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WESCO FINANCIAL CORPORATION

Annual Report 1989

Form 10-K Annual Report 1989

The 1989 Annual Report of Wesco Financial Corporation included the following letter to Wesco stockholders from the Chairman of the Company.

WESCO FINANCIAL CORPORATION
LETTER TO SHAREHOLDERS

To Our Shareholders:

Consolidated "normal" operating income (i.e., before all unusual operating income and all net gains from sales of securities) for the calendar year 1989 increased to $24,414,000 ($3.43 per share) from $23,564,000 ($3.31 per share) in the previous year.

Consolidated net income (i.e., after unusual operating items and all net gains from sales of securities) increased to $30,334,000 ($4.26 per share) from $30,089,000 ($4.22 per share) in the previous year.

Wesco has three major subsidiaries, Mutual Savings, in Pasadena, Wesco-Financial Insurance Company, headquartered in Omaha and currently engaged principally in the reinsurance business, and Precision Steel, headquartered in Chicago and engaged in the steel warehousing and specialty metal products businesses. Consolidated net income for the two years just ended breaks down as follows (in 000s except for per-share amounts)[1]:

	Year Ended			
	December 31, 1989		December 31, 1988	
	Amount	Per Wesco Share	Amount	Per Wesco Share
"Normal" net operating income of:				
Mutual Savings	$ 4,191	$ .59	$ 4,694	$ .66
Wesco-Financial Insurance business	14,276	2.00	12,094	1.70
Precision Steel's businesses	2,769	.39	3,167	.44
All other "normal" net operating income[2]	3,178	.45	3,609	.51
	24,414	3.43	23,564	3.31
Gain on sale of interest in Bowery Savings Bank	—	—	4,836	.68
Net gains on sales of marketable securities	5,920	.83	1,689	.23
Wesco consolidated net income	$30,334	$4.26	$30,089	$4.22

(1) All figures are net of income taxes.

(2) After deduction of interest and other corporate expenses. Income was from ownership of the Mutual Savings headquarters office building, primarily leased to outside tenants, interest and dividend income from cash equivalents and marketable securities owned outside the savings and loan and insurance subsidiaries, and the electrical equipment manufacturing business, 80%-owned by Wesco since yearend 1988.

This supplementary breakdown of earnings differs somewhat from that used in audited financial statements which follow standard accounting convention. The supplementary breakdown is furnished because it is considered useful to shareholders.

Mutual Savings

Mutual Savings' "normal" net operating income of $4,191,000 in 1989 represented a decrease of 11% from the $4,694,000 figure the previous year.

The decrease in 1989 was primarily attributable to a less favorable interest rate "spread" as cost of holding savings increased more than yield on loans and investments.

As usual, these "normal-income" figures come from a decidedly abnormal savings and loan association.

Separate balance sheets of Mutual Savings at yearend 1988 and 1989 are set forth at the end of this annual report. They show (1) total savings accounts rising to $293 million from $289 million the year before, (2) a very high ratio of shareholders' equity to savings account liabilities (near the highest for any mature U.S. savings and loan association), (3) a substantial portion of savings account liabilities offset by cash equivalents and marketable securities, and (4) a loan portfolio (mostly real estate mortgages) of about $154 million at the end of 1989, up slightly from $137 million at the end of 1988.

The loan portfolio at the end of 1989, although containing almost no risk of loss from defaults, bore an average interest rate of only 9.23%, probably near the lowest among U.S. savings and loan associations, but up moderately from 8.70% at the end of 1988. Because the loan portfolio is almost entirely made up of instruments of short maturity or bearing interest rates that adjust automatically with the market, there is now much less unrealized depreciation in the loan portfolio than the net unrealized appreciation in Mutual Savings' interest-bearing securities and public utility preferred stocks. That appreciation at December 31, 1989 was about $11.3 million.

While the "spread" between Mutual Savings' average interest rates paid on savings and received on loans remains too low to provide respectable profits, this "spread" improved again last year. Moreover, the disadvantage from inadequate "spread" has been reduced in each recent year by the effect of various forms of tax-advantaged investment, primarily preferred stock and municipal bonds. The negative side of this tax-advantaged antidote to inadequate interest rate margin on loans is the risk that preferred stock and municipal bonds, with their fixed yield and long life, will decline in value and not provide enough income to cover Mutual Savings' interest and other costs, if the general level of interest rates should sharply rise. In view of this risk, Mutual Savings' total commitment has been kept conservative, relative to the amount of its net worth.

Mutual Savings remains a "qualified thrift lender" under the old federal regulatory definition (which ends June 30, 1991) requiring 60% of assets in various housing-related categories. It plans to continue keeping substantially all loans receivable either with short expected lives or with interest rates that fluctuate with the market. All new variable-rate loans are "capped" at the 25% per annum level, which is over ten percentage points higher than the common 2½-points-over-market "cap" offered by competing associations. Naturally, to gain this extra protection from interest rate increase, Mutual Savings "pays" by (1) getting lower "spreads" over an interest rate index, and (2) not being able to make loans in amounts desired.

As pointed out in Note 10 to the accompanying financial statements, the book value of Wesco's equity in Mutual Savings ($48.9 million at December 31, 1989) overstates the amount realizable, after taxes, from sale or liquidation at book value. If all Mutual Savings' assets, net of liabilities, were to be sold for the $48.9 million reported as book value, the parent corporation would receive much less than $48.9 million after substantial income taxation imposed because about $47 million of what is designated shareholders' equity for accounting purposes is considered bad debt reserves for most tax purposes.

Mutual Savings has not only a buried value in unrealized appreciation of securities but also a buried value in real estate. The foreclosed property on hand (mostly 22 acres at or near the oceanfront in Santa Barbara, acquired in 1966) has become worth over a long holding period considerably more than its $8.4 million balance sheet carrying cost. Reasonable, community-sensitive development of this property has been delayed over 14 years in the course of administration of land-use laws. But, miraculous to report, eight houses, plus recreation facilities, are in various stages of completion on the property as part of an authorized development into 32 houses interspersed with large open areas. Mutual Savings plans to make the development first-rate in every respect, and unique in the quality of its landscaping.

The buried value in real estate is limited by the small number of houses allowed (32) and by the fact that only about half of such houses will have a significant ocean view. Additional limitation will come from high cost of private streets, sewage and utility improvements and connections, landscaping, and non-standardized, environmentally sensitive adaptation of housing to the site. Also, various charges and burdens, including heavy archaeological obligations imposed by governmental bodies, will drastically reduce our potential recovery from what it would have been had the zoning and development climate of the early 1970s continued into the present era. We have "given" a very large fraction of the value of our land to the County of Santa Barbara in exchange for permission to use it at all.

