To Our Stockholders:

Consolidated operating income (i.e., before all net gains from sales of securities, mortgages and important fixed assets) for the calendar year 1982 increased to $22,241,000 ($4.30 per share) from $20,895,000 ($4.03 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 $45,342,000 ($8.76 per share) from $27,626,000 ($5.33 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 fin 000s except for per-share amounts):

Net operating income (loss) of

Year ended about	See's(1)	Mutual Savings(2)	Steel Business	Buffalo Evening News(3)	All other net income(4)	Net gains on sales of securities & fixed assets(5)	Blue Chip consolidated net income
December 31, 1982	$12,217	$3,296	$276	$(598)	$7,050	$23,101	$45,342
Per Blue Chip share	2.36	.64	.05	(.11)	1.36	4.46	8.76
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

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 year 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 but 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 1982 a net adjustment of Blue Chip's stamp liability account in the amount of $339 or $.07 per Blue Chip share, net of taxes, as explained below under "Promotional Services Business and Miscellaneous Sources of Operating Income."
5. The 1982 figures comprise $(1,943) or $(.38) per Blue Chip share attributable to Mutual Savings' sale of mortgage-backed securities at a loss, as explained below under "Mutual Savings and Loan Association," and $25,044 or $4.84 per Blue Chip share of net securities gains realized by the various entities 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 have taken 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 have tried 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 have made 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. We see no more advantage in avoiding repetition in basic information documents like letters to shareholders than, say, in successive editions of a service manual for a slowly-changing engine.

We have no illusion that our type of repetitive annual report, restricted to letters and figures in black and white, represents an optimum. We recognize that the invention of graphs and color pictures improved communication, yet we continue in our own way because it seems adequate in our special case, is cheaper, and is less associated with financial public relations practices we prefer not to emulate.

SEE'S CANDY SHOPS, INCORPORATED

The earnings of our 100%-owned subsidiary, See's Candy Shops, Incorporated, increased 13.8% last year, a respectable performance considering the general state of retailing in the 1981-1982 recession. We have now owned See's for exactly 11 years. Comparative figures for See's for the entire 11-year period of our ownership are set forth below:

Year ended about	Sales	Profits after taxes*	Number of pounds of candy sold	Number of stores open at year end
December 31, 1982	$123,662,000	$12,661,000	24,216,000	202
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	2,332,000	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 arising 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 Chip.

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 decreased 1.0% despite the impact of additional stores. Shops operating throughout both years registered a a greater decrease in poundage of 2.3%. Ingredient costs per pound decreased slightly, the first such decrease in years, but other costs increased sharply. The failure to control these other costs so as to more closely match inflation prevented an earnings increase which, considering the favorable trend in ingredient costs, otherwise would have been greater than the 13.8% reported.

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 eleven 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 and 1982 by a subnormal increase followed by a decrease 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 of affairs 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 See's 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 1982, the portion of Blue Chip's consolidated net worth represented by its interest in See's amounted to $50.5 million and included liquid assets more than adequate to finance See's substantial annual build-up of pre-Christmas inventories. Obviously, based on See's 1982 earnings of $12.7 million, this investment in See's is worth considerably more than its carrying value in Blue Chip's consolidated balance sheet.

Last year we stated that See's would try again to increase earnings in 1982 and that a modest increase was quite conceivable. This same statement now seems appropriate with respect to 1983.

MUTUAL SAVINGS AND LOAN ASSOCIATION

Our equity in Mutual Savings' operating income declined slightly in 1982 to $3,296,000 from $3,393,000 in the previous year.

The 1982 operating income equity of $3,296,000 is before deduction of Blue Chip's $1,943,000 share of an after-tax loss from Mutual Savings' sale last year of mortgage-backed securities. This special loss contribution of $1,943,000 has been included, instead, in computing "Net Gains on Sales of Securities, Mortgages and Important Fixed Assets," the final category in our earnings breakdown for purposes of this letter.

