Table of Contents

Copyright

© 2013 Jason Rivera

Dedication

For my wife, kids, and family. Thank you for being there over the years and supporting me through everything. I would not have been able to do this without you.

Acknowledgements

"If I have seen a little further it is by standing on the shoulders of Giants." Sir Isaac Newton

Thank you to John from CSInvesting, Red from The Red Corner Blog, Taylor From Valueprax, Jeff, from Ragnar Is A Pirate, John from Shadowstock, The Brooklyn Investor, The Fundoo Professor, and all other value investing and related blogs for sharing your knowledge, conversations, and encouragements over the years. You all have had an extraordinary impact on my life and me as an investor and I would not be where I am today without all of you. Thank you so much.

Thank you to Dr. Wes Gray and Tobias Carlisle, authors of Quantitative Value, for your feedback and encouragements. This book is infinitely better because of the feedback from you both.

Thank you to Benjamin Graham, Warren Buffett, Seth Klarman, and Joel Greenblatt for sharing your experience and wisdom with the world.

Thank you to Tim Ferriss for sharing how to hack the world and sharing your adventures. Without the Four Hour Work Week and the sharing of your amazing life adventures I would have never had the motivation to finish writing this book.

Thank you to Eda Nelson and Chen Vincent for believing in the book enough to preorder it.

Introduction

"All intelligent investing is value investing--to acquire more than you are paying for. Investing is where you find a few good companies and then sit on your ass." Charlie Munger

I originally started my value investing blog, Value Investing Journey, and now this book, because I was frustrated that I could not find any other single site, group of sites, or books that talked about the things are in this book. Most value investing blogs will talk about the companies they think are good investments, show some basic valuations, talk about why they think the particular company is a good investment, and go into some detail about the company's operations. This approach is fine if you already know how to value and evaluate companies. If you do not however you are in for a very long, often times frustrating journey, through the infinite internet until you are finally able to piece enough disparate information together to start the process of learning and implementing valuation techniques, thought processes, and how to properly gauge whether a company is a potentially good investment into your own repertoire.

When the Value Investing Journey blog was started it was to keep a journal of my thoughts and valuation and analysis articles so that I could see what I was learning, how fast I was learning, and as a way to see how far I had come in the time since the blog was started. There was one other major reason it was begun and why this book was written. I wanted to help newer to intermediate level investors who like me could not, or did not, want to go to a big time university to learn the techniques that will be shown and talked about in this book so that you could jump-start your own investing journey a lot faster than the nearly 5 years it has taken me to gain the knowledge that I have. Throughout this book, and on the accompanying blog, I will show you and give you access to all the best information I have learned from, that took me thousands of hours to put together. You will be shown how to do the valuation techniques for yourself, talk about my investment thought processes and why I did what I did, and you will be given all the tools and necessary information so that you can also become an excellent investor without going to college and without having to spend potentially tens or hundreds of thousands of dollars. With this book and the accompanying blog you will not only be saving potentially hundreds of thousands of dollars on tuition costs, but you will also save potentially thousands of hours of time as well.

The premise of this book is very simple: You no longer need to go to an expensive Ivy League level school to learn how to become an excellent investor, and you will be shown the steps I took to teach myself about investing to become an excellent value investor. Almost 100% of the information that was learned was found free online but supplemented with books which is where the minimal costs came from. Since I have dealt with extreme dizziness since I was a senior in high school, I am now 26, and have not been able to go to college and do the typical Bachelor's degree in finance coupled with an MBA, finding a mentor and working for an investment firm of some kind. All of the learning I have done was on my own through the internet and its various websites, blogs, articles, newsletters, and books that were found or recommended where the disparate pieces were very slowly put together. This book will boil down all the important information that has taken me years to learn and if you have the right mind-set and drive to learn and practice the techniques and processes that will be shown than you too can become an excellent value investor.

The main reason it took me so long to learn the processes that will be shown throughout this book are because I have never been able to find one or even a few resources to learn from that taught all the techniques that will be shown in this book. One site may talk about the basics of investing but stops there, the next may show you advanced techniques that make no sense to you and could be written in Chinese for all you know since it is just a confusing blob of information, another site may show you basic valuation techniques but not what they mean or how to learn how to do them yourself, and the list goes on all the while eating into your precious time. This lead to frustrations and monetary loss either through losing money in the market like I did or delaying you from making money in the market because you are not confident in what you are doing.