The savings and loan association described in the foregoing paragraphs, quite different from most other associations for a long time, added a significant new abnormality during 1988. Mutual Savings increased its position in stock of Federal Home Loan Mortgage Corporation (widely known as "Freddie Mac") to 2,400,000 shares. This is 4% of the total shares outstanding, the legal limit for any one holder at the time the shares were purchased. Mutual Savings' average cost is $29.89 per share, compared to a price of $67.12 per share in trading on the New York Stock Exchange at the end of 1989. Thus, based on 1989 yearend trading prices, Mutual Savings had an unrealized pre-tax profit in Freddie Mac shares of about $89.4 million. At current tax rates the potential after-tax profit is about $52.6 million, or $7.39 per Wesco share outstanding.

Freddie Mac, formerly created and long run by a federal agency (the Federal Home Loan Bank Board), is now owned privately, largely by institutional investors and is now governed by an independent board of directors. Freddie Mac supports housing primarily by purchasing housing mortgage loans for immediate transmutation into mortgage-backed securities that it guarantees and promptly sells. In the process Freddie Mac earns fees and "spreads" while avoiding most interest-rate-change risk. This is a much better business than that carried on by most (or indeed most of the top 10% of) savings and loan associations, as demonstrated by Freddie Mac's high percentage returns earned on equity capital in recent years. One ironic cause of the high returns is that this creation of federal regulators pays no deposit-insurance premiums as it replaces much of the former function of the savings and loan industry.

At Freddie Mac's current dividend rate ($1.60 per annum per share), Mutual Savings' pre-tax yield is only 5.35% on its $29.89 average cost per share. Post-tax, the dividend yield is only 4.4%, but this amounts to about 75% of the current after-tax yield from very high grade mortgages. Moreover, Freddie Mac has a very creditable history of avoiding significant loan losses and increasing its earnings and dividend rate, thus contributing to increases in the market price of its stock. Following are figures for 1985-1989:

Year Ended 12/31:	Earnings per Share	Dividends per Share	Year-End Market Price per Share	Freddie Mac's Return Earned on all Average Equity
1985	$2.98	$ .53	$ 9.19	30.0%
1986	3.72	1.13	15.17	28.5
1987	4.53	1.10	12.12	28.2
1988	5.73	1.25	50.50	27.5
1989	6.57	1.60	67.12	25.0

When Wesco's annual report went to press last year, Congress was midcourse in considering revisions to the savings and loan laws. But it was clear that associations were shortly to be "re-regulated" into some mode less likely to cause a fresh torrent of deposit-insurance losses, borne by taxpayers. Provoking that legislative action was a previous torrent of losses which now seems likely to exceed $150 billion. These losses were caused by a combination of (1) competitive pressure on the "spread" between interest paid and interest received put on associations and banks when federal deposit insurance is provided to entities free to pay any interest rates they wish in order to attract deposits, (2) loose asset deployment rules for associations, (3) admission and retention of crooks and fools as managers of associations without regulatory objection, (4) general real estate calamities in certain big regions, and (5) continuous irresponsible protection and enhancement of unsoundness by the savings and loan lobby and certain members of Congress beholden to the most despicable savings and loan operators.

The new laws, under the acronym FIRREA, were composed and enacted with a speed caused by congressional indignation. (A recent example of such indignation, employing remarkable comparisons, is provided by the words of Congressman Jim Leach: "[If certain allegations are true] Charles Keating is a financiopath of obscene proportions — the Reverend Jim Bakker of American commerce, given a license to steal by a bank board headed by the Neville Chamberlain of regulation — a cheerleader who saw little evil and thus spoke little truth.")

Mutual Savings modestly contributed to tough legislative action by resigning from the U.S. League of Savings Institutions, using a letter of resignation which drew widespread media attention despite its understated criticism. A copy of this letter of resignation is appended at the end of this letter to shareholders.

Mutual Savings, desiring to act responsibly, supported virtually all the law revisions made by FIRREA, even though many of them will hurt Mutual Savings' profits.

For example:

(1) In stages, by July 1, 1994, Mutual Savings (and its service corporation subsidiary) must dispose of:

- (a) High-quality public utility preferred stocks, having tax-advantaged dividend rates averaging about 10.8% per annum, with a carrying value of $41.4 million at yearend 1989, and a market value then higher by about $8.7 million; and
- (b) High-quality convertible preferred stock of Salomon Inc, bearing a tax-advantaged dividend rate of 9% per annum, with a carrying value of $26 million, believed to be below the amount which could be realized in the event of sale.

(2) In stages, by the same date, July 1, 1994, Mutual Savings must write down to zero, in computing net worth for regulatory purposes, its 2,400,000 shares of Freddie Mac, which

had a carrying value of $71.7 million at yearend 1989, and, as reported above, a market value then higher by about $89.4 million.

(3) All new asset commitments, fitting Mutual Savings' proclivities and tax position, are pretty well restricted to (a) housing loans (including indirect loans in the form of mortgage-backed securities) and (b) debt instruments of the U.S. Government or its agencies.

(4) In stages, designed to create compliance during a two-year period commencing July 1, 1991, Mutual Savings will have to increase "qualified thrift lender" assets by 10 percentage points to a 70%-of-assets level, using a new and more limited definition of such "qualified thrift lender" assets which, to our surprise, does not include Freddie Mac stock. If the new test had been in full effect at December 31, 1989, Mutual Savings would have complied by disposing of about $74 million of non-home-loan assets (including some cash equivalents) and placing the proceeds in home loans (including indirect home loans in the form of short-term mortgage-backed securities).

(5) Deposit-insurance premiums have been increased. Short term, Mutual Savings is protected by credits of a nonrecurring nature. But by the mid 1990s the new premium rates will reduce Mutual Savings' annual earning power by about $200,000 from the level which would have occurred if it were still paying at the 0.083%-of-deposits rate which was in effect for years, instead of the new rate of 0.23%. The adverse effect of the higher deposit insurance costs on percentage return on shareholders' equity is much lower at Mutual Savings than at almost all other associations, which suffer substantially. The cause of Mutual Savings' advantage is its much larger percentage of equity, compared to deposits. This is a "one-time" advantage related to one ratio; on an incremental dollar of savings Mutual Savings faces the same damage as everyone else.