Earning any operating income at all was an achievement because in 1982 almost all other savings and loan associations suffered operating losses. The generally poor results 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. 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, including a massive sale of branch offices, has been that Mutual Savings has continued to earn a modest amount of operating income 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 (7.4% per annum at the end of 1982). The 1982 operating income 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 1982 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 as interest rates were rising, 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, although industry conditions are now considerably improved from their worst state, due to a substantial decline in interest rates incident to recession.

What Mutual Savings has left is a less-than-mediocre business in terms of the return it earns on the capital it employs. As it keeps its books it had $46.2 million in shareholders' equity at the end of 1981, on which its operating income was of less-than highest quality and amounted to only $3.3 million in 1982, or at the inadequate rate of 7.1% per annum. (The operating income was of less-than-highest quality because it came largely from tax savings through inclusion in its parent's consolidated income tax return, and such income, while real, has less cushion in reserve against future adversity than the highest quality income on which full income taxes have been paid in cash and are recoverable from the IRS in the event of future losses.) However, as Blue Chip reports earnings from its equity in this less-than-mediocre business, the results are considerably 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 1981 Blue Chip's equity in Mutual Savings was carried in Blue Chip's consolidated balance sheet, net of minority interest, at $18.2 million, and this equity contributed $3.3 million to Blue Chip's consolidated operating earnings in 1982, or at the rate of 18.1% 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.

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	Blue Chip's share of the cash dividend paid by Mutual Savings during the	Annual percentage return on Blue Chip's equity from the Mutual Savings

	sheet	year	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
1982	20,965,000	801,000	3.8

This table pretty well reflects the essence of real, and on balance quite favorable, economic effects on Blue Chip shareholders caused by Blue Chip's acquisition of a large interest in Mutual Savings.

In last year's letter we reported that we expected Mutual Savings to pay no dividend at all in 1982. Instead, despite the loss from an unusual sale of mortgage-backed securities, a modest 1982 dividend was paid, as reflected in the table above, and we now guardedly forecast a larger dividend from Mutual Savings in 1983. Any increase would be welcome, because the present dividend return on Blue Chip's carrying value of its investment is inadequate, and not in any small degree.

Operating a savings and loan association under the more competitive conditions which will almost surely prevail in the future as a consequence of deregulation of rates of interest paid to savers is going to present a challenge which, so far, we haven't fully figured out how to meet. We are sobered by the examples of deregulation effects presented by trucking companies and airlines, and by the possibility of shocks to the whole bank/savings and loan system which now appear more conceivable than at any other time after World War II. National legislators in both political parties, pressured by our financial institutions, have recently augmented the hermaphroditic part of the bank/savings and loan system, where deposits are insured (in effect) by the U. S. Treasury while interest rates paid to depositors on those deposits can be (roughly) whatever an insured institution decides to pay. We hope we are wrong in foreseeing, from the recent changes in the system, increased encouragement of what in the long run will be unsound practice by institutions needing encouragement in precisely the opposite direction.

We do have one central determination: to preserve a lot of options by retaining financial strength and by remaining very flexible with respect to expansion (including acquisition), contraction and revisions of services designed to create more differentiation in the market place from standard financial services provided by others.

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 more 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. Our 80% share of the price was thus about $12 million. 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 $276,000 to our consolidated net income in 1982 compared with $1,560,000 in 1981. The decrease in earnings was caused by a continuation of (1) severe recessionary conditions in the steel industry, and (2) effects of a business mistake, now corrected at substantial cost, namely entry into a small measuring-tool distribution business, closed down in 1982.

Even under recessionary conditions operations remain profitable, and we anticipate at least some improvement in earnings for 1983.

The minimum shareholders' equity, at Blue Chip's carrying value per unit of equity, required to own and operate 100% of Precision Steel's business at its 1982 level is about $13 million on which the business earned $.3 million in 1982 or at a very inadequate rate of 2.3% 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.

