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QV Investors Inc.

Money Making Performance

Some of us arrived at the office a little late Monday morning. Each one of us had our favourite moment from the most riveting entertainment event of the year. Mine was when ~~Leonardo DiCaprio~~ Warren Buffett received the award for Best Compounding Machine. Yes, that's right, Berkshire Hathaway – a holding in our Global Equity Fund – released its annual report this past weekend. Whether a Berkshire shareholder or just a student of investing, Buffett's annual letter offers wisdom for all.

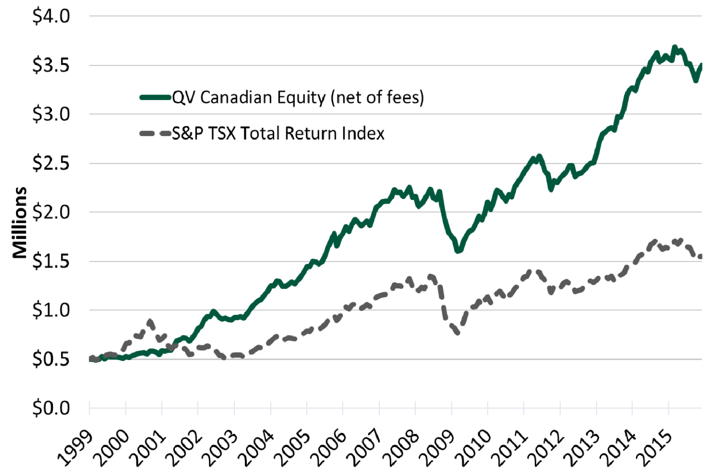
Berkshire's outstanding track record starts with operational excellence at its subsidiaries and investment holdings. A noteworthy advantage to Berkshire's conglomerate structure is having a master capital allocator at the helm. Given his history of decision making, we are content with Buffett reinvesting Berkshire's free cash flow rather than paying a dividend. After all, Buffett has grown Berkshire's book value per share at the compounded rate of 19.2% per year since 1965.

Going forward, Berkshire plans to improve the earnings power of its subsidiaries through organic growth and by its subsidiaries making small "bolt-on" acquisitions where accretive. Occasionally Berkshire will make sizeable acquisitions, like the purchase of Precision Castparts earlier this year. Finally, and only when the price is right, Berkshire will create value by transacting directly with shareholders.

Buffett re-iterated his long-standing intention of repurchasing shares should they sell as low as 120% of book value. At this price, Buffett states, shares trade at a significant discount to their intrinsic worth, and their repurchase therefore instantaneously creates value for shareholders. Our investment in Berkshire is attractive at its current price of 130% of book value.

An investment of $1,000 of Berkshire in 1965 would be worth about $15 million today. Buffett's performance is worthy of two Lifetime Achievement Awards. Indeed, the wealth that Buffett has generated in his fifty-one years at Berkshire would have taken over a century if invested at the corresponding rates earned by the S&P 500.

Over the past twenty years we at QV have been managing our own compounding machines, building wealth by managing risk. A $500,000 tax sheltered investment in our Canadian large cap strategy on January 1, 1999 would have grown to $3.4 million by December 31, 2015 (solid green line in the chart below). The same amount invested in the TSX would be worth only $1.5 million (grey dotted line).



Source: QV Investors Inc. & Bloomberg

In order to benefit from our risk-managed investing style, however, you needed the discipline to avoid tragedies such as the tech bubble.

Through the late 1990s the prominent investment strategy for Canadian investors was "go long Nortel", when a better script may have been inspired by "The Big Short". At the time, we favoured consumer staples, utilities and telcos, then trading at attractive valuations but widely ignored because they were boring. It would take considerable time before the wisdom of our actions was rewarded by Mr. Market. And if time is the friend of compounding then impatience is its enemy. Furthermore, being a bit early to the party is a classic trait of value investors. Although as Howard Marks – another great investor – points out, being early can sometimes be indistinguishable from being wrong.

To get long-term results like those in the picture above, you need a terrific script (buy high quality businesses at attractive prices) and a talented cast who demonstrate patience and discipline. At QV we have both. Managed Risk Investing plays all day at Livingston Place in Calgary. We hope you enjoy the show.