These combined effects will reduce Mutual Savings' normal earning power. While conservatively operated, Mutual Savings has been scrambling through recent years in its own way, obtaining a modest success made possible largely by the wide variety of asset-deployment options available under pre-FIRREA law. Consequently, FIRREA will adversely affect Mutual Savings, however wise the new restrictions, public needs considered. Nevertheless, it is probable that Mutual Savings' normal earning power will not be much reduced in 1990 and 1991.

We predict this deferment of decline in normal earnings because:

(1) FIRREA's asset-mix effects are phased in, subject to wide regulatory discretion; and

(2) We anticipate that regulators will be wise enough to exercise their discretion to allow extra-strong associations, with easy-to-sell assets, the same forbearance which will be granted to weak associations with hard-to-sell assets.

If we prove wrong in our prediction about regulators, Mutual Savings' wisest alternative will probably be withdrawal from the savings and loan business and the related obligation to pay deposit-insurance premiums.

If, as seems likely, Mutual Savings stays in the savings and loan business, it will retain a business even more mediocre than before, with only two interesting near-term prospects:

(1) During the next few years, Mutual Savings is almost certain to make a pre-tax profit of a nonrecurring nature as it disposes of the Santa Barbara property it acquired through foreclosure in 1966; and

(2) Mutual Savings will retain prospects for gain from its Freddie Mac stock if, as anticipated, Freddie Mac pays ever-higher dividends and the price of the stock also rises.

Long term, Mutual Savings hopes to find within the savings and loan business some constructive, continuing role which is not dependent on either of the foregoing anticipated near-term prospects. Until the right long-term role is found, our policy is simply to "stagger through."

The FIRREA law revision, while greatly improving the savings and loan system from the taxpayers' point of view, took an approach which can fairly be described as "all stick and no carrot." This is no way to create felicity for the donkey, but we deserve our share of the beating because we were previously so passive in the presence of obvious error and evil. Moreover, the safety-enhancing features of the law revision fell short in one fundamental respect which leaves profits under pressure: banks and associations remain free, within wide limits, to attract government-insured deposits at any interest rate they wish, while they must resell the ultimate fungible commodity, the use of money, into a brutally competitive market. The resulting squeeze on interest-rate "spread" safely attainable, combined with normal competitive disadvantages of associations, leaves the average well-run association with a likely future which should not excite its owners.

The normal competitive disadvantages of the average association, compared with the average bank, now include the following: higher deposit-insurance costs, more confusing new regulation, and less experience and momentum in various important remunerative activities. As a result, even a superbly run conventional association, like the one owned by H. F. Ahmanson & Co., sells in the stock market at a much lower price-to-book-value ratio than a superbly run bank. And the average savings and loan branch office probably now offers more incremental value to an experienced bank than it provides to its present owner.

Moreover, the average association does not now compete only with banks. Also gathering "deposits" are the money-market funds which:

(1) pay no deposit-insurance premiums, saving 0.23% of deposits each year, compared to associations;

(2) are required to employ exactly no capital from profit-earning proprietors ("management companies" in fund parlance), while capital requirements for associations have been raised;

(3) have lower-cost regulation (from an understaffed SEC) than associations;

(4) maintain no expensive branch offices, although they provide check-writing privileges and accept frequent deposits, using fast, low-cost systems which are better adapted in many ways to the new order than the systems of the average association; and,

(5) as a result of all the foregoing advantages, have total annual costs (before proprietors' profits), as a percentage of assets, which are more than 50% lower than annual costs of the most efficient association.

Thus, the natural "almost-no-brainer," non-home-mortgage, deposit-gathering niche is now occupied by a competing, better-adapted new species. This leaves associations in roughly the position of the original rabbit-like mammals which lost ecological market share when the rabbit was introduced into Australia. The adjustable-home-mortgage niche may now provide a decent home for some large, extremely efficient loan originators like Home Savings, but, as we seem to say each year, we have not yet found for Mutual Savings a permanent lending niche which is attractive, as distinguished from bearable. In the mortgage business we thus constantly confirm Samuel Johnson's observation that: "Life is a state in which much is to be endured and little to be enjoyed."

Left in place in the revised savings and loan system is a significant (although much reduced) structural risk for the federal government as deposit insurer. Associations retain a considerable residue of temptation to act imprudently. The temptation, in response to the profit-pressure which is a natural consequence of the structure of the system, is the same one which caused troubles in the past: the temptation to seek an acceptable interest rate "spread," not available any other way, by bearing undue risk from either (1) mismatched maturities of loans and deposits or (2) losses through defaults of a gamier class of borrowers willing to promise extra-high interest rates. It is almost impossible to have asset deployment controls so tough that a bank or association can't look good for a while (and give the appearance of justifying higher compensation of management) as it takes risks which will in due course destroy its owners' equity and also cause deposit insurance losses. The "all stick" method of control is much better than nothing, but it is far from ideal when it is the exclusive method for prevention of losses borne by the deposit insurer. In contrast, when, long ago, the federal deposit insurer had low losses, the savings and loan system used both carrots and stick, so that the average savings and loan operator could do well without exceptional luck or ability. (The carrots were very low income taxation plus interest-rate controls which reduced cost of holding deposits while giving an advantage over banks in attracting deposits.) We think the present, revised system continues to impose more risk than taxpayers should bear, with high deposit-insurance costs contributing to the risk as well as compensating for it.

Housing is now less assisted than before by the existence of savings and loan associations. An example of the drift away from housing assistance is provided by FIRREA's new restriction preventing large loans to any one house builder. The new requirement is that an association loan no more than 15% of owners' equity to one customer, with exceptions permitted up to 30% for adequately capitalized associations with good records. The new requirement would have greatly reduced the profits and housing contributions of Mutual Savings in its early days when it concentrated resources in development loans while trusting only a few house-builders. And the new requirement now has the same general effect. It will significantly restrict availability of house-building loans in many regions of the country. This result demonstrates the impossibility of revising a complex system without undesired "by-product" effects. The first law of ecology and the first law of legislation are one and the same: "You can never do merely one thing."

Of course, a "by-product" of law revision sometimes helps, instead of hurts, some participant in a market. New "risk-based" capital requirements under FIRREA have such an effect, as they give associations new incentives to transfer monies they otherwise would have earned to Freddie Mac, through exchange of mortgages for credit-enhanced, mortgage-backed securities. (Although the securities then provide less income, they help satisfy regulatory capital requirements, because the securities require less owners' equity to hold.) This income-transfer effect should help Mutual Savings, through its large shareholding position in Freddie Mac.