It has taken me nearly five years reading thousands of books, articles, blogs, etc, probably tens or hundreds of thousands of pages of information, and thousands of hours practicing to get to the point where I am and feel like a lot of that time was wasted on stuff that didn't really matter in the grand scheme of things about how to evaluate a company. The reason I am writing this book because I want to help newer to intermediate level investors save potentially years of time by teaching you how to properly evaluate a company's prospects by reading its financial reports and any other information you can find online about the company, its management, competitors, and industry. Along with showing you the steps I took to learn what I have, you will also be shown various valuation techniques, taught how do to them, learn what they mean for the overall investment thesis, and be shown how to adjust the numbers so that you can cater them to your particular needs since every investors mind-set and needs are different. It took me a while to learn how important valuation is in terms of knowing whether a company is a good one to invest in at the time. Valuation is of utmost importance not only so that you do not buy into a company that is overvalued but also because it will let you decide what a company is worth so you can determine what a proper margin of safety is so that you can buy underneath that price. This is necessary because if you do make a mistake in your valuation or analysis you will still have a chance to make money by buying into said company at a substantial discount to it estimated intrinsic value. I will show you how to do this and much more by showing you real life valuation and analysis articles that I have written where you will be shown the thought process that I had while evaluating the company and how I came to my conclusions.

Like the premise of this book the structure of it is very simple and straight to the point as well. The first two chapters of this book are an introduction where I will talk about what originally got me interested in investing, how I started, some of the challenges I have had to overcome in the intervening years, and what finally got me to become serious about learning about investing. I will also detail some of the many mistakes I made early on to warn you and hopefully save you the investment money and time that was lost. Chapter three will tell you about my investment philosophy so that you can get an idea of where I am coming from when I talk about why I thought certain things while evaluating a company and my overall thought process. The rest of the book will be showing you the valuation and analysis articles, explain how to do everything, show you where the techniques were learned from and pointing you to those sources so that you can learn from them if you want deeper knowledge on the techniques.

If you want to become an excellent investor faster by spending less than continue on and learn from my value investing journey where I will show you how you too can become an excellent investor without having to go to college.

Chapter 1

"If your goal is to beat the market, an MBA or a Ph.D. from a top business school will be of virtually no help." Joel Greenblatt

I have always liked the thought of investing since learning the very basics of it and the power of compound interest during my senior year of high school in 2004/2005. At my high school every senior had to take one semester of government and one semester of consumerism; a kind of hybrid class that taught about a lot of different subjects one of them being the basics of investing. The power of compound interest which I did not fully understand at the time, and probably still do not understand fully, was one of the main things taught during the investing portions of that class along with basic investing ratios, what dividends were, and other very basic investing concepts. At the end of the class for the semester there was a project where we got put into groups of three or four people and found companies to invest in and invested money in those companies in a fake money account online. The group whose portfolio went up the most in the few week experiment won the contest and got the highest grade for that particular project.

I ended up being the leader of my particular group mainly because I was the only one who was very interested in the concept of investing in companies and the others in my group showed almost no interest in stocks or investing in general and just seemed to want our senior year to get over with as soon as possible while doing as little work as possible. The first batch of companies we picked were ones that typical hormone fueled teenage boys might pick to buy into (Playboy, Nike, etc.) I do not remember picking those particular companies for any reason other than we liked the products as they pertained to Nike, and thought that it would be cool to be Hugh Hefner and own Playboy (For the articles of course). This was the depth of our analysis on the first batch of companies that our group bought into. As the weeks went on and the school year got closer to ending, being normal seniors, the other members of the groups' interest dropped even further to becoming almost nonexistent and I was the only one still doing work on the project as the semester was getting ready to end.

Since I was pretty much left to my own devices, at that point I decided to start actually doing minimal research on a company that would be a fantastic investment not only for the class project but over the long term. The company was overtaking its competitors very quickly, it had its IPO within a year or two of that time frame, and was quickly becoming one of the most used and well known sites in the world. Again, this was the depth of the analysis at that time. Even then with my very limited knowledge I recognized without even knowing it what later I would call and look for in companies, a sustainable competitive advantage, or moat that made the company very attractive to own and something that a lot of investors look for when buying companies. Since I was, and still am, extremely competitive and wanted to win the contest, I dumped all of the other stocks in the portfolio that we bought just because they were cool and put the entire fake money portfolio into buying stock in this one company that was valued somewhere between \$60-\$70 a share if memory serves me right.

The company's stock did not end up going up enough for our group to win the contest but I was proven right over the long-term as the company that the entire fake money portfolio was put into,

$100,000, was selling for between $60-$70 a share at that time. If I would have held those 1428-1666 shares of stock until this present writing with the company now selling for around $793 a share I would have turned that original 100K fake investment into between $1,132,404-$1,321,138 in eight years. That comes out to a compound annual growth rate (CAGR) of between 35.44% and 38.08% respectively. As an example of how phenomenal that is Warren Buffet, widely regarded as the best investor ever, has averaged a CAGR of 20% over 40 years so the potential gains would have been incredible.

This potential result while phenomenal was almost completely luck due to the lack of any kind of in-depth research and analysis on my part but it did teach me one very valuable lesson that I still adhere to today. If you buy stock into a company that has huge market share and a sustainable competitive advantage, over time you will do very well in investing. Combine that with other factors such as the company's margins, its competitors, industry and making sure a company is either undervalued by a substantial margin or fairly valued, and the results can be fantastic.

