Michael Mitchell - Fundamental Opportunist
The Business Brew

Welcome to the first episode of The Business Brew. Our first guest is Michael Mitchell. Michael is a former partner at Locust Wood Capital Advisors. He describes himself as 80% Greenblatt and 20% Buffett. Alternatively, he can be described as fundamental and opportunistic. Labels aside, he's a great thinker and a cool guy.

[The Business Brew intro]

Bill: How's it going, everybody? Welcome to the inaugural episode of Brewster's Billions. We have IgnoreNarrative with us. Couple disclaimers that are important to get out of the way. IgnoreNarrative is also known as Mike Mitchell, I refer to him as his Twitter handle. First of all, neither of us are your financial advisor. This is not financial advice. It's not investment advice. We are two people that are interested in how people look at investments. Do not come here for financial anything. That is the best thing that I can tell you. Do your own work. This is for entertainment purposes only, a peek into one man's mind that I respect a lot. So, Mike, how you doing?

Michael Mitchell: I do well. Just to add to that, I'm not sure you want my financial advice anyway.

[laughter]

Mike: I'm not sure it would help you.

Bill: Yeah.

Mike: Oh, it depends on the day, I guess.

Bill: Something that is funny is I think a lot of people are going to say, like, “Oh, great. These two are talking. They're clearly going to talk QVC.” What I would tell people is if you don't think you want to own a business like QVC, that's a pretty good indication that maybe you don't want to follow us.

Mike: [chuckles] I guess, that's right. What better way to get through and weed out people who follow you? Throw out QVC is your best idea and see who runs away? My guess is a lot of people.

Bill: That's exactly right. So, I guess it's a natural place to start. Why did you run to it since it's the reason that we know each other? And one of my favorite parts of it is, I've gotten a friend out of you from the idea.

Mike: I'm already up a ton just in friendships and communication. I've been following you for a while. I'm just not sure we would have connected really, except for QVC. I would say too, just anybody who's listening, I should say, Bill is the one who had got me into this. So, if it doesn't work, we're all going after Bill.

Bill: [laughs] That's fantastic.

Mike: [crosstalk]

Bill: I don't want that.

Mike: [crosstalk] I'm just here to support Bill.

[laughter]

Bill: Fair enough.

Mike: I've got a long history with QVC, sort of long. I mean, it starts in 2012. Before that, I only knew it as a channel. I didn't really know it as a business. A good friend of mine, actually, when it was Lenta, pitched me on it. The idea for the pitch was not to own QVC. Really, it was to get involved before the Liberty Ventures spanned as a venture in hedge fund, and we love spins and splits, and any opportunity for dislocations and disruptions, we got excited. The problem I had with it was I didn't really like QVC as a business. It wasn't because I had some view. It was just like, it's old women buying stuff on TV, how can that be an exciting business? He said, no-- actually, he's a very sharp guy, I think he'd be embarrassed if I called him out, but he's a very sharp guy and said, "Actually, no, it's really a better business than you think it was, you should give it a chance."

So on his advice, and he's probably the best analyst I know-- On his advice, I went through the numbers, and the numbers at this time, and it really still were pretty phenomenal. I mean, returns on capital are good, margins are good, sales were consistently growing. You dig through and you're like, "Well, this screens like a nice business, but I really want to get underneath it." Every two years, they hold an Investor Day in Westchester, Pennsylvania. They were supposed to do it in 2020, but because of COVID, they did not. In 2012 in May, I went to their Investor Day, and it fell into place for me. The insight on that was not when I heard them present and I heard Mike George who I really like. Of course, now the Liberty people who I really like. The insight was when I walked through the studio. They don't do them anymore, but they used to do studio tours. Anybody, you could buy a ticket to go. But they did it for analysts as well. We were of course [audio cut] pay.

What I saw, I saw a line producer behind an unscripted television program, and they were selling-- always give the example, they were selling sandals. I saw a line producer with a dozen huge screens in front of them, one of which had the feed, one of which had the next product lineup that was coming up for the day, and maybe even for the week. Then, they had this little graph that would show anytime a purchase was made, I believe, online and then also when people called in. What the producer could do is they could see whatever the hosts were saying and how sales reacted based on what they said and what they showed, and then they could feed that information back to the hosts. For me, a guy had spent some time in retail before, which I'm sure you're going to want to talk about, like the light bulb went off of, "Oh, my God." They know exactly how well it's selling, what they can do to reposition their floor.

