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Personal trading examples are to demonstrate and educate individuals. They are not representative of the consistent returns in an account, or an expectation of future gains. Speaker and trainers may have other positions, which are positive or negative. Trading examples are solely for an educational purpose. Neither the information nor any opinion represented by Rule #1 Investing, Inc. or any of its affiliates constitutes a solicitation or offer to buy or sell and securities, future, or options, or other financial instruments.

You, the trader, assume the entire risk as to the results and performance of the trading methods.
Welcome to Rule #1

Rule #1 is about “Investing.”

Good Investing is about “Certainty.”

Phil Town

Earl Davis
Franklin and Buffett said it best:

“Empty the coins from your purse into your mind and your mind will fill your purse.”

Ben Franklin

“What you’re doing when you invest is deferring consumption and laying money out now to get more money back at a later time. And there are really only two questions. One is how much you’re going to get back, and the other is when.”

Warren Buffett
THIS COURSE WILL COVER:

• **Rule #1 Investing** – value investing with growth for long term success and short term cash flow.

• **Using the Four Ms** and **the Big Five Numbers** to find wonderful companies and their “true value.”

• **How to read stock charts** to be able to identify investing and trading opportunities.

• **How to use options** to **reduce** risk and increase profits on Rule #1 investments and trades.

• **How to build and manage your investment portfolio** so that you can have financial security.
Special Characteristics of a “Ruler”

• **Be patient** and eventually, your wonderful company will fix its problem and the stock market will start paying fair value or higher.

• **Pay attention to details** – rarely is anything the way that it seems. Look into the details of a company until you know why they are on sale and that they can fix their problem.

• **Manage risk** in your investing, and the profits will come.

• **Don’t quit** – ask questions until you know what you need to know to reach “Certainty”.
1) Rule #1 Investing through the 4Ms
2) Finding Payback Time to buy companies on sale
3) Analysis of a Wonderful Company from A-Z
4) How Options work and how we use them
5) A Rule One Put (ROP) and Rule One Call (ROC)
6) How Technical Indicators work and how we use them
7) Rule #1 Short Term Trading rules and strategies
8) How Credit Spreads work and when we use them
9) Risk Management and managing a trade gone bad
10) RUT Expiration Day BPS System Trade and Money Management
11) Rule One Short Strangle (ROSS) and other Ruler combination trades
12) Lowering Cost Basis and Creating Equity Bonds
13) Review and Q&A from real trading experience
Tonight’s class will introduce:

1. Our Tradition of Successful Investing
2. The Two (2) Requirements of a Rule #1 Investment
3. The Four M’s & the Big Five Numbers
4. Determining a Future Growth Rate (FGR)
5. Using the Margin of Safety Calculator
6. Calculating Payback Time
The Stock Market Is An Auction and a Voting Machine
Tradition of Successful Investing

➢ Ben Graham
➢ Warren Buffett
➢ Charlie Munger *
➢ Phil Town
➢ You.
Ben Graham was the originator of “value investing” and introduced the concept of “Margin Of Safety.”

Warren Buffett is the modern originator of Rule #1 Investing. He and his partner, Charlie Munger, brought the concept of “Moat” to the Strategy.
Phil Town brought the concept of “Meaning” to the Strategy, and thanks to the Internet, has made it available to anyone willing to put in some “work”.
Successful Investing
With One Simple Rule

Get the best of my New York Times best-sellers and learn how I turned $1,000 into $1.45 million in just 5 years.

Send Me The Best of Both Books Now

It's Free!
Buffett said, "When I got up this morning I actually looked at a stock on the computer, on the trades in London that we're buying, and it's down, and I felt good. ... We were buying it on Friday and it's cheaper this morning and that's good news."
# Phil Town’s partial list of Rule #1 Style Money Managers

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<th>Company</th>
<th>Number of Stocks</th>
<th>Total Value</th>
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<tr>
<td>Warren Buffett</td>
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<td>David Einhorn</td>
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<td>Seth Klarman</td>
<td>The Baupost Group</td>
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<td>$6,141 Ml</td>
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<tr>
<td>Mohnish Pabrai</td>
<td>Pabrai Mohnish</td>
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<td>$481 Ml</td>
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<td>Julian Robertson</td>
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<td>Lou Simpson</td>
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<td>Fairfax Financial Holdings</td>
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<td>$1,462 Ml</td>
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Tonight’s Class

• Rule #1 Investing – a long tradition of success!
• The Two (2) Requirements of a Rule #1 Investment
• The Four Ms
• Determining a Future Growth Rate
• Margin of Safety Calculator
• Payback Time
Two Requirements Before We Invest

1) It must be a Wonderful Business
   -- we understand it (Meaning),
   -- it has a durable, competitive advantage (Moat)
   -- it is being run by passionate, talented, honest people (Management).