For those who have not guess the company that we would have made a killing on if it was a real money portfolio, it is the worldwide search engine leader, one of the biggest and most innovative companies in the world, Google, stock ticker (GOOG.)

Thus my first lessons in competitive advantage, market share, compound interest, and opportunity cost left an indelible mark on as I still vividly remember those lessons to this day and helped to kick-start my value investing journey.

Chapter 2

"Why do we fall? So we can learn to pick ourselves up." Thomas Wayne, Batman Begins.

During my senior year of high school I also started getting dizzy spells often that made me nauseous and dizzy to the point where I could only lay down and watch TV until the feeling went away. This problem, which still persists to this day, only got worse over time and for the better part of three or four years after graduating high school all I could really do was lie around and watch TV. Luckily I found some doctors, physical therapists, and others who have somewhat figured out my problem and I have been slowly…….very slowly, getting better since around 2007 or 2008. During this whole time I have only been able to work at a paying job for around three month's total over nearly 10 years.

In 2009 we found out that my wife was pregnant with our first child which left me a bit stunned and made me scramble to figure out something I could do while still dealing with my dizziness all day every day that I could eventually make money at. The three things I came up with at that time were getting involved in local politics but I figured the world didn't need any more scum bag politicians. I thought about becoming a writer but at that time didn't really have any passion for writing and remember being told by one of my teachers in high school that "Hopefully you never want to become a writer because you are really bad at it." She was right as I was absolutely awful at that time, even worse than now if you can imagine that. The only other thing I came up with at the time was remembering how much I liked learning about stocks and the stock market when I was in high school. I finally decided to go down the path towards learning about investing not necessarily because I was excited about it but because out of the ideas I came up with it was the only one I even remotely liked.

By this time I had completely forgotten everything learned in consumerism class in high school other than how amazing compound interest is and the money I could have made if I would have invested real money in Google. Armed with this exciting and depressing memory of what could have been with Google, I started relearning the basics by reading book after book and any website I could find that looked like it had decent information. Slowly after gaining what I thought was enough knowledge (Looking back I am appalled that I started investing real money with the very limited amount of knowledge then) I started investing REAL money in companies who had good-looking ratios. Sadly to say that was pretty much my only basis of research before buying into a company at that time. I was not even looking at balance sheets, cash flows, reading annual or quarterly reports, no valuations of any kind, and only did very minor research into what the company even did for business, YIKES!

This begins the first lessons that you can learn:

1) When you think you know enough about investing to start using real money stop yourself and invest in a fake money portfolio, watch your returns for a while and learn from your mistakes so you do not lose real money like I did.

2) If you are going to be serious about investing you need to read at the very least: The company's most recent annual report called a 10K, the company's most recent quarterly report called a 10Q, and the company's most recent proxy report which outlines things likes how much management gets paid and how they get paid, how much certain companies and people own of the company including company insiders, and if there are any family or related party transactions. I would actually recommend reading AT LEAST five years (I generally read at least 10 years worth of annual reports now) worth of annual reports, but starting with one year is better than nothing.

3) DO NOT invest in a company just because it has "good looking ratios" or because you have heard that the company is about to come out with a fantastic product, or that the company has amazing future potential, etc. This is almost all hype and usually does not end up coming to fruition and you will most likely lose money if you invest off of hype like the previous examples. Do your own in-depth research and invest in companies that way or you will get punished like I did.

Mr. Market, Benjamin Graham's term for describing the stock market, saw that I was making a mockery of him by only investing real money with minimal knowledge and decided to punish me for it. Because I only invested in companies that had good-looking ratios, a good chunk of my portfolio was in Chinese small caps and shortly after starting to invest in them rumblings started coming from all directions that a lot of these companies were nonexistent in some cases, their financial statements were not accurate, and that some were outright lying to customers and shareholders. Various other problems also started to come out about Chinese small caps shortly after I decided in my infinite wisdom to put half of my portfolio into these small Chinese companies. The continuous bad news led people to flee these stocks leaving me with around a 50% decline in my portfolio in a matter of months after starting real money investing. Luckily I was smart enough to only invest a small amount of money at that time so the absolute loss ended up being only about $500 but it still stings and embarrasses me to this day how naïve I was then.

After this happened I took a breath and reevaluated what I was doing and what I wanted to accomplish through investing. What I was doing then was not actually what I would consider investing now. What I was doing then I consider speculation, akin to gambling, since I was doing only minimal research into companies before deciding to buy into them and which is a big no-no if you want to truly become a better investor. I had a realization at that point that if I wanted to get serious about becoming a true investor and stop losing money that I needed to dedicate myself to the craft, cut out outside distractions, and actually learn how to evaluate and value companies properly before deciding to buy into them. I either needed to do this or stop investing completely because if I kept doing what I was doing I would have ended up losing a lot more money.

