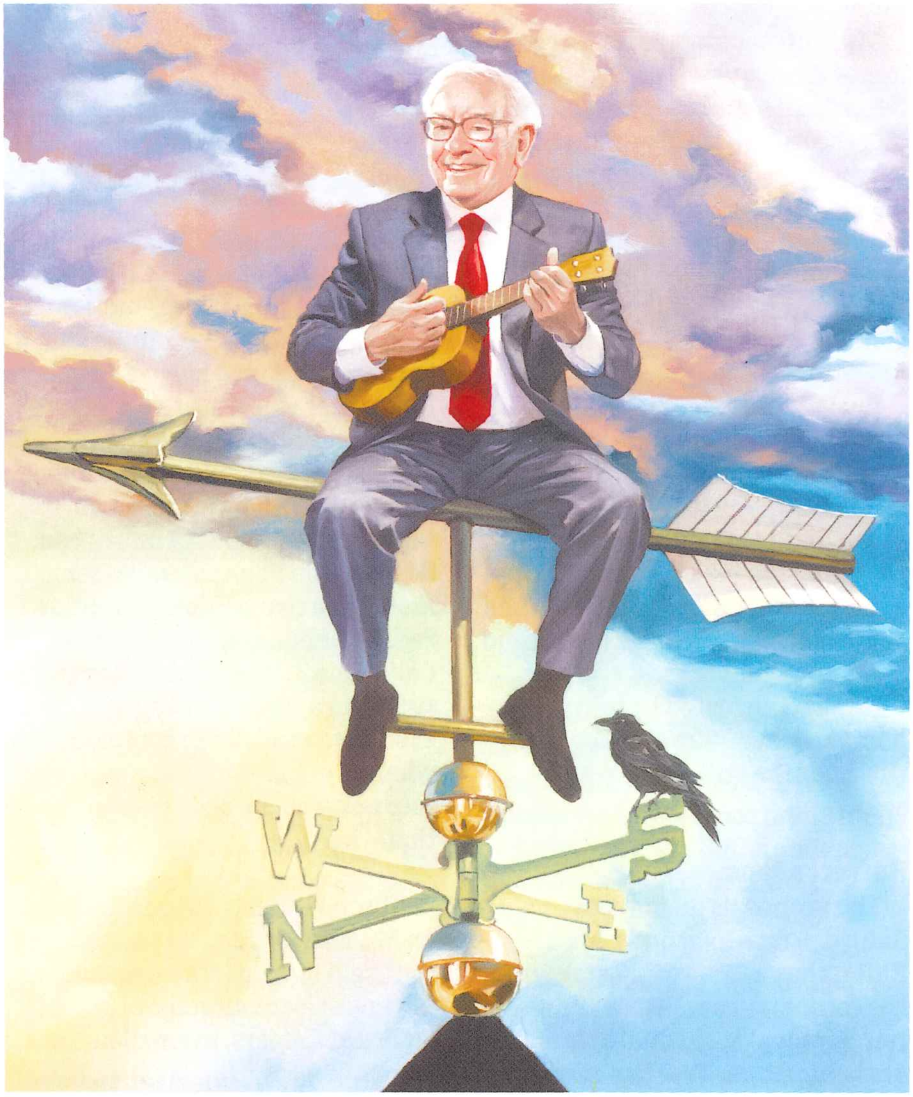
THE WALL STREET JOURNAL.

SATURDAY/SUNDAY, APRIL 30-MAY 1, 2022

Buffett Faces the Winds of Change

The Oracle of Omaha, at 91, sits atop a conglomerate that is outperforming the S&P 500 and earning record profits. Yet some shareholders want him to cede more control.

BY AKANE OTANI



ROBERTO PARADA

Berkshire Hathaway Inc. posted its best earnings in its history last quarter. Its stock is trouncing the S&P 500. And Warren Buffett's star power seems to be as strong as ever.

More than 40,000 people are expected to descend on Omaha, Neb., this weekend for Berkshire's first in-person shareholder meeting since 2019. They will be traveling hundreds, and in some cases, thousands of miles just to have a chance to hear from the famed "Oracle of Omaha," who turned 91 in August.

But even as Berkshire thrives, it is contending with an unusual number of big challenges.

The nation's largest public pension fund, California Public Employees' Retirement System, plans to back a shareholder proposal that would oust Mr. Buffett, who is both chief executive and chairman of Berkshire, from his chairman role. The proposal's backers argue that companies are better off when different individuals fill the two roles. Asset manager Neuberger Berman is supporting another proposal that demands Berkshire disclose data on climate-related risks across its businesses. Three giant institutional shareholders, BlackRock Inc., Vanguard