After acquisition, as above reported, Precision Steel's earnings have been a disap-pointment, but its facilities and balance sheet remain in first-class shape.

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 1982 annual report. Simply make your request to:

Wesco Financial Corporation
315 East Colorado Boulevard
Pasadena, California 91109
Attention: Mrs. Jeanne Leach, Treasurer

BUFFALO EVENING NEWS, INC.

The operating loss, before taxes, of our 100%-owned newspaper subsidiary, Buffalo Evening News, Inc., in 1982 was higher than that of 1981, increasing marginally to $1,270,000 from $1,091,000 in the previousy ear Thus the surface indication from our newspaper figures for the full year 1982 would app. ear to be that we were correct last year when we stated with respect to the News: "We confidently predict a lack of improvement [in the News' 1982 operating figures]. We anticipate terrible market conditions for the News in 1982."

However, the underlying reality as we enter 1983 is quite different from the poor situation forecast in last year's letter to stockholders. What we failed to foresee last year was the business failure of the Courier Express, the News' most important competitor in Buffalo, which ceased publishing its newspaper on September 19, 1982, leaving the News as the only area-wide metropolitan daily newspaper in Greater Buffalo, New York.

Before the failure of the Courier Express the News and its employees were locked into an intense survival struggle in a recession-plagued market (albeit a fine city). The outcome of this struggle was always uncertain. Now the economic prospects for both the News and its employees are improved from the extremely hazardous state which formerly existed. Indeed, profits were earned in November and December of 1982 adequate to offset a major portion of extraordinary costs and losses incident to circulation-building, including start-up of the News' first weekday morning edition, after the Courier Express stopped publishing in September. We now expect the News to be profitable for the full year 1983. Our eventual target is a 10% margin on sales after taxes, and we hope to be well over halfway to this target in 1983. Our target return on sales is somewhere close to the norm for newspaper operations like the News.

We will not here repeat in detail our long account of the competition and litigation in Buffalo between the News and the Courier Express. That chapter has ended. Shareholders who wish to refresh their memories should read the section about the News in last year's letter. Highlights of an up-dated history from our acquisition of the News in 1977 through year-end 1982 are as follows:

1. We purchased the News for about $34 million in April, 1977.
2. The News lost about $12 million, before taxes, after our acquisition and through December 31, 1982.
3. The after-tax effect of these losses reduced the carrying value of our News subsidiary in our consolidated balance sheet to about $28 million at the end of 1982. (In addition, of course, we have realized no return at all for a great many years from employment of the $34 million originally expended in buying the newspaper, and we would have realized a substantial and compounded return if we had invested the money elsewhere.)

4. However, the newspaper which we owned at the end of 1982 is a much better business operation than the newspaper we purchased in April of 1977. The following comparisons indicate the rough dimensions of change at the News:

	In April, 1977	**At 12/31/82**
Weekday circulation	279,000	323,000
Saturday circulation	300,000	271,000
Sunday circulation	-0-	354,000
Estimated revenues for next 12 months	$43,000,000*	$85,000,000+

- Represents approximate actual revenues for twelve months beginning April 1977.

As this is written, the News ranks 21st among the nation's daily newspapers in weekday circulation, which was about 321,000 in February, 1983. At the same time Sunday circulation was about 367,000. Notwithstanding economic decline in Buffalo the present Sunday circulation of the News is 95,000 higher than the 272,000 Sunday circulation of the Courier Express in 1977 when it alone published a Sunday edition!

Plainly, considering the ambitions of other publishers to add to their newspaper holdings, the News could now be sold for considerably more than the amount at which it is carried in Blue Chip's consolidated balance sheet. However, we have no interest in selling. We are proud of the News and of our association with its people — including Henry Urban, Stan Lipsey, Murray Light, Clyde Pinson, Dave Perona, Dick Feather and many more — who have led the News to its present position. We are proud, too, that we have nourished as well as we have the journalistic tradition we inherited from the News' legendary Editor, Alfred H. Kirchhofer, predecessor to Murray Light. We hope to be better known as the years pass as good stewards of good traditions, as we believe we have been at both the News and See's.