Sometime around then I found John Chew's amazing site, now csinvesting.org, which at least partly saved my investing and my family's financial future. Through his site I learned a lot and still learn a lot about how to evaluate and value companies and owe a good part of what I know and have become as an investor to him and his site and would highly recommend it to anyone who wants to become a better investor. Shortly after finding his site and taking Aswath Damodaran's free online course on how to value companies, which I would also recommend, I decided to completely dedicate myself to becoming a true value investor and set myself on that path.

However, even with his wonderful site and the hundreds or thousands of other sites, books, blogs, articles, etc that I have read, specific information that was sought was still too far spread out in my opinion and I have not been able to find one book or site that encompasses even close to everything that I will share throughout this book. It has taken me almost five years to get to the point where I am at now and I think I can help you save months or years of time by teaching you specifics on how to evaluate and value companies. There is no one right way to do things and I will be showing you the ways that make the most sense to me. The best thing I can recommend to anyone who wants to become a better investor is that as soon as you get comfortable with the concepts and terms that will be shown in this book is that you should go and start reading annual and quarterly reports for public companies and start practicing the techniques and start taking notes on the companies you are researching so that you can evaluate and value the company for yourself. I can only help to show you the way to becoming a better investor but you have to walk down the path yourself.

Chapter 3

“Nothing in the world can take the place of Persistence. Talent will not; nothing is more common than unsuccessful men with talent. Genius will not; unrewarded genius is almost a proverb. Education will not; the world is full of educated derelicts. Persistence and determination alone are omnipotent. The slogan ‘Press On’ has solved and always will solve the problems of the human race.” Calvin Coolidge

Throughout the rest of the book you will be seeing my actual analysis and evaluation articles where that will show you the valuations and analysis that I have done on real world companies. You will be shown how to value companies using various valuation techniques and how to adjust the numbers for yourself, and what those numbers and valuations mean for the overall investment thesis. You will also be shown my reasoning’s and thought processes for why I decided what I did and why the particular company was a buy or sell decision for me at that particular point. Before we get to that though I need to state my investing philosophy so that everyone knows what frame of mind I am approaching the analysis with.

I look for companies that have some combination of the following criteria: Some kind of long-term sustainable competitive advantage, or moat as it is also called, companies that produce and sell products in niche markets, companies that I find to be substantially undervalued, have very good management, high insider ownership, are fantastically profitable, have a lot of cash and/or hidden assets, etc.

I only take into consideration in the valuations and analysis what I can see now, and pay almost no attention to rumoured future possibilities or estimates of revenues and margins into the future. The only time future possibilities play even a small role in my articles are in situations where there is a clear catalyst: Activist/value investing firm or individual involved, the company is undergoing a strategic review and is owned and controlled by a few people as in the case with Dole (DOLE) that you will see later in the book, or the company’s management is trying to figure out ways to unlock the companies undervaluation by asset sales or spin offs as in the situation with Vivendi (VIVHY.PK) that you will see later in the book. Even with the above mentioned companies I only valued and analysed the company as it stood then, and treated future potential as icing on the cake that played almost a zero role in the evaluations.

My number one rule when I buy into a company is preserving capital and making sure that I do not lose money. The fewer losses I have, the more money that is kept and is able to compound faster when I do find winners so I am a very strict, disciplined, and conservative value investor. I generally only buy into companies that are selling at a substantial discount, or margin of safety, to my estimate of value for the company so that this way if I do make a mistake in the analysis or valuations then I will still have a chance to make some money. I usually look for a catalyst that could help unlock the undervaluation of a company such as: Potential for spin-off or asset sale, land or buildings that are not being used that could be sold, activist funds/investment firms that own stock in the company and could push for changes to be made, etc. I try to find areas of the market where a lot of investors do not or cannot invest and I generally only research companies that have market caps of less than $100 million or special situations like spin offs. Now that I am more confident in my abilities to value and evaluate companies I do not hesitate to put 20+ percent of my portfolio into one or more companies. The fewer companies I own the better I know each company. I am also a very contrarian investor and try to find companies that are either unknown, unloved, or are having problems for potential investments as well. The less competition there is the better when looking for investments so I try to steer clear of the herd who generally concentrate on bigger companies. I do not forecast numbers years or even months in advance at all and only value and analyze what I see in the company now so you will not see any DCF valuations in this book. There are a lot of books out there that explain how to do DCF valuations and I would highly recommend Aswath Damodaran's free online course on valuation where he teaches how to do DCF valuations if you are interested in those kinds of valuation techniques.

I generally plan to hold the companies I buy for years, decades, or hopefully forever if it turns out to be an exceptionally good company and generally only plan to sell if the companies if their share price rises to the high-end of my valuation range quickly or far above what I think its intrinsic value is after I have bought into it, or if I can find another company that I think is a better investment.