Precision Steel

The businesses of Wesco's Precision Steel subsidiary, located in the outskirts of Chicago at Franklin Park, Illinois, contributed $2,769,000 to normal net operating income in 1989, down 13% compared with $3,167,000 in 1988. The decrease in 1989 profit occurred as pounds of product sold declined by 12%. Revenues were down less, by 5% to $59,440,000.

Under the skilled leadership of David Hillstrom, Precision Steel's businesses in 1989 continued to provide an extraordinary return on resources employed.

As we never tire of saying, the good financial results have an underlying reason, although not one strong enough to cause the results achieved in the absence of superb management. Precision Steel's businesses, despite their mundane nomenclature, are steps advanced on the quality scale from mere commodity-type businesses. Many customers of Precision Steel, needing dependable supply on short notice of specialized grades of high-quality, cold-rolled strip steel, reasonable prices, technical excellence in cutting to order, and remembrance when supplies are short, rightly believe that they have no fully comparable alternative in Precision Steel's market area. Indeed, many customers at locations remote from Chicago (for instance, Los Angeles) seek out Precision Steel's service.

It is not common that steel warehouses have results like Precision Steel's. What we see, year after year, under David Hillstrom's leadership is boring, repetitive excellence as he remembers a basic catechism emphasizing service of the highest quality. We hope to be associated with him for a long time.

Wesco-Financial Insurance Company

A new business was added to the Wesco group in 1985, in co-venture with Wesco's 80% owner and ultimate parent corporation, Berkshire Hathaway Inc.

With the enthusiastic approval of all Wesco's directors, including substantial Wesco shareholders in the Peters and Caspers families, without whose approval such action would not have been taken, Wesco in 1985 invested $45 million in cash equivalents in a newly organized, wholly owned insurance company, Wesco-Financial Insurance Company ("Wes-FIC"). Another $58 million was invested in 1986, 1987 and 1989.

The new subsidiary, Wes-FIC, reinsured, through another Berkshire Hathaway insurance company subsidiary as intermediary-without-profit, 2% of the entire book of insurance business of the long-established Fireman's Fund Group. Wes-FIC thereby assumed the benefits and burdens of Fireman's Fund's prices, costs and losses under a contract covering all insurance premiums earned by Fireman's Fund during a four-year period ending August 31, 1989. The arrangement put Wes-FIC in almost exactly the position it would have been in if it, instead of Fireman's Fund, had directly written 2% of the business. Differences in results occurred only from the investment side of insurance, as Wes-FIC, instead of Fireman's Fund, invested funds from "float" generated. Wes-FIC's share of premiums earned in 1989, before contract termination, exceeded $37 million.

Upon contract termination, Wes-FIC returned to Fireman's Fund $15.6 million in unearned premiums, net of related ceding commissions, and retained assets of about $91 million offset by claims reserves which will be exhausted slowly over many future years. We regard the totality of Wesco's four-year participation in the Fireman's Fund reinsurance contract as having excellent prospects, all future claim payments considered. Wesco's ultimate parent corporation (and 80% owner) almost certainly did Wesco a favor in allowing Wesco's participation, as was planned at the time.

There was some good luck in the selection, years ago, of a termination date for the Fireman's Fund contract. The date, August 31, 1989, happened to be just before occurrence of both Hurricane Hugo and the San Francisco earthquake. There was some heavenly justice in this outcome, because Wes-FIC caught a share of hurricane losses within hours after the inception of the contract in 1985.

Wes-FIC in 1988 began to write direct business, as distinguished from reinsurance. It is now licensed in Nebraska, Utah and Iowa, but it wrote only $183,000 in direct premiums, almost all surplus lines coverage (permitted for non-admitted insurers) in Alabama. Earned direct premiums were $438,000.

Wes-FIC's "normal" net income for 1989 was $14,276,000, versus $12,094,000 for 1988. The net "normal" income figures excluded securities gains, net of income taxes, of $5,910,000 in 1989, compared with $6,071,000 (including $4,836,000 realized on sale of Wes-FIC's 9% equity interest in Bowery Savings Bank) in 1988. These items are reported as "Net Gains on Sales of Securities," below. Wes-FIC's net income benefitted by about $215,000 in 1989, versus $260,000 in 1988, because of an unusual adjustment to its income tax provision caused by the Tax Reform Act of 1986.

It is in the nature of even the finest casualty insurance businesses that in keeping their accounts they must estimate and deduct all future costs and losses from premiums already earned. Uncertainties inherent in this undertaking make financial statements more mere "best honest guesses" than is typically the case with accounts of non-insurance-writing corporations. And the reinsurance portion of the casualty insurance business, because it contains one or more extra links in the loss-reporting chain, usually creates more accounting uncertainty than the non-reinsurance portion. Wesco shareholders should remain aware of the inherent imperfections of Wes-FIC's accounting, based as it is on forecasts of outcomes in many future years.

Wes-FIC retains a "longage" of capital and a shortage of good insurance business. We see few present opportunities for sound expansion, but we expect more insurance writing in due course, made possible by fear that other insurers will become unable or unwilling to pay fair claims.

Effective January 1, 1990, Wes-FIC has begun to reinsure 50% of the book of insurance business (largely workers' compensation insurance) of Cypress Insurance Company, a wholly owned subsidiary of Berkshire Hathaway. Wes-FIC's share of premiums written is expected to approximate $8 million in 1990. We regard this reinsurance contract as worth having at Wesco, but it is not nearly as promising, per dollar of insurance written, as was the Fireman's Fund contract.

All Other "Normal" Net Operating Income

All other "normal" net operating income, net of interest paid and general corporate expenses, decreased to $3,178,000 in 1989 from $3,609,000 in 1988. Sources were (1) rents ($2,518,000 gross, excluding rent from Mutual Savings) from Wesco's Pasadena office building block (predominantly leased to outsiders although Mutual Savings is the ground floor tenant), (2) interest and dividends from cash equivalents and marketable securities held outside the savings and loan and insurance subsidiaries, and (3) earnings of New America Electrical Corporation. The decrease in this "all other" component of earnings in 1989 resulted primarily from transfer of assets, with their related incomes, to Wesco's insurance subsidiary to augment its capital position.

