BUFFETT AND BEYOND...

Clean Surplus is a model developed by the accounting profession which allows investors to both compare stocks and predict future portfolio returns relative to the benchmark S&P 500 index. Comparability and predictability are not available through the use of traditional accounting methods. The research and later CPA reviewed portfolios indicate that portfolios made up of stocks with higher Clean Surplus ROEs outperform portfolios made up of stocks with lower Clean Surplus ROEs. The statistically measured comparisons (correlations) of high Clean Surplus ROEs and high future returns are statistically significant.

STOCKS IN BUFFETT'S PORTFOLIO
Walmart
With Comparisons to Ross Stores, Coach and Family Dollar

LISTEN TO US ON WSBR (740) AM RADIO M-F 5PM to 5:30 PM or go to our site, Buffettandbeyond.com to hear archived radio shows.

What Do We Know About Buffett?

Buffett continues (except for this year) to outperform the S&P 500 index. However, our own portfolios not only outperform the S&P, but we also outperform the Great one himself by a wide margin. In fact, since the end of 2002, the Clean Surplus portfolios have outperformed both Buffett and the S&P by more than double on a compounded basis. Of course, your question is how did we do that if we're using the same system as Buffett?

The main reason Buffett is not performing as well today as in the past is because he is handling too much money and for this reason and this reason alone he just cannot continue to generate the type of returns he did two decades ago. Here is a quote from Buffett's 2010 report to shareholders.

"Our 46-year record against the S&P, a performance quite good in the earlier years, is now only satisfactory. The bountiful years, we want to emphasize, will never return. ***<u>The huge sums of capital we currently manage eliminate any chance of exceptional performance.</u>*** *We will strive, however, for better-than-average results and feel it fair for you to hold us to that standard."*

What else do we know about Buffett? We know Buffett used and I say used (past tense) a system called Clean Surplus which was not his system, but rather a system developed by the accounting profession that allows comparability among all stocks. It is also a predictive model which gives a pretty good estimation of the future returns (stock appreciation) of a company.

I've been studying and using this system since the late 1990s. I wrote and published a Doctoral dissertation on the subject as well as a book which is appropriately entitled "Buffett and

Beyond."   I can tell you with great certainty, Clean Surplus is a great methodology for stocks. However, Buffett is presently into currencies, oil, natural gas, derivatives, preferred stocks, real estate and who knows what else? What else? Yes, he purchased an entire railroad which we know as Burlington Railroad. All in all, stocks traded on the exchanges just don't account for a major portion of his present day portfolio.

The most positive aspect of our knowledge of Clean Surplus is that we will remain loyal to the this methodology and always will because it is this system that allows us to outperform almost all of the money managers out there in investment land including Warren E. Buffett.

Let's look at one of the present holdings in Buffet's portfolio and we will see why we are able to outperform not only the S&P 500 index, but also Warren Buffett. We will look at Walmart which he is holding at the present time.