Having stated all of this you now have a frame-work for my thought process going forward and how I manage my personal portfolio and the other portfolios that I manage. If you come across any terms that you do not know refer to investopedia.com as it is the best site I have found that explains investing terms and it is still a site I use to this day when coming across things I do not know or understand. If you do not find a definition that you find satisfactory or just want to study something further you should search for the term, person, book, etc on my blog or through Google.

I would also like to mention that I have received no formal training in evaluating companies and some of the ratios that will be talked about throughout the book I came up with on my own and have never seen used anywhere else such as the total obligations, commitments, and debt/EBIT ratio which will be talked about later. I am sure that some professional investors and college professors out there will say that I am technically probably not doing some of the things in this book properly or "How they should be done" but since I had to learn on my own, I have learned to do things that make sense to me, help me to understand the inner workings of a company, and help me to make an informed decision about whether or not a company is a good investment. In my opinion understanding these things in your own particular way, which makes sense to you, is more important than doing things just because someone else says they are proper. If something in this book doesn't make sense to you, don't use it, find your own way to make sense of things, and come back to it later. This book is meant to be a practical guide of learning how to evaluate and decide if a company is a good investment without having to spend potentially hundreds of thousands of dollars on a college degree. Use what makes sense to you, skip the rest, and come back to it later when it does make sense to you and you want to learn how to use it.

One piece of advice before we get to chapters about technique and analysis is that at the beginning of each chapter I will state which company I am valuing and analysing. If you want to get the most out of this book once you get comfortable with the terms and techniques you should stop reading after finding out the company and time period the evaluations were done and go online to Morningstar.com or the company's website and download the annual, quarterly, and proxy reports from the time period mentioned. If you are a new investor I would recommend starting at the beginning of the book and go chapter by chapter because the book is structured to start slow with easier concepts and a lot less information. I then build up to harder to understand concepts as it can be very easy to get overwhelmed by some of the later chapters if you are just starting out. I also built this book with more advanced investors in mind who only want to learn about certain specific techniques. In the title of each chapter you will be shown which company the chapter is about, the stock ticker in parenthesis, the time period the company was researched, and what will be talked about in the chapter so you can go back and read those financial reports and skip to specific chapters if you want to learn a specific technique.

I highly recommend reading though the chapters, writing down some of your own notes, thoughts and valuations and then come back and read the analysis, valuations, and my thought and decision-making process to see if we came to different conclusions. This is a very good way to practice the techniques that you will be shown and will help you retain more information faster. We may come to similar conclusions or we may not, and just because we may come to different conclusions does not mean either of us is wrong. As long as you put thought into your analysis, do the research, and come to logical, unemotional decisions only Mr. Market can decide after a few years whom is right or wrong. Learning a sound investment process that makes sense to you and leads you to logical, unemotional investing decisions should be very high on your priority list because if you do develop those traits you will generally do well investing over time. Anyone can learn the techniques and terms in this book, not everyone can develop or have the proper investment thought processes and other traits that will be talked about later to become an excellent value investor. If you can come up with a very sound investment process then you will already be far ahead of most MBA's and professional investors who generally invest with the herd and let their emotions take control of their decision-making process.

For the rest of this book you will be shown real life valuation and analysis that I have put together on companies. For further insights and to learn from people who have commented on some of my research I have listed ways below to view the original articles and the comments and discussion they have garnered. Some of the comments on my articles have had very valuable information in them that I have learned from and would highly recommend going to the following sites for further discussion. You can go to the following pages and search for the specific articles which will have the comments at the bottom of the pages.

- My Blog-Value Investing Journey
- Seeking Alpha author page: **http://seekingalpha.com/author/jason-rivera/articles**
- Guru Focus author page: **http://www.gurufocus.com/news.php?author=Jason+Rivera**

Chapter 4 Vivendi (VIVHY.PK) June 2012. Asset Reproduction and Sum of the Parts Valuations. Spin offs, Asset Sales.

"The important thing is not to stop questioning. Curiosity has its own reason for existing. One cannot help but be in awe when he contemplates the mysteries of eternity, of life, of the marvelous structure of reality. It is enough if one tries merely to comprehend a little of this mystery every day. Never lose a holy curiosity." Albert Einstein

- **Vivendi**

Vivendi (VIVHY.PK) combines the world leader in video games (Activision Blizzard ATVI), the world leader in music (Universal Music Group), the French leader in alternative telecommunications (SFR), the Moroccan leader in telecoms (Maroc Telecom), the leading alternative broadband operator in Brazil (GVT), and the French leader in pay-TV (Canal+ Group). The previous information was taken from Vivendi's website. I will get to further descriptions of the subsidiaries later.

For a discussion of the unsponsored Vivendi ADR, versus the foreign listing of Vivendi (VIVEF.PK), view the comments in http://seekingalpha.com/article/523121-vivendi-undervalued-french-media-and-telecom-conglomerate.

I have used two different valuation techniques for Vivendi. The first is an asset reproduction valuation done on 4-2-2012. All numbers are in millions of Euros unless otherwise noted, except the per share numbers. Valuations were done using 2011 10K.