2) It must have an Attractive Price (MOS) and/or (PBT)
   to know what “attractive” is, we must know its fair value, i.e.
   .... what is it worth as a business today based on the profits that it will produce in the future?
Don't think you have to be an expert to profit from stocks:

"The stock market just offers you so many opportunities, thousands and thousands of different businesses. You don't have to be an expert on every one of them. You don't even need to be an expert on 10 percent of them. You just have to have some conviction that either a given company, or a group of companies ... are likely to make more money 5, or 10, or 20 years from now, than they're earning now.

... And that is not a difficult decision to come to."
Tonight’s Class

• Rule #1 Investing – a long tradition of success!
• Two Requirements of a Rule #1 Investment
• The Four Ms
• Determining a Future Growth Rate
• Margin of Safety Calculator
• Payback Time
The Four Ms

- **Meaning** – Know what you’re buying – you have to be *capable* of understanding the industry and your business.

- **Moat** – The company has a durable competitive advantage! What is it? How good is it? Why?

- **Management** – The CEO has a vested interest in the business and proves it with Passion, Talent, Honesty, and is Shareholder Oriented.

- **Margin of Safety** – Buying the business cheap enough so that we can make mistakes and still not lose money.
Finding a Wonderful Company

WE USE THE FIRST THREE Ms

• **Step One:** Identify companies that have Meaning to you – you MUST start here! *(the 3-Circle Exercise)*

• **Step Two:** Identify whether a company has a Moat, what kind it is and how big is it?

• **Step Three:** Dig deep into the CEO and analyze whether the company Management is up to our Rule #1 standards.

Out of the thousands of stocks you can choose from, your job is to pick those very few companies that you would hold forever*. 

*Note: The asterisk (*) indicates a reference to a rule or guideline that is not explicitly stated in the text. Additional context or clarification might be needed for a complete understanding.**
Meaning = We Believe:

❖ Put your money where your values are.
❖ Companies that you invest in should have meaning to you, and the world.
❖ Do **Not** invest in a company that you don’t want to see succeed because of what they do.
❖ Don’t be a hypocrite* with your money.
Meaning

• Are you capable of learning (more) about the business?
  – We gain UNDERSTANDING through research.
• What do you know about the company and industry?
• Why does it have meaning to you?
• What is the company’s meaning to the world?
• Does the product or service the company produces conflict with your personal ethics?

Go through the three circle exercise on the Rule One website, and focus on just a few industries/businesses, for now.
Coca-Cola has an almost perfect Brand Moat. You have to love* a legal Business that:

1. Can raise prices when costs rise (inflation proof)
2. Can charge more because of the name on the can (don’t have to compete based on price)
3. Is nearly impossible to copy
   -- (they have secrets and can keep them)
4. The product and company name are synonymous
Whole Foods Market

• Which of the five Moats do they have?
• Identify the advantage(s) and analyze the strength(s) against the competition.
• Durability – Think out 15 or 20 years!

It is the advantages over the competition that allow for increasing profits for years to come.
Research starts with the 10-K

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FORM 10-K

WHOLE FOODS MARKET INC - WFM

Filed: November 22, 2013 (period: September 29, 2013)

Annual report with a comprehensive overview of the company
Read about the company in: Business

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Part IV
Item 15

Forward-Looking Statements
Business
Risk Factors
Unresolved Staff Comments
Properties
Legal Proceedings
Marine Safety Disclosures
Executive Officers of the Company

Market for Registrant’s Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities
Selected Financial Data
Management’s Discussion and Analysis of Financial Condition and Results of Operations
Quantitative and Qualitative Disclosures About Market Risk
Financial Statements and Supplementary Data
Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
Controls and Procedures
Other Information

Directors, Executive Officers and Corporate Governance
Executive Compensation
Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters
Certain Relationships and Related Transactions, and Director Independence
Principal Accountant Fees and Services

Exhibits and Financial Statement Schedules
Signatures
Whole Foods Market Inc. (NASD: WFM)

My Analysis: View Your Analysis

Business Description:
Whole Foods Market, Inc., is a retailer of natural and organic foods and a 'Certified Organic' grocer. Its products include seafood, grocery, meat and poultry, bakery, prepared foods and catering, coffee and tea.