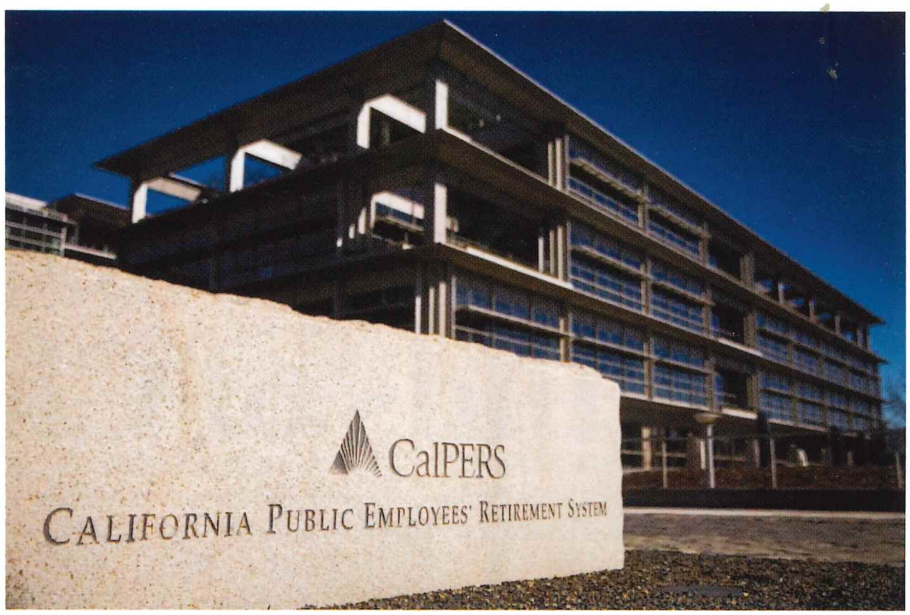
Group and State Street Corp., backed a similar measure last year.

Mr. Buffett also faces other questions: what to do with an enormous pile of cash amassed over the last decade, how the company will operate when he is no longer at the helm and whether he is doing enough to adapt to a changing investment world where funds are pouring into new types of assets such as cryptocurrencies. All these pressures are building at a difficult time, as central banks dial back their support for the economy and markets get more volatile.

Mr. Buffett didn't comment on any of these questions ahead of Saturday's meeting. At past gatherings, he said Berkshire had a proper succession plan in place and that he had every bit of confidence in his lieutenants. Mr. Buffett said to shareholders in his latest annual letter that he had struggled to find companies that met his criteria for long-term ownership.

During the pandemic, he kept traveling to a minimum. He told ex-CBS News anchor Charlie Rose in an interview in April that he took two plane flights in two years, once to see his sister. He said is still happy in his job even though he can't read or crunch numbers as fast as he did in his younger years.

He also suggested he is in no hurry to leave. "I'm still in overtime, but I'm still out there," he said.



A view of California Public Employees' Retirement System headquarters in Sacramento, Calif.
PHOTO: MAX WHITTAKER/REUTERS

Buffett's fans

The proposals up for vote Saturday face long odds. Mr. Buffett has a 32% voting stake in the company, as well as a legion of fiercely loyal individual shareholders behind him. That has allowed Berkshire, which is recommending that investors vote against the proposals, to strike down similar measures in past years.

The National Legal and Policy Center -- which filed proposals calling for board independence not just at Berkshire but also at Goldman Sachs Group Inc., Coca-Cola Co., Mondelez International Inc. and Salesforce.com Inc. -- argues that a corporation's governance structure is stronger when the two roles are held by different individuals.

It has support from a retirement system, known by its acronym Calpers, that oversees more than $450 billion in investments for more than two million current or retired public employees across California. Calpers said it generally supports a separate chair and chief executive at all of the companies where it owns stock because corporate governance is more effective that way.

"Our position is not a reflection on Mr. Buffett's acumen as an investor," said Simiso Nzima, managing investment director of global equity at Calpers, in emailed comments.

Berkshire's board said in its response to the proposal that it agrees the two roles should be split -- just not while Mr. Buffett is chief executive. Once Mr. Buffett steps aside, the board intends on naming a nonmanagement director to be its chair. Mr. Buffett has said his son, Howard, will succeed him as chairman.

Companies have increasingly moved toward making their boards more independent, making Berkshire an outlier -- though by no means the only one. Last year, 59% of the companies in the S&P 500 had a separate chair and chief executive, according to Spencer Stuart, an executive and board recruiting firm. That is up from 55% in 2021 and 41% in 2011.

Academic research on the matter has been mixed. One study from Indiana University's Kelley School of Business, for instance, found splitting the roles helped companies if they were struggling but actually hurt them if they were already doing well.

Mr. Buffett's longtime followers have seen variations of this fight play out before. They are familiar with complaints that Berkshire -- whose head office counts roughly two dozen employees and has no formal press or investor relations employees -- is too opaque. Mr. Buffett doesn't hold meetings with institutional investors to try to curry favor with them. Nor does he set aside special time with sell-side analysts covering the company.

But investors say their faith in Mr. Buffett runs so deep that they couldn't care less about all that.

The first stock Paul Lountzis, president of Lountzis Asset Management, bought when he founded his firm in 2000 was Berkshire. This weekend will mark what he estimates is his 32nd or 33rd Berkshire shareholder meeting. (It is hard to keep count.) When he spoke to The Wall Street Journal from his office, he sat facing bobbleheads of Mr. Buffett and right-hand man Charlie Munger and in front of a portrait of the two men together.

"I think they're smoking too much cannabis out there," he said in jest about Calpers, the pension fund pushing for an independent board chair.