Net Gains On Sales Of Securities

Wesco's aggregate net gains on sales of securities, combined, after income taxes, decreased to $5,920,000 in 1989 from $6,525,000 in 1988. As noted above, $5,910,000 of these gains were realized in the Wes-FIC insurance subsidiary in 1989, versus $6,071,000 realized in 1988.

Convertible Preferred Stock of Salomon Inc

On October 1, 1987 Wesco and certain of its wholly owned subsidiaries purchased 100,000 newly issued shares of Series A Cumulative Convertible Preferred Stock, without par value, of Salomon Inc ("Salomon"), at a cost of $100 million. Salomon's primary business is transacted by its subsidiary, Salomon Brothers, a leading securities firm. Our investment was part of a $700 million transaction in which other subsidiaries of Berkshire Hathaway Inc., Wesco's parent, invested $600 million. Principal terms of the transaction included the following: (1) the preferred stock pays dividends at the annual rate of 9%; (2) each preferred share, purchased at a cost of $1,000, will be convertible into 26.31579 shares of Salomon common stock on or after October 31, 1990, or earlier if certain extraordinary events occur; and (3) the preferred stock is subject to mandatory redemption provisions requiring the retirement, at $1,000 per share plus accrued dividends, of 20% of the issue on each October 31, beginning in 1995, so long as any shares of preferred stock remain outstanding.

At the stated conversion price of the preferred stock, a profit (subject to certain procedural requirements) will be realizable whenever, after October 31, 1990, the common stock of Salomon (listed on the New York Stock Exchange) trades at over $38 per share. At the time of our commitment to buy the new preferred, the common stock of Salomon was selling in the low 30s. However, shortly after Wesco acquired its new stock certificates, the October 19, 1987 "Black Monday" stock market crash occurred, which caused temporary but substantial operating losses plus a lowered credit rating at Salomon. Although Salomon, among securities firms, suffered only its rough share of the general debacle, its common stock at one time after the crash traded as low as $16⅝.

At the end of 1989 Salomon common stock was trading at $23⅜, compared with $24⅛ at the end of 1988, after much constructive adjustment of Salomon's business to new conditions.

Salomon's credit as a potential source of preferred dividends and stock redemptions improved during its 1988 recovery, when generally available dividend rates on preferred stock were roughly stable. And during 1989 Salomon was a star performer, compared to most other securities firms. With Wesco's preferred stock now shorter in contractual duration, and its conversion privilege enhanced in value during the last two years, we believe that the fair market value of Wesco's investment was somewhat in excess of its cost, and that the aggregate amount of any such excess was not material to Wesco, at December 31, 1989.

Berkshire Hathaway's Chairman, Warren Buffett, and the undersigned joined the board of Salomon on October 28, 1987, and are very pleased with the association.

Other Convertible Preferred Stocks

In transactions similar to that which created our Salomon investment, Wesco and its subsidiaries during 1989 invested a total of $75 million in several new issues of convertible preferred stock. The common stock of all issuers is listed on the New York Stock Exchange. These transactions are briefly summarized below:

(1) ***The Gillette Company***
On July 20, 1989, Wesco's Wes-FIC subsidiary invested $40 million in newly issued shares of convertible preferred stock of The Gillette Company ("Gillette"). The stock provides an 8¾% annual dividend, must be redeemed by Gillette in 10 years, and is convertible into Gillette common stock at $50 per share. Warren Buffett, Chairman of Wesco's parent company, has joined Gillette's board of directors. Gillette has just introduced a new product, the Sensor razor, which will sell well because it provides significant improvements to the wet-shaving process.

(2) ***USAir Group, Inc.***
On August 7, 1989, Wes-FIC invested $12 million in the newly issued convertible preferred stock of USAir Group, Inc. ("USAir"). The stock provides an annual 9¼% dividend, must be redeemed by USAir in 10 years, and is convertible into USAir common stock at $60 per share.

(3) ***Champion International Corporation***
On December 6, 1989, Wesco and certain of its subsidiaries invested $23 million in a new issue of convertible preferred stock of Champion International Corporation ("Champion"). The stock provides an annual 9¼% dividend, must be redeemed by Champion in 10 years, and is convertible into Champion common stock at $38 per share.

While we admire the corporations and managements involved, we regard these investments in the aggregate as sound but not exciting. Few, if any, investors have ever prospered mightily from investing in convertible preferred stocks of leading corporations. Considering alternatives available when the investments were made, we were pleased to buy the stocks, but Wesco shareholders should expect no bonanza.

New America Electrical Corporation

At the close of 1988, Wesco acquired 80% of the stock of New America Electrical Corporation ("New America Electric") for a price of $8,200,000. Of this price $7,165,000 was cash paid to a liquidating trust for the former shareholders of New America Fund and $1,035,000 was a ten-year, 10% note payable to Glen Mitchel, CEO of New America Electric, who retains the 20% of New America Electric not acquired by Wesco. The pattern of this acquisition is a common one within the Berkshire Hathaway group, where we are willing to be an 80% owner in many a business we would not be in if we did not admire and trust people who retain the other 20% and are expected to continue to operate the business, with little help and no hindrance from us.

Glen Mitchel is a long-time friend and trusted and admired business associate of the undersigned, Wesco's CEO. Indeed, because Wesco's CEO and his family owned a higher percentage of New America Electric than Wesco, our whole transaction was approved by the Wesco board with the recommendation and participation of Warren Buffett, CEO and major shareholder of Berkshire Hathaway, Wesco's parent company. Mr. Buffett had no financial interest in New America Electric, and he, plus Messrs. Munger and Mitchel, all believed that $10,250,000 was a fair valuation for 100% of New America Electric at yearend 1988.

This acquisition became available to Wesco because Glen Mitchel preferred minority (20%) ownership of a Berkshire Hathaway group subsidiary instead of dominant 30% ownership in New America Electric, with all other New America Electric stock pretty well scattered through a new public offering, which was the alternative offered. We like causing such confidence and try always to deserve it.

New America Electric is a manufacturer of various electrical products including switchgear, circuit breakers, lighting ballasts and starters and electrical equipment for marinas and mobile home and recreational vehicle parks. Its facilities are in Orange County, California.

When Wesco purchased its 80% interest, New America Electric had a book net worth of about $6,400,000, including approximately $2,500,000 in cash and equivalents, and a long history of earning high returns on capital, but with current earnings reduced by an industry-wide price war.