Address: 550 Bowie Street
Austin, TX 78703

Telephone: +1 512 477-4455
Facsimile: +1 512 482-7000

Website: http://www.wholefoods.com
Email: ir.questions@wholefoods.com

Details

CEO:
Employees: 78,400


Issue Type: CS

Auditor: Ernst & Young LLP

Last Audit: UQ

Indices:
S&P 500 Food Retail (Sub Ind) (*SP500_30101030), Dow Jones U.S. Food Retailers & Wholesalers Index (*DJUSFD), S&P Composite 1500 Food Retail (Sub Ind) (*SP1500_30101030)

Industry Classifications
INVESTOR RELATIONS

The things that make Whole Foods Market special to our customers, make us special to our investors. The fact that we are a company with a mission is very important to many of our investors.

Throughout this section you will find the latest and archived financial news and press releases related to Whole Foods Market common stock.

Financial Press Releases
Browse our archived press releases by year

Conference Call Scripts
Browse our archived conference call scripts by year

Financial Results
Browse our historical financial data by year

ELECTRONIC ENROLLMENT
Whole Foods shareholders may elect to receive the Annual Report and Proxy Statement electronically over the Internet.

Sign Up

3rd Quarter Earnings Conference Call
Wednesday
July 30, 2014
4:00 p.m. (CT)
Understand the Competition
Management

• **Passion** – CEO wants to change the world!
• **Stockholder Oriented** - Knows who they work for and why.
• **Honesty** – willing to tell us the bad news along with the good.

Steve Jobs
CEO (deceased)
Apple

John Mackey
CEO
Whole Foods
Annual Reports for CEO Letter to Shareholders
Tonight’s Class

- Rule #1 Investing – a long tradition of success!
- Two Requirements of a Rule #1 Investment
- The Four Ms
- **Determining a Future Growth Rate (FGR)**
- Margin of Safety Calculator
- Payback Time
What is the True VALUE of our Business?

What are the steps we need to go through in order to determine the Fair Market Value of a Business or Company the we are doing our research on???

• Where do we start looking???

• What are we looking for???
  – FGR & …
  – EPS (TTM)
Start Here! Stock-at-a-Glance
### Whole Foods Market Inc. (NASDAQ: WFM)

**My Analysis:** View Your Analysis

###摩尔值: 复合增长

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<th>10 Years</th>
<th>7 Years</th>
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###Management: 平均增长率

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###摩尔值: 复合增长
Use Numbers View to Create a FGR

### Moat: Compound Growth Rate

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### Management: Average Growth Rates

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### Last 11-Year Growth Rate

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<td>-11.7%</td>
<td>-18.9%</td>
<td>80.2%</td>
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<td>7.6%</td>
<td>9.0%</td>
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<td>ROIC</td>
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<td>9.9%</td>
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<td>4.7%</td>
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<td>2.8%</td>
<td>1.4%</td>
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<td>Total Shares</td>
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<td>240.63 Mil.</td>
<td>271.82 Mil.</td>
<td>279.21 Mil.</td>
<td>278.48 Mil.</td>
<td>280.57 Mil.</td>
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<td>344.07 Mil.</td>
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<td>260.18 Mil.</td>
<td>278.66 Mil.</td>
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<td>279.77 Mil.</td>
<td>280.83 Mil.</td>
<td>332.49 Mil.</td>
<td>354.40 Mil.</td>
<td>364.80 Mil.</td>
<td>371.20 Mil.</td>
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Tonight’s Class

• Rule #1 Investing – a long tradition of success!
• The Four Ms
• Two Requirements of a Rule #1 Investment
• Determining a Future Growth Rate
• Margin of Safety Calculator
• Payback Time
Future Growth Rate - Summary

• Choosing a Future Growth Rate (FGR) is the key to a successful valuation. It is not as hard as it might appear on first glance and with a little repetition you will become very proficient.