Although the News is now a much stronger economic operation than it was last year, it nonetheless occupies no bower of roses, for the following reasons, among others:

1. Metropolitan newspapers as a group have lost advertising market share to electronic media in recent years. Newspaper publishing is inherently a very intense user of resources, energy and human time, compared to many other media, the influence of which is growing, assisted by rapidly improving technology. Newspaper costs have escalated more rapidly in some recent years than utility to advertisers, particularly at some large, old newspapers. One cause is newspaper inability, because of provisions in labor contracts, to realize anything like the full reduction in various costs possible with modern automation, while competitors not so restricted gain full benefits from technological change.

2. Competition from free publications and suburban newspapers has increased in vigor.

3. Retailing has increasingly been concentrated in chain-store operations which have learned how to deliver advertising circulars without using newspapers and often do so when dissatisfied with newspaper run-of-press or pre-print advertising rates.

4. Buffalo has suffered and continues to suffer from far more than its share of the national recession. Unemployment has been as high as 15.3%, and many large and important retailers have gone out of business, shrinking the total amount of advertising available to newspapers by millions of lines per year. It was this extreme Buffalo-area business decline, plus general conditions making it difficult or impossible for two competing newspapers to survive, even in cities with above-average prosperity, which combined to cause Buffalo to become yet another American city with only one area-wide metropolitan newspaper. As things worked out, the News may well have realized some advantage as well as disadvantage as recent, above-average business misery in Greater Buffalo contri-buted to the disappearance of a major competitor. But any continuation of local business decline from this point will be a pure curse for the News. All managers know that it is easier to keep both owners and employees happy in a business in an expanding market, instead of a declining one. Shrinking-pie division is usually more troublesome and controversial than expanding-pie division.

These are not small problems, and in a few other cities (some more prosperous than Buffalo) without economic competition between two area-wide metropolitan newspapers, we surmise that little or no profit is now being earned by the metropolitan newspaper operation.

Finally, our shareholders should recognize that if our 1977 purchase of the News has now worked out acceptably from their viewpoint, which contrary to our prediction last year may now be true even after taking into account time delays, the conclusion does not follow that we made a sound managerial decision buying the News when we did for the price we paid. In retrospect, we were strongly influenced because we liked the newspaper, its people and the city, and we may simply have gambled shareholders' money against the odds and won. Our stewardship may have been, at best, dubious in this instance. We know that the financial outcome we now report could with slightly different breaks just as well have been either (1) a large loss on closure of the News or (2) the expectation of much more money-losing in continued operation, as part of the only defensive strategy with reasonable prospects.

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 slightly increased profit, after parent company interest and other general expense and income taxes, last year, up to $4,212,000 from $3,659,000 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 (1) "float" caused by trading stamps issued but not yet redeemed plus (2) a reasonable amount of shareholders' equity capital. Our shareholders should not be encouraged by the increase in after-tax profit, which was attributable in part to the fact that favorable revisions in our estimates of our liability to redeem outstanding trading stamps were made in 1982 but not in 1981 and in part to increased shareholders' equity capital. The revisions in redemption liability, which by their nature will not frequently recur, increased 1982 after-tax profit by $339,000.

Moreover, as we forecast in last year's letter, trading stamp service revenues declined drastically in 1982 to $9,203,000 from $15,619,000 in 1981. The Stater Bros. supermarket chain, which accounted for 51% of our trading stamp revenues in 1981 discontinued giving trading stamps on April 1, 1982, and we have not replaced the lost revenue. The main good news coming out of our trading stamp business last year was an increase in sales to service stations, attributable to very intense competition caused by the current gasoline glut, plus some heartening examples of customer success after adoption of our programs.