Assets:	Book Value:	Reproduction Value
Current Assets		
Cash	3,304	3,304
Marketable Securities	1,544	1,544

Accounts Receivable (net)	6,730	4,500
Inventories	805	500
Prepaid Expenses	0	0
Deferred Taxes-Tax Liability	700	400
Total Current Assets	13,083	10,248
PP&E Net	9,001	6,000
Goodwill	25,029	12,514.50
Intangible Assets	6,814	3,407
Total Assets	53,927	32,169.50

- Number of shares is 1,242 million.

Reproduction value:

- With IA 32,169.5/1,242= 24.90 Euros per share = $34.24 per share
- Without IA 28,762.5/1,242= 23.16 Euros per share = $30.62 per share

Current share price on 4-21-2012 = $16.50 per share

Sum of the parts valuation done on 4-26-2012 all numbers in millions of Euros unless otherwise noted, except per share data.

- 44% of SFR bought in 2011 for 7,750 Euros. Implied value of total stake since Vivendi now owns 100% of SFR = 17,360 Euros
- 60% of Activision (ATVI) =6,587 Euros

- 100% of SFR + 60% of ATVI =23,947 Euros = $31,629 million

Vivendi has a total market cap currently of $23.46 billion

You are getting most of the 60% of ATVI, all of GVT, all of Canal+, all of UMG, 53% of Maroc Telecom, which equals 5.41 billion Euros, all cash and debt for free, just by purchasing part of ATVI and all of SFR. GVT, Canal+, UMG, and Maroc Telecom are the rest of their subsidiaries whose operations will be described later.

Valuing the whole of Vivendi, cash, and debt using my above estimates, I am estimating a very conservative 40 Billion Euros, which equals $53.832 billion of total value for Vivendi.

- $53.832 billion/number of shares at full dilution of 1.250 billion= $43.07 per share
- Current share price = $18.60 per share

This valuation would be used if it were to do a spin-off or selling some of its assets and companies.

The reproduction valuation is generally the most conservative intrinsic value estimate and the one I use the most since I am very conservative and want the biggest margin of safety as possible.

Some other things I like about Vivendi besides the massive margin of safety are: It pays a healthy yearly dividend, has consistent free cash flow of at least 3 billion Euros per year after cap ex, very good margins, cash and cash equivalents of over 3 billion Euros, and it also has net operating loss carry forwards of around 8 billion Euros.

Seth Klarman owns shares of Vivendi at his hedge fund Baupost Group, and has been buying more recently. I actually got lucky and bought shares of VIVHY at a cheaper price than Klarman. Also the management of Vivendi is reviewing what it could do to unlock the value that is missing right now, by its own estimates at least 40%.

Risks: A lot of debt and continual huge amounts of cap ex in the telecom subsidiaries. The continuing European debt issues, with most of its business being done in Europe, specifically France. If it decides not to do a spin-off or asset sale it could take a while to unlock value, which would not bother me since it would enable me to acquire more shares.

I would like it to eventually do some kind of spin-off or asset sale to pay down its debt, which should also increase the share price. I would not mind if it cancelled the dividend for a year or two to pay down debt either.

Description of subsidiaries:

Activision Blizzard description - World's biggest video game company, and in my opinion has the best overall portfolio of games in the entire industry. Call of Duty, Skylanders, Diablo, Starcraft, World of Warcraft, among others are included in the portfolio. This is the asset that I think would make the most sense to sell or spin off.

Call of Duty produces over $1 billion of revenue by itself with every game produced, which comes out once a year usually in November.

However, most of these franchises have either just come out with games or are past their prime in my opinion. World of Warcraft, while still a cash cow, is gushing subscription members every month, and Blizzard has already started to move resources into the next MMORPG, which has no release date. Diablo III just came out so I don't expect another game in that series for a while. Call of Duty, while still producing huge revenue and profits, is at its peak in my opinion and can only go down from here. The development studio that makes the Call of Duty series has also been fighting with and losing a lot of team members over the last several years, which will hurt quality in the future.

I also see the entire console video game industry in a decline as well. You can only keep asking people to pay more for less for so long before they decide to stop buying games and consoles, especially with cheaper games coming out either free to play or for under $10 on tablets and phones.

The next generation of gaming systems is going to start coming out later in 2012. That is generally a bad thing for game publishers because of higher development costs and lower profitability. Thus another reason it should sell before the new consoles start coming out.

In my opinion now would be the perfect time to sell ATVI. Vivendi will likely never be able to get a higher price than now due to the above. The only problem would be finding someone big enough to buy.

GVT description - A fixed phone line and internet telecom with operations in Brazil who Vivendi recently bought. GVT has great growth potential but will cost a lot in the short term due to high amounts of cap ex in the telecom industry. Should be one of the better Vivendi holdings over the long term though as the margins are currently very good. My main concern with this one is that Vivendi over paid for it so it will take longer to recoup the initial investment. Also being in Brazil, you never know what company might be expropriated by the governments in South America.