Unfortunately, financial results in New America Electric's first year after acquisition are an embarrassment to us. In 1989, New America Electric earned only $168,000, after taxes (before adjustments under consolidated accounting convention incident to our purchase of stock), which is (1) only 2.6% on historical book value of shareholders' equity, and (2) only 1.6% on the price Wesco paid. After consolidated accounting adjustments, the total contribution of New America Electric to Wesco's 1989 earnings was even lower: only $59,000 (included in our earnings breakdown in the "all other normal net operating income" category).

The year-to-year earnings decline at New America Electric was a stunning 77%. Part of the earnings decline was caused by high expense incurred in consolidating previously scattered operations in a large, newly leased building. Other factors were (1) escalation of the price war accompanied by a 2.5% year-to-year decline in sales, (2) a ridiculous, unfair result in a lawsuit, and (3) at least one decision which, with hindsight, looks like an error.

New America Electric's 1989 troubles were limited to the income statement. Its balance sheet remained strong. For instance, at yearend 1989, despite major improvements of facilities and purchase of new equipment, the same amount of cash and equivalents was on hand as at the start of the year: $2.5 million.

We appraise the 1989 earnings decline as temporary. We think Glen Mitchel is tackling the problems with his usual skill and diligence. We are impressed with the new building and new equipment, which will both reduce costs and improve quality of products and service. And we admire not only Glen Mitchel but also his chief officers: Thomas Johnson, Jeff Mowry and Thomas Vogele.

We will be very supportive as operations are fixed. Our sharing of disappointing times without irrational panic is an entitlement for people who choose to make these 80%-20% deals with us. But we will not obscure, in reports to our shareholders, poor financial results, temporary or not, from any recent business acquisition. And we will be particularly anxious to highlight bad results, no matter how "immaterial" (in accountingspeak), in a case where Wesco's Chairman had an interest in the business acquired. If Wesco's shareholders don't hear much about New America Electric in the future, it will be success, not failure, which causes de-emphasis.

Consolidated Balance Sheet and Related Discussion

Wesco's consolidated balance sheet (1) retains a strength befitting a company whose consolidated net worth supports large outstanding promises to others and (2) reflects a continuing slow pace of acquisition of additional businesses because few are found available, despite constant search, at prices deemed rational from the standpoint of Wesco shareholders.

As indicated in the accompanying financial statements, the aggregate market value of Wesco's marketable equity securities was higher than their aggregate carrying value at December 31, 1989 by about $98 million, up significantly from about $54 million one year earlier. The consolidated aggregate market value of all marketable securities, including bonds and other fixed-income securities, exceeded aggregate carrying value by about $103 million. As earlier emphasized, about $101 million of this unrealized appreciation lies within the savings and loan subsidiary, and includes $89.4 million of appreciation in stock of Freddie Mac. In addition, there is about $29 million of unrealized appreciation in common stocks (mostly stock of The Coca Cola Company) held by Wesco's insurance subsidiary. Under a peculiar accounting convention applicable only to insurance companies this appreciation, after deducting income taxes which would be due if the stocks were sold, is already included in Wesco's audited net worth, even though the gain has never passed through any audited report of income.

Wesco's Pasadena real estate comprises a full block containing (1) about 125,000 first-class net rentable square feet, including Mutual Savings' space, in a modern office building, plus (2) an additional net rentable 34,000 square feet of economically marginal space in old buildings, which it would probably be wiser to destroy than improve. This real estate has a market value substantially in excess of carrying value. The existence of unrealized appreciation is demonstrated by (1) mortgage debt ($4,643,000 at 9.25% fixed) against this real estate now exceeding its depreciated carrying value ($2,862,000) in Wesco's balance sheet at December 31, 1989, and (2) substantial current net cash flow (about $1 million per year) to Wesco after debt service on the mortgage. The modern office building is 97% rented, despite a glut of vacant office space in Pasadena. We charge just-below-standard rents and run the building as a sort of first-class club for tenants we admire. In fact, we are about to refurbish all the bathrooms, even though there is almost nothing wrong with them. (We have observed many recent instances of mismanagement at other buildings where managers prefer to paint the financial record, instead of the building. We try, with an occasional lapse, to stay a long way removed from such conduct, considering it contrary to both implicit obligation to tenants and long-run interest of the owner.) With these practices, a prime location and superior parking facilities, we anticipate future increases in cash flow, but at no better rate than the rate of inflation.

Wesco remains in a prudent position when total debt is compared to total shareholders' equity and total liquid assets. Wesco's practice has been to do a certain amount of long-term borrowing in advance of specific need, in order to have maximum financial flexibility to face both hazards and opportunities. Following this practice, and to reduce interest costs, Wesco during 1989 paid off at par its $25 million of 10⅛% debentures due in June 1991, and issued $30 million of new 8⅞% debentures due in November 1999. The low interest rate on the new debentures was made possible by Wesco's AA+ credit rating.

It is expected that the balance sheet strength of the consolidated enterprise will in due course be used in one or more business extensions. The extension activity requires patience, at least for people like us, as explained below.

It is assumed by many business school graduates, and by almost all consultants, that a corporation can easily improve its outcome by purchasing unrelated or tenuously related businesses. According to this widely shared view, if only the obvious steps had been taken, if the right "mission statement" had been adopted and the right "experts" hired, then each railroad, instead of remaining bound in chains by new forms of competition and obsolete and hostile laws and union rules, would have become another Federal Express, another United Parcel Service, or even another brilliant performer in the mode of Emerson Electric.

Our experience, both actual and vicarious, makes us less optimistic about easy solutions through business acquisition. We think undue optimism arises because successful records draw too much attention. Many people then reason as I would if I forecasted good prospects in big-time tennis after observation limited to Ivan Lendl and Steffi Graf, or good prospects in the California lottery after limiting observation to winners. The converse is also true, only more so. Far too little attention is given to the terrible effects on shareholders (or other owners) of the worst examples of corporate acquisitions such as CBS-DuMont, Xerox-Scientific Data Systems, General Electric-Utah International, Exxon-Reliance Electric, Sohio-Kennecott, First Interstate Bancorp-Allied Bancshares, Arizona Public Service-MeraBank, USX-Texas Oil & Gas, Prudential Insurance-Bache, Mobil Oil-Montgomery Ward, General Motors-Hughes Aircraft, and Avon Products-Practically Anybody. The list ends here for want of space, not a shortage of additional examples. The acquiring corporations listed are great enterprises, honorably run. In fact, their greatness augments their utility as examples as they show how hard it is, even for managers promoted to power through meritocratic procedures at admired corporations, to advance by acquisition the interests of owners.