Our continued substantial profits in the trading stamp business, in the face of huge decreases in sales, are made possible only by the slow departure of "float" from trading stamps sold in earlier and better years. This "float" — resulting from past issuance of trading stamps when volume was many times greater than the current level — is very large in relation to current issuances. (Trading stamp revenues peaked at $124,180,000 in fiscal 1970, and our 1982 revenues of $9,203,000 therefore represented a decline of 93% from peak volume.) Eventually, unless stamp issuances improve, earnings from investing "float" will decline enormously. And, since the trading stamp business already operates at a loss before taking investment revenues into account, such future declines in "float" will aggravate what is already a poor situation. This happens because any significant decline in non-investment revenues is inevitably more rapid than the related decline in costs. Such is the normal result for any operator of a chain of retail stores (like our trading stamp redemption stores) whose "same store" sales decline in dollars from year to year.

Under such conditions it has been helpful to us that our decline in "float" in recent years has proceeded at so extremely slow a rate, leaving our reserved liability for trading stamp redemption at $60,240,000 at yearend 1982, down only 6.3% from 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 1982 we made revisions increasing operating income as above described, as explained in detail in Note 2 to our accompanying financial statements. Recent changes, including that in 1982, both decreased our estimates of stamps ultimately to be redeemed and increased our estimates of total redemption costs per stamp. Merchandise cost per stamp redeemed has remained relatively constant as volume has declined, and we hope this state of affairs will continue. Non-merchandise or redemption service cost per stamp redeemed is another story. Such cost per stamp is now virtually certain to go up sharply from last year's level as stamps redeemed in the future share store and warehouse operating expense which cannot be reduced at the same rate as redemptions. The 1982 changes take all the foregoing into account.

A higher proportion of non-merchandise costs in our redemption liability has an unfortunate income-tax effect, diminishing true "float" per dollar of book liability. The cash available to us for use from aggregate redemption liability as reported in our books is always considerably lower than the amount of liability shown. One cause is U. S. Treasury regulations (which we have conformed to despite doubting their legality) which do not allow us to deduct for income-tax purposes future redemption service cost (for instance, store operating expense) as distinguished from future merchandise cost. Both types of cost are unavoidable and require accrual of real liabilities in our audited financial statements. The cash-use consequences of the divergence (all of which is not caused by the U. S. Treasury regulation cited above) of IRS-specified income-tax accounting and our audited accounting are substantial. For instance, out of our total trading stamp redemption liability as we report it of $60,240,000 at yearend 1982, we must leave $17,175,000 in a non-interest-bearing deposit with the U. S. Treasury, designated "prepaid income taxes" in our balance sheet.

We remain convinced 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 related motivation business revenues decreased slightly in 1982 to $1,351,000 from $1,446,000 in 1981. Revenues are expected to increase in 1983.

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 $2,838,000 in 1982 compared with $2,167,000 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 1982 as we report consolidated revenues of $252 million and consolidated net worth of $218 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 until January 1, 1983 was 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 irregularly 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. No significant sale of fixed assets occurred in 1982.

Our aggregate share of all types of special net gains combined, after income taxes, was $23,101,000 in 1982 compared with $6,731,000 in 1981. All the 1981 net gain came from the sale of securities. The 1982 share of net gain consisted of $25,044,000 from sale of securities, offset by $1,943,000 in net loss from Mutual Savings' sale of mortgage-backed securities. The 1982 share of net gain from sale of securities included $23,901,000 from disposition of our entire holdings in Pinkerton's, Inc., discussed in the next section of this letter.

PINKERTON'S, INC.

Pursuant to a contract made in 1982 we received cash from American Brands early in 1983 for our entire Pinkerton's holding. The after-tax gain of $23,901,000 is included in our 1982 financial figures.