Maroc Telecom description (MAOTF.PK) - Maroc Telecom is a mobile/internet/fixed line phone company with most of its business in Morocco. It has the same problem with cap ex as GVT above, especially since it is going to be transitioning into 3G coverage from 2G. That could eventually pay off however due to more data plan subscriptions from the smart phones that will run 3G. Maroc has also been having problems with the government in Morocco as it has had to cut phone rates, thus losing out on revenue and lowering margins.

Canal+ description - A pay TV/cinema company with operations mainly in France. Canal+ is another asset I could see the company spinning off or selling because it currently owns 80% of Canal+ France and has been trying to buy the remaining 20% to no avail, which could lead it to sell its portion of it. It does own the rights to show Ligue 1 soccer matches and UEFA Champions League matches in France, which is a major advantage.

Universal Music Group description - Biggest owner of music and music publishing rights in the world. UMG produces the lowest EBITDA and CFFO margin of the entire group. Also doesn't seem to fit the profile of the rest of the subsidiaries, which might lead this to being sold. However, it owns the rights to music from the likes of: Rihanna, Lady Gaga, Justin Bieber, Eminem, Taylor Swift and various other major music artists. The music industry could also see a comeback to higher profitability with things like ITunes, Pandora and Spotify though if it can figure out how to monetize the publishing rights properly.

Description of SFR - A mobile/fixed phone/internet telecom with operations mostly in France. Currently Vivendi's biggest revenue generator and probably the most important to the group's success in the future. SFR is currently facing some headwinds in France, having to cut rates, which are lowering margins. SFR is also facing new, tougher and cheaper competition in its market, which is currently lowering margins and causing a loss of subscribers. It is also losing some business due to the difficulties of the European economy and the loss of discretionary income by some individuals. Vivendi recently bought out the remaining 44% of SFR from Vodafone, which in my opinion it overpaid for, but should hopefully pay off in the future when and if SFR's operations turn around.

Analysis Explanation

For the rest of this book every company’s valuations and analysis chapters will be left to the most part intact from the period I originally wrote it with only minor grammatical, formatting, and editing changes made.

This is the first true valuation and analysis article that I published. Looking back now I would have done a few things differently (Add debt into the sum of the parts valuation, add in the net operating loss carry forwards, and some other things that we will talk about later) but overall this is a good starting point for this book. The entire thesis after evaluating Vivendi was that they were extremely undervalued, at least 40% by managements own estimates, and that there were potential short and medium term catalysts that could help unlock this undervaluation. The company was going through what is called a strategic review at the time where management was trying to figure out ways to improve the price of the company’s stock and were talking about either doing a spinoff of one of its subsidiaries to current Vivendi shareholders, or outright selling one of the subsidiaries to a third-party. The reason for doing this was that Vivendi is hoping that it could use the proceeds from a spin-off or asset sale to pay off company debt, which was substantial at the time, to become a more focused and profitable company which would hopefully help raise the share price and in turn the perceived value of the company.

Vivendi management was further incentivized to do a spin-off or asset sale of some kind because debt rating companies were threatening to downgrade the company's debt rating to just above junk level if it was not able to lower its substantial debt load. The lowering of an entities debt can be a very bad thing as this makes it harder for the company to raise debt, it makes it more expensive to raise debt, and it can raise the interest rate on the company's current outstanding debt which would lead to a further decrease in profitability due to higher interest and debt related costs.

The factors I talk about in the article, combined with the factors directly above and below led me to believe this company was a good buy. Management was incentivized to do some kind of spin-off or asset sale to raise cash and lower the company's debt, I was buying the company at a substantial discount to the intrinsic value that was calculated for the company, (buy price around $18 a share and a minimum estimate of value of $30 per share) all of which made this company a very good, safe buy at that time. In addition to the above factors my downside was covered by several very valuable and saleable assets; in this case other companies. Some of the subsidiaries are public companies so you could gauge how much they were worth in the open market in comparison to what the total of Vivendi was worth. As an example Activision Blizzard, which Vivendi owned 60% of at the time is a public company so I checked out what it was selling for by itself. ATVI at the time was selling as a whole in the stock market for around 9.222 billion Euros or about $12.15 billion just by itself. Vivendi owns 60% of ATVI which was worth at the time $7.29 billion and it had five other subsidiaries and cash that were not even counted. Vivendi's entire market cap at the time was around $23 billion meaning that just one of its subsidiaries, one of the smaller ones at that, covered about 32% of Vivendi's entire value. Remember that Vivendi still had five other subsidiaries to count, its cash, NOL's and the subtracting of debt as well.

Asset Reproduction Valuation

For an explanation of the asset reproduction valuation, the reasoning behind it, and how to adjust the numbers I highly recommend reading Bruce Greenwald's Value Investing: From Graham to Buffett and Beyond. I learned from this book and other sources on how to adjust the numbers to get a realistic valuation but have adjusted some of the numbers further from what is recommended in the book and various other places I have learned from to meet my specific criteria, which will be explained below.