To Berkshire's longtime investors, Mr. Buffett's track record speaks for itself. Between 1965 and 2000, Berkshire produced 20% compounded annualized gains. The S&P 500 returned 10.2% including dividends over the period.

That is why, Mr. Lountzis said, Berkshire remains his firm's biggest equity holding -- and why he thinks that, even at 91 years old, Mr. Buffett is completely capable of continuing to wear both hats.

"What Warren has done so well over so many years is create shareholder value. And that's ultimately the most important thing," said Ryan Kelley, chief investment officer of Hennessy Funds, which holds Berkshire shares in its large-cap financial fund.

All that cash

A more pressing issue for Berkshire? What to do with its enormous pile of cash.

Berkshire had a near-record $144 billion of cash and equivalents at the end of last year, excluding

Paul Lountzis, president of Lountzis Asset Management. Berkshire remains his firm's biggest equity holding. PHOTO: PAUL LOUNTZIS

what it held at its freight railroad and utilities businesses. That is far more than Mr. Buffett and his investors would prefer. In fact, Mr. Buffett wrote to shareholders in February, he'd prefer to keep 100% of his net worth in equities.

The problem? He was struggling to find anything he felt was worth buying and holding for the long run.

"These periods are never pleasant," Mr. Buffett said in his February letter.

Since that letter, Berkshire has put some cash to work. In March, it reached an agreement with Alleghany Corp. to acquire the insurer for $11.6 billion. In April, Berkshire unveiled it had built a roughly $4.2 billion stake in HP Inc.

Investors are itching to see Mr. Buffett make some big moves. "Are there still places Warren can find value? I'm curious to hear his thoughts," Mr. Kelley said.

Hot-button issue

Another pressure point for Berkshire is how it is handling climate change. Two separate shareholder proposals ask Berkshire to disclose how it manages climate-related risks across all of its businesses, as well as to share whether it will begin measuring and publishing the greenhouse-gas emissions associated with its insurance operations.

It is far from the only company that activist investors are targeting. Investor advocacy groups say climate change is the No. 1 issue among the record number of shareholder proposals that have been filed so far this year.

Berkshire's board said in its response to the shareholder proposal that the vast majority of its greenhouse-gas emissions are generated by two businesses, Berkshire Hathaway Energy and freight railroad BNSF. It sees no need to disclose information about all of its units, which include businesses as varied as jewelry retailer Borsheims, clothing manufacturer Fruit of the Loom, paint manufacturer Benjamin Moore & Co. and See's Candies.

Both Berkshire Hathaway Energy and BNSF have publicly committed to reducing their carbon footprint over the coming years. The former is aiming to achieve net-zero greenhouse-gas emissions by 2050; the latter is aiming to cut emissions by 30% by 2030 from 2018 levels.

Neuberger, a big asset-management firm based in New York, said in a statement explaining its support for a proposal that the company could improve its disclosures "given the importance of the topic."

Ultimately, Mr. Buffett might not have a choice. In March, the Securities and Exchange Commission formally proposed requiring publicly traded companies to report the greenhouse-gas emissions generated by their businesses, as well as from the energy they consume. Regulators haven't made the rule final.

Berkshire without Buffett

If Berkshire seems stuck in its ways, that is likely partially a reflection of Mr. Buffett's approach to investing. It is slow. It is deliberate. And it hasn't really changed over the decades.

Some of his critics take issue with his reluctance to venture into newer, highly volatile investments. Billionaire venture capitalist Peter Thiel said at a bitcoin conference in April that Mr. Buffett is part of a "finance gerontocracy" keeping cryptocurrency prices from taking off further, along with JPMorgan Chase & Co. Chief Executive Jamie Dimon and BlackRock Inc. Chief Executive Larry Fink.

Yet as markets have swooned this year, Mr. Buffett's value approach is back in fashion as money managers seek areas of the markets that can ride out a more volatile environment. Whether that type of outperformance can continue when Mr. Buffett is no longer at Berkshire's helm is up in the air.

Berkshire has a succession plan in place. Mr. Buffett has tapped Vice Chairman Greg Abel, 59, who manages all of Berkshire's noninsurance operations, to ultimately succeed him as chief executive.

Meanwhile, portfolio managers Todd Combs, 51, and Ted Weschler, 59, are expected to run the company's massive investment portfolio by themselves once Mr. Buffett departs the job. Although Mr. Buffett still controls much of the portfolio himself, Mr. Combs and Mr. Weschler had "total authority" over $34 billion of investments as of the end of 2021, Mr. Buffett wrote in his February letter.

"They're setting themselves up for a good transition," Mr. Kelley said. Combined with the fact that Berkshire largely leaves its subsidiaries to manage their day-to-day operations, the company will likely continue to be a well-run collection of businesses even when Mr. Buffett is no longer around, he said.

What's less easy for investors to figure out is how much of Berkshire's cachet disappears when Mr. Buffett, a bona fide household name, is replaced by men far fewer people know.

That is a question likely to be left unanswered at this weekend's shareholder meeting.

"There's nobody else like him. Period," Mr. Lountzis said.