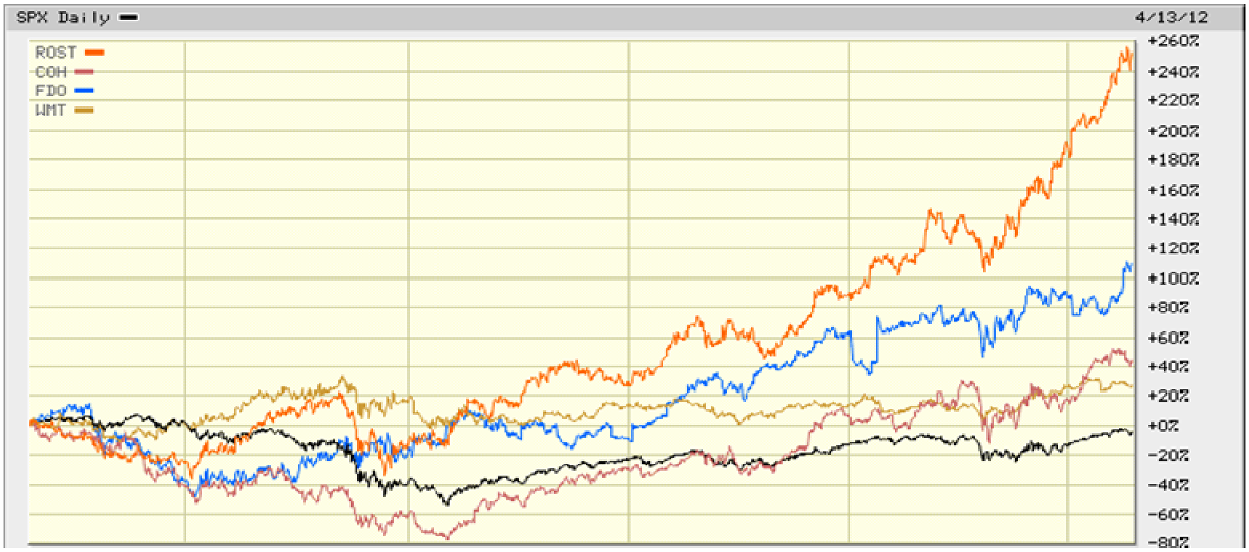
RETAIL STORE INDUSTRY					
	ROSS STORES	FAMILY DOLLAR	COACH	WAL-MART	S&P 500
Symbol	ROST	FDO	COH	WMT	SPX
YEAR	ROE	ROE	ROE	ROE	ROE
2012	23%	18%	23%	16%	13.0%
2011	25%	19%	24%	16%	13.0%
2010	26%	18%	23%	16%	13.0%
2009	23%	16%	23%	16%	13.0%
2008	18%	14%	33%	17%	13.5%
2007	16%	15%	37%	17%	14.5%
2006	17%	15%	39%	18%	14.5%
5 Year Return	240%	105%	50%	40%	5%
DIV	1.0%	1.2%	1.5%	2.6%	2.0%
YTD	25.0%	12.0%	23.0%	1.5%	2.0%

Clean Surplus allows us to compare stocks in the same manner as we would our bank accounts. The ROE you see above is NOT the traditional accounting ROE but rather the ROE configured by Clean Surplus. All you need to know in order to compare stocks in a Clean Surplus manner is to think of your bank account. The S&P 500 **bank** is returning us 13%. The Walmart **bank** is returning 16% on the money investors have put into the Walmart bank which means we would rather invest in Walmart than an index fund representing the S&P 500 index.

Now look at Family Dollar. It is a bank returning 18%. We like that, but we like Ross Stores and Coach even better as they are banks with ROEs of more than 20%.

We try and fill our yearly portfolios with stocks from the S&P 500 index which have a Return on Equity (in a Clean Surplus Condition) of 20 % or greater. Buffett has Walmart in his portfolio which is a bank paying him 16% this year while **WE** have both Coach and Ross Stores in our portfolio both of which are banks returning more than 20%.

If Clean Surplus is a predictor of how well a stock will perform, Coach, Ross and Family Dollar should be outperforming Walmart and all of these stocks including Walmart should outperform the S&P 500 index. Let's look at a 5 year chart of these stocks along with the S&P 500 index.



This chart is a 5 year chart of the stocks we just analyzed as of April 12, 2012. If Clean Surplus is a good predictor of returns we should see Coach, Ross Stores, Family Dollar and Walmart outperforming the S&P 500 index. On the chart, the black, bottom line is the S&P 500 index which shows us that all the stocks predicted to outperform the S&P did indeed do so. The top line and best performer is Ross Stores (ROST) returning about 240% in the past 5 years ending April 12, 2012. Family Dollar is next with a 105% return followed by Coach with a 50% return and finally WalMart with a 40% five year return. Notice the market as measured by the S&P 500 index returned a negative 5%, but with dividends of 10% over five years actually returned a positive 5%.

Notice from the table above, that our two portfolio holdings, Ross Stores and Coach are up 25% and 23% YTD (Year to Date).

We've had Coach in our portfolio for a long time and just added Ross Stores at the end of 2010, but the bottom line here is that our portfolio consisting of stocks with a 20% or higher ROE should continue to outperform not only the S&P 500 index (13% ROE), but we should also continue to outperform the greatest investor of all time, Warren E. Buffett.

You can see it is relatively easy to select a portfolio which will outperform most money managers out there in investment land just by looking at their Clean Surplus generated ROEs. The difficult part is putting the numbers together in order to generate this Clean Surplus ROEs. But then again, you know us and putting together numbers is what we do for you.

See you next time.

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