Cash, cash equivalents, short-term investments, and marketable securities: For the most part these are valued at 100% of book value. The only time I discount any of the above is if a company has operations in a foreign country and some of its money is in that foreign country. The reason I discount the cash and other above items in this case are because if the company wanted to repatriate this money back into the US it would have to pay taxes on this amount. Generally I estimate about a 40% tax rate on the portion of cash that would need to be repatriated.

Accounts Receivable Net: As a general rule I always use 85% of book value as my estimate of reproduction value. If the company needed to collect these in an emergency they could collect a pretty high portion of them if they needed to which is why I use a high estimate here.

Inventories: This is where the valuations start to get to be more art than science as what to discount this number and the ones that follow is highly subjective and dependant on what industry the company is in and how conservative of an investor you are. For example a clothing retailer who caters towards teenagers; their inventory may need to be discounted more because of how fast fashion and teenagers in general change their minds. Keep in mind for the rest of these calculations that I am an extremely conservative investor and that I want as safe a valuation as possible. I generally use about 60% of stated book value as my estimate of reproduction value for inventory. Some companies are higher, some are lower but I have found 60% is generally a pretty good estimate.

Prepaid expenses, tax assets, and other financial related assets: Again, this is highly dependent on the company and how they operate but I generally use between 40-60% of stated book value as my reproduction value estimate. As I will talk about in a later chapter these can be a very good source of float which can be a very desirable thing to find in a company.

Property, Plant, and Equipment-PP&E, net after depreciation: This one is also highly dependent on the industry but is easier to judge than some of the above amounts because you can generally find comparison values for these things. Generally I use around 50% of stated book value as my reproduction value estimate. Companies who are manufacturers and have old plants and equipment may need to be discounted by more than this amount. This number can also be deceiving though because if a company’s PP&E has been fully depreciated then these assets come off the company’s books completely. As an example a company like Dole (DOLE) who has owned some of its land in Hawaii for more than 100 years has a completely hidden asset that has been taken off the books due to depreciation that needs to be counted in the valuation and could be worth a lot of money. In the case of Dole, which will be talked about in a later chapter, potentially as much as $500 million in land value is either understated or completely off the company’s books.

Goodwill: This is one term that needs to be very carefully learned and looked at when evaluating a company as it can be dangerous if counted on too much. This is a personal bias of mine but I generally do not like goodwill and generally take 50% and under of stated book value and use it as the estimate of reproduction value. In some cases I write this completely off when finding the reproduction value of a company as it is pretty much just an accounting number that has almost no effect on tangible assets. I highly recommend reading Professor Aswath Damodaran’s many discussions on his blog about this subject to get a better idea of how this “asset” should be counted while doing valuations. Goodwill is considered an intangible asset and the following description should also be thought about when valuing goodwill as well.

Intangible assets: These are things like the value of patents, trademarks, and customer lists. I generally use 50% and under of this value stated at book as my estimate of reproduction value, again sometimes writing this off completely if it is warranted. The reason I discount these assets so much is that unless it is a long-term trademark or patent then generally these assets are not things that should be counted on for years or decades as a source of value for the company. For example how much value should a company's IA be worth in a pharmaceutical company that only makes one product that it has patented and exclusive rights to for a set amount of time, generally around 10 years. If the patent has just started it is probably fine to count all or most of the intangible assets when doing an asset reproduction valuation. But what if the patent is due to expire within 5 years and the company has no other products that are even close to coming on the market? What if the patent is expiring next year and the company's next product won't come out for 4 more years, would you want to count this whole amount in your valuation? As a conservative investor I wouldn't and generally don't like to count on things that are so-called intangible too much. This is why I generally exclude goodwill and IA from my asset reproduction valuations when dividing the total amount by the number of shares to find the per share value of the company.

Sum Of The Parts Valuation

This type of valuation is best used when evaluating a holding company or conglomerate that has a lot of subsidiaries as is the case with Vivendi or has a lot of land, buildings, and equipment that you can find approximate values for as in the case of Dole which we will get to later in the book. This valuation is one of the simplest valuations to understand but can take the longest to find all the numbers to use in the calculations. If a company is like Vivendi and has a few subsidiaries that are public companies you can just go to Morningstar or other financial sites to get the value of the company by looking at its market cap. If the company owns only a percentage of the company and not the whole thing just take the percentage of the company owned and take away that percentage of the market cap as I showed above with Vivendi's portion of Activision Blizzard. If the company owns a lot of land, buildings, and equipment, you will need to find exact or at least the best approximate values you can online. I will detail this in my chapter on Dole later and while this is still very straight forward this can be very time consuming but is necessary to do in these kind of cases because you may find a company who has a lot of so called hidden value as you will see later in the chapters about Dole and Paradise Inc.