The full implications of the worst examples are lost, in part, because the conventions of corporate reporting cause managers to present data in a manner which obscures both facts and implications. Horrible results are obscured, and mediocre results are made to look fine. Techniques for masking the truth include (1) mixing bad or mediocre results into other good results which would have been much better, absent the mixture, and (2) taking several poor results off the stage at once through the "big bath" technique. The "big bath" technique, in turn, is often accompanied by some extraordinary gain elsewhere which is cashed on a time schedule designed for obfuscation. Or a loss is mixed into a "restructuring," adopting word usage which would explain Napoleon's outcome at Waterloo as a thoughtful strengthening of France.

As we appraise it, the corporate mode of "solving your problems by acquisition" far more often ends in the mediocre "follow-the-fad-of-the-year" record of a Peter Grace than in the wonderful record of a Dover Corporation. Nor does the avoidance of dubious methodology guarantee success. It is hard to win at the game, even if one (1) does not rely on the valuation judgment of outside acquisition "experts" paid per transaction recommended and closed, and (2) does not create the in-house equivalent of the outside adviser who must buy to thrive, namely the internal department which has no function except acquisitions and often bears a label including "planning," or even "strategic planning."

Perhaps more instructive than the rarity of good corporate acquisition records is the striking rarity of important acquisitions within the few good records. Most winners act as a wise baseball hitter would if permitted to pass as many pitches as he wished before swinging.

For instance, among the best acquisition records is that of Tom Murphy and Dan Burke at Capital Cities/ABC. Yet the major acquisitions, which accounted for more than 80% of ending economic value for continuing shareholders, occurred less often than once each two years. This slow pace occurred even though they were in full control, were (and are) two of the quickest learners and actors around, did all the important work themselves, and were located in the midst of a profit- laden and long-lasting communications revolution (television broadcasting) wherein rapid change churned out opportunities for the acute at an above-normal rate. (The writer has to believe that the opportunities seized by Murphy and Burke were recognizable only by the acute. This follows from the writer's participation in rejecting a television-station opportunity, long ago given by Murphy and Burke when they were barred by law from purchase. The price was less than one-tenth of present-day value.)

A particularly depressing lesson, for the action-prone, might also be extracted from the business acquisition record of Wesco's ultimate parent, Berkshire Hathaway. Over 24 years, Berkshire transformed a small, doomed New England textile enterprise into a large and diversified company, without ending up with many more shares outstanding. Yet if you removed from Berkshire's record the six most significant acquisitions, extracting occurrences averaging one every four years, the record would not now be mentioned here, or anywhere else.

It has always been easy (indeed, one attracts scores of helpers) to make disadvantageous business purchases in a hurry with corporate cash. And it has been even easier to cause disadvantage if one is unwise enough, like General Electric in the Utah International merger, or Xerox in the merger with Scientific Data Systems, not to be super-sensitive to the probability that any attainable stock-for-stock merger will transfer more intrinsic business value than is acquired. On the other hand, advantageous business purchases, not involving competitors or branded products which can be sold through the acquirer's present sales system, are difficult to find.

It is not just the Peter Principle which makes corporate acquisition records so bad, on average, although that Principle does especially intense damage in the acquisition field. (This occurs because, when you promote the General Sales Manager to CEO making unrelated business acquisitions, you naturally cause more trouble than you earlier did when you made a less substantive change by promoting the Sales Manager of some territory to General Sales Manager.) Even a CEO with good acquisition judgment is lucky if, in his remaining career, he finds one large opportunity which tempts rational response.

The scarcity of good acquisition transactions, of course, does not imply that no wonderful businesses are ever for sale. It is just that, in a finite, competitive world, no business is so wonderful that it can't be ruined as an acquisition candidate by increasing the price. When this happens, many corporations buy anyway, for reasons Columbia's great philosopher, Charles Frankel, so well understood. The system is so constructed (irresponsibly, Frankel would say) that the corporate manager gains even though the shareholder loses. (Incidentally, Frankel was mugged to death in a final inadvertent contribution to the study of irresponsible systems, reminding many conservative social critics of Socrates.)

At this point, a last question remains: If successful corporate business acquisition is so hard, how does one explain the widespread recent success of most of the leveraged-buy-out ("LBO") operators who have purchased corporations? A huge part of the answer comes from income-tax effects and other simple effects. When, in a typical LBO, the typical mostly equity corporate capitalization was replaced by 90% debt plus a new 10%-of-capitalization common stock position:

(1) the combined market value of all the new common stock plus all the new debt became much higher than the previous market value of all the old common stock, because the existing stream of pre-tax earnings was no longer shared with corporate income tax

collectors who, in many cases, had previously received more cash each year than shareholders; and

(2) even after the value-enhancing effect of the corporate tax reduction was shared with former shareholders by paying them extra-high prices to leave, a retained residue of value-enhancing tax effect made the new common stock (which now became much like a speculative warrant with good terms) worth considerably more than cost as the ink dried on acquisition papers; and

(3) the new "owners" then resorted to strategies, difficult neither to conceive nor implement, including the following:

   (a) they eliminated many of the easily removable costs (largely personnel costs) and sub-par segments which in some mix (i) bedevil successful corporations (including ours) with sloth and folly and (ii) create their humane grace and, through present sacrifice, good long-term prospects, justifying sacrifice endured; and

   (b) they sold off a few operations at super-high prices, sometimes exercising the easiest microeconomic insight by selling to a direct competitor and sometimes selling to a surprisingly easy-to-find non-competitive corporate buyer, not owned by its managers, willing to pay almost as high a price as a competitor would; and

(4) the new "owners" then profited, in due course, not only from the tax effect and other simple reshuffling activities described above, but also from the wonderful upside effects of extreme financial leverage during a long business boom accompanied by a rising stock market.