• Use the company’s history of growth combined with your understanding of the company’s future growth prospects to create a FGR that is both conservative and rational. “Optimism is the enemy of good investing.”

• As you do more research on a company, you may change your mind about the Future Growth Rate, if so, you will need to recalculate the MOS.
PayBack Time
Payback Time Calculation

MARGIN OF SAFETY CALCULATOR

Future Valuation
Smoothed EPS: 1.53
Future Growth Rate: 13.60
Future EPS: 5.67
Future P/E: 27.60
Future Value: 153.73
MARR %: 15.00
MOS %: 50.00

Stock Price: $39.52
P/E Ratio: 40.70
Low and High PE Ratio: 8.60 - 52.10
PEG: 2.95
Historical Growth Rate in BVPS: 12.4%
Price to Book: 4.79
Analyst Consensus Growth Rate: 13.80%
Earnings Yield: 3.78%

VALUATION RESULTS

STICKER PRICE: $38.02
MARGIN OF SAFETY PRICE: $19.01
MARGIN OF SAFETY YIELD: 8.05%
PAYBACK TIME: 7 yrs.
PAYBACK TIME PRICE: $22.87 at 8 yrs.
RED ZONE PRICE: $45.63
GREEN ZONE PRICE: $15.01
Free Cash Flow (FCF) Calculation
### Calculate Free Cash Flow (FCF)

**Cash Flow for Whole Foods Market Inc. (WFM)**

<table>
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<td>687.72</td>
<td>585.29</td>
<td>574.85</td>
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<td>238.44</td>
<td>68.93</td>
<td>(13.27)</td>
<td>(130.00)</td>
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</table>
Calculate Free Cash Flow (FCF)

- Cash from Operating Activities: $1,009.00 Million
- Purchase of Property, Equipment: $198.00 Million

Total Free Cash: $811.00 Million

Divided by Total Outstanding Shares: 372.40 Million

Free Cash Flow Per Share: $2.17 (use for Smoothed EPS)
Recalculate MOS with FCF

MARGIN OF SAFETY CALCULATOR

Future Valuation

- Smoother EPS: 2.17
- EPS @ 9/6/2014 11:14 PM EST
- Future Growth Rate: 13.80
- Future EPS: 7.90
- Future P/E: 27.60
- Future Value: 218.04
- MARR %: 15.00
- MOS %: 50.00

Valuation Results

- Stock Price: $39.52
- P/E Ratio: 40.70
- Low and High PE Ratio: 8.60 - 52.10
- PEG: 2.95
- Historical Growth Rate in BVPS: 12.4%
- Price to Book: 4.79
- Analyst Consensus Growth Rate: 13.80%
- Earnings Yield: 3.78%

Green Zone Calculation:
- Margin of Safety (MOS) ▼
- 8 yrs. ▼

- STICKER PRICE: $53.93
- MARGIN OF SAFETY PRICE: $26.96
- MARGIN OF SAFETY YIELD: 8.05%
- PAYBACK TIME: 7 YRS.
- PAYBACK TIME PRICE: $64.71
- RED ZONE PRICE: $32.44 at 8 Yrs.
By next class, locate a company that has Meaning to you and looks promising. Evaluate the company based on the 4 Ms.

- Start a journal and write a few sentences on the Meaning of the company to you and meaning to the world.
  - What kind of Moat does it have and how good is it compared to the competition?
  - How good is Management in terms of honesty, talent, passion and shareholder orientation?
  - Etc.
Homework for Class #1

• Use the R. U. L. E. S. acronym
• Record the Margin Of Safety calculation numbers:
  – Current Stock Symbol, Name;
  – Current Price;
  – EPS (TTM);
  – # of outstanding shares;
  – Current PE Ratio
  – Current Market Capitalization
  – Future Growth Rate (FGR); (Yours vs the Analysts)
  – Future P/E (F P/E);
  – Sticker Price;
  – Margin of Safety Price (MOS) Price;
  – FCF/share;
  – Payback Time Price (PBT) Price;

If you want, you can email a one page summary of the above to:

earld@ruleoneinvesting.com