The holding sold consisted of non-voting stock representing 37% of the equity in Pinkerton's, long 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 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 have always expected 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 an uncommon willingness to own "nonvoting-partnership" interests in businesses and to attract other offerings like that which produced our Pinkerton's holding. And we are sure, based on six years' observation from our non-voting position, that Pinkerton's wouldn't have been managed or merged one whit better or one whit more in its shareholders' interests if we had purchased voting control.

Only the dividends we have received from Pinkerton's are included in our reported operating income. These dividends were 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 $2,011,000 in 1982 and $1,730,000 in 1981.

There will, of course, be no future operating income from Pinkerton's dividends, only income from reinvesting the $47,265,000 after-tax proceeds of disposition of the Pinker-ton's holding. Our average compounded, after-tax return from owning non-voting Pinker-ton's stock was 15% per year, merging the effects of both dividends over the years and the final large capital gain included in the portion of our 1982 income listed above under the heading "Net Gains on Sales of Corporate Securities, Mortgages and Important Fixed Assets."

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 25, 1982. 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 has always been very important to us. When combined with our practice of doing a certain amount of long-term borrowing in advance of specific need, impeccable credit has given 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 immediately following this letter. 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 liability, 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.

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 at constant physical volume, even while reporting apparently satisfactory profits, is a very dubious candidate, absent some special factor, for acquisition by a rational acquirer.

Our balance sheet net worth at March 3, 1973 was about $53 million. By the end of 1982 our balance sheet net worth had increased to approximately $218 million, up 311% in ten years, after payment of regular dividends. At March 3, 1973 our equity in aggregate securities was worth about $4 million more than balance sheet cost. At the end of 1982 this equity was worth about $27 million more than balance sheet cost. Our average annual total percentage return earned on shareholders' investment over the ten years ending December 25, 1982 was approximately 16.7% per annum, without taking into account (1) the increase from $4 million to $27 million in unrealized appreciation in our equity in marketable securities or (2) unrealized net appreciation in such subsidiaries as See's and the Buffalo Evening News. The percentage return earned was acceptable in a moderate inflation environment, considering the headwinds in our initial trading stamp business.

In 1982, the year just ended, our total percentage return on the beginning investment of our shareholders was approximately 27%. 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.

In the future we hope to earn a higher average (though sharply fluctuating) annual total percentage return on shareholders' investment — at least for a while until we are dragged down by some law of regression toward mean results, an outcome sure to occur eventually at any corporation which retains a high proportion of its earnings. Some short-term prospects are favorable, for instance, the prospect that the Buffalo Evening News will have earnings in 1983, compared to a loss in 1982. Furthermore, 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.

However, even if above-average returns on shareholders' equity are earned for a long time in the future — far from a sure thing — the inflation problem for our shareholders will not automatically be solved. 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 and trying to serve 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 intrinsic value underlying each outstanding share. Our unwillingness to accept any such dilution explains our long-unchanged common stock capitalization.

Even in the presence of the moderation in inflation caused by the current severe recession, we think the likelihood of future inflation remains high in the United States, as well as in other modern democracies. In a sense the current recession has compounded the inflation problem by demonstrating that a conscientious corporate manager must take precautions not only against inflation but also against severe slump — no small order, considering the inherent contradictions involved.

Current conditions have only intensified our long-standing belief that a (1) heavy managerial emphasis on the cash-generating characteristics of businesses, (2) managerial 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.

This may well be the last annual report our shareholders will ever receive from Blue Chip Stamps as a separate corporation, because work is in progress on a proposal that our corporation be merged with Berkshire Hathaway Inc., long a 59.6%-owner of Blue Chip Stamps. If such a merger occurs, our shareholders will become holders of common shares of Berkshire Hathaway Inc. We will not here further discuss merger possibilities, because such discussion will be contained in a formal merger proposal and proxy statement, which Blue Chip shareholders will receive in due course if such a proposal is approved by the board of directors of each corporation.

Cordially yours,

Charles T. Munger, Chairman of the Board
Donald A. Hoeppel, President

February 17, 1983