Whether the country wants a large number (or even any) of its large corporations to have extremely leveraged capitalizations, except through occasional adversity, presents interesting social questions. Is one social function of corporations to be financially strong so that they act as shock absorbers, protecting dependent employees, suppliers and customers from part of the volatility implicit in capitalism? Was Ben Franklin right when he included the following folk wisdom in *Poor Richard's Almanac:* "It is hard for an empty sack to stand upright." Is a weak corporation, borrowed to the hilt, the social equivalent of a bridge with an inadequate reserve of structural strength? Granting that leveraged buy outs have some favorable effects (as well as unfavorable effects) on long term efficiency, how many thousands of able people do we wish to attract into promotional corporate recapitalization activity which (1) reduces corporate income taxes, (2) often tests the limits of antitrust law, and (3) focuses business attention on short-term cash generation to pay down oppressive levels of debt? Finally, as Columbia Law School's Professor Lou Lowenstein puts it (more or less): "Do we really want entire corporate businesses, as important social institutions, continuously traded like pork belly contracts?"

However the social questions are answered, three aspects of the present situation are clear. First, the corporate tax effect is so large in LBO transactions that easy success in such transactions does not imply that success is easy in ordinary corporate acquisitions. Second, the hordes of leveraged-buy-out operators now with us raise the general level of acquisition prices to the detriment of other would-be acquirers, including Wesco, which are not willing to maximize tax benefits through maximized borrowing. And, third, the LBO operators will not go away so long as present permissive laws last. The operators have a real advantage under such laws, not just a fig leaf aiding promotion. Even though failure and disgrace will reduce their number, and prices paid in leveraged-buy-out transactions will fall, the capitalized value of reducing the corporate income tax will remain. Therefore, plenty of rational incentive will remain for transactions. The LBO genie will encounter reverses, but he is not going back in the bottle unless ordered to do so by new laws.

It should also be noted that the LBO operators' incentives to bid high do not end with real advantages derived from tax law and willingness to reshuffle businesses with much speed and few scruples. Additional incentives for high bids come from typical structures in which general partners of LBO partnerships risk little of their own money (often less than none after fees are taken into account), yet share significantly in gains. Such arrangements are similar to the system of the race track tout. And who has ever seen a tout who didn't want his backer to make a lot of bets?

To Wesco, as a non-LBO operator, the good-corporate-acquisition game was always tough. And that game in each recent year has become more like fishing for muskies at Leech Lake, in Minnesota, where the writer's earliest business partner, Ed Hoskins, had the following conversation with his Indian guide:

"Are any muskies caught in this lake?"

"More muskies are caught in this lake than in any other lake in Minnesota. This lake is famous for muskies."

"How long have you been fishing here?"

"19 years."

"And how many muskies have you caught?"

"None."

When a management has our point of view, infrequency of business acquisition may safely be predicted. Whether this happens, as we like to believe, because the game is hard for almost everyone, or merely because the game is hard for us, the result for Wesco shareholders is the same: less worthwhile activity than we all would like. But there may be one consolation: A series of big, incorrectable acquisition troubles, with no meaningful salvage, is seldom caused by people who think the acquisition game is like fishing for muskies at Leech Lake. One terrible acquisition result is, of course, quite possible. For instance, Wesco would cheerfully invest $75 million tomorrow, with a 60% chance of total loss, provided the pay-off for winning was large enough to cause statistical expectation to provide a handsome return.

As indicated in Schedule I accompanying Wesco's financial statements, investments, both those in the savings and loan and insurance subsidiaries and those held temporarily elsewhere pending sale to fund business extension, tend to be concentrated in very few places. Through this practice of concentration of investments, better understanding is sought with respect to the few decisions made.

The ratio of Wesco's annual reported consolidated net income to reported consolidated shareholders' equity, about 11% in 1987-89, was dependent to a significant extent on securities gains, irregular by nature.

The considerable, and higher than desired, liquidity of Wesco's consolidated financial position as this is written does not result from our forecast that business conditions are about to worsen, or that interest rates are about to rise, or that common stock prices are about to fall. Wesco's condition results, instead, from our simply not finding opportunities for more aggressive use of capital with which we are comfortable.

Wesco continues to try more to profit from always remembering the obvious than from grasping the esoteric. It is remarkable how much long-term advantage people like us have gotten by trying to be consistently not stupid, instead of trying to be very intelligent. There must be some wisdom in the folk saying: "It's the strong swimmers who drown". Our approach, while it has worked fairly well on average in the past and will probably work fairly well over the long-term future, is bound to encounter periods of dullness and disadvantage as it limits action.

Moreover, our approach continues to be applied to no great base position. Wesco has only a tiny fraction of its total intrinsic value in businesses with enough commercial advantage in place to assure permanent high future returns on capital employed. In contrast, Berkshire Hathaway, Wesco's parent corporation, has a much larger proportion of its intrinsic value in durable high-return businesses.

The foregoing description of attitude, as well as the following historical explanation of the current situation, is repeated in the annual report each year, accompanied by a standard disclaimer designed to deter inappropriate optimism. When Wesco's parent corporation acquired control, Wesco's activities were almost entirely limited to holding (1) some surplus cash, plus (2) a multi-branch savings and loan association which had many very long-term, fixed-rate mortgages, offset by interest-bearing demand deposits. The acquisition of this intrinsically disadvantageous position was unwisely made, alternative opportunities considered, because the acquirer (including the signer of this letter) was overly influenced by a price considered to be moderately below liquidating value. Under such circumstances, acquisitions have a way of producing, on average, for acquirers who are not quick-turn operators, low to moderate long-term results. This happens because any advantage from a starting "bargain" gets swamped by effects from change-resistant mediocrity in the purchased business. Such normal effects have not been completely avoided at Wesco, despite some successful activities, including a large gain in 1985 from an investment in General Foods.

A corporation like Wesco, with no significant proportion of intrinsic value in great businesses, continues to be like a tortoise in a race of hares. And, as we have demonstrated in one more year, this particular tortoise is not very sprightly. Moreover, what sprightliness remains is often deterred by remembrance of past new-activity outcomes which were at least as bad as those of the writer's dog when it limped home from its first foray outside the yard both (1) injured by a car and (2) bloated from overeating garbage. (Some long-time Wesco shareholders may painfully remember one such once-new activity: hillside subdivision in the place with the ironic name, "Friendly Valley.")

On January 25, 1990, Wesco increased its regular quarterly dividend from 19½ cents per share to 20½ cents per share, payable March 13, 1990, to shareholders of record as of the close of business on February 28, 1990.

This annual report contains Form 10-K, a report filed with the Securities and Exchange Commission, and includes detailed information about Wesco and its subsidiaries as well as audited financial statements bearing extensive footnotes. As usual, your careful attention is sought with respect to these items.

Charles T Munger

Charles T. Munger
Chairman of the Board

March 5, 1990