You think of a traditional retailer, a big box. You dump a lot of crap into it, you hope it moves. And by the way, you're getting this crap from China. So, you hope it moves, you get 90 days. If it doesn't move, you just mark it down and get it out, and then put a bunch more stuff in there. It's very merchandising dependent. When you look at QVC, they've got perfect information. For me, it was just like, “Oh, my God,” And by the way, you can change your floor, not to the day, but maybe to the week or the month. If you see shoes are selling or kitchen is selling, and electronics are not, it's airtime, you could swap out the airtime for electronics. For me, I saw that as like, “Oh, my God, these guys really know.” Then, which I'm sure you're going to want to talk about, their best customers. When you start really peeling back the onion of people who shop there, they're almost fanatics would be the way I would say it. They are religious about shopping at QVC, which says, in my mind, they're doing something right. These customers, I believe their spend is like $1300 a year, they buy something on average once a month, and their attrition rate is tiny, 1% or 2% a year. And that accounts for a huge chunk of their business, I think it's almost 70%.

When I looked through that, I thought, “Oh, my God, I discovered penicillin. This is a wonderful business and nobody understands it. Everybody hates it, and it's my kind of thing,” and I sort of pro forma that you could buy this thing for 10 times earnings, looking through for ventures and everything else. So, I got really excited, we bought a bunch, I followed it very closely. At one time, it was a huge position.

Rolling forward, I lived through mostly good times, one really bad time with them in the summer of 2016, where sales just went completely off the rails and it was just massive, eight or nine things went wrong at once. They started getting our business back on track.

Bill: 2012 happened, you do your underwriting. 2013, 2014, 2015, we're chugging along. 2016 comes and you own this in size. When stuff starts to go wrong, especially on an entity that is a retailer, how do you think through, “Hey, is this thing broken?” Where do you draw the line between thesis creep and figuring out reality? If you don't mind going through sort of your thought process on that, that'd be great.

Mike: It's a great question. It's one that I don't think that there's a uniform perfect answer. I think it depends on the situation every time. This conversation bleeds into my personal process, and I feel very strongly that I have to know and trust and like the people that I give my money to. When I think about a management team, I don't think of a guy running a retailer. I think of a guy who's got not only all of my invested capital, but then all of my future invested capital. Everything my capital turns into, unless they're giving it back to me, I'm counting on that person to do the right thing. My process is the number one thing I look for are people that I trust, and that I like, and that I think are rational and competent. If I don't check that box, it really doesn’t. Nothing else really matters. I mean, if that's not there-- there are some instances that I invest in some things like liquidations, which I love doing, you can't do that on any sort of scale, but the returns are phenomenal. It doesn't matter because I'm getting all my money back. As long as they're not crooks, then it's fine. For a business where I'm investing capital, and I'm expecting future earnings to be my returns, I need to make sure not only they can run their business, but they're going to invest my capital well.

So, I start with the people with Mike George with Liberty, when 2016 hit in that-- By the way, I learned that from Zale, that was a huge--

Bill: We're going to get into that. [laughs]

Mike: --takeaway from my experience with Zale, but people matter, they matter a lot. With Mike, I had extreme confidence. What Mike would tell me is, “Look, we don't know for sure, but we have eight things we can point to that all just went wrong.” That happens. Forgive my French with this, but my kids aren't around, so I can curse. Shit happens. It just does. That's part of life. I have yet to have an investment that even in hindsight, you look at it-- we could talk about Charter, like, “Oh, God, that's just amazing.” I promise you, there were some times it was not amazing. I mean, I sat through a meeting my old firm that all based on Charter’s 40% drawdown in 2018, and the meeting started out, the stock’s down 40%. You're wrong. Why do we own this? The whole meeting was about how Charter was down. I guess, for me, shit happens, and I'm okay with that. I have a lot of tolerance for difficulty, but to your point, it does get to, well, how do when the right time that--? How do when your thesis is wrong? That's really the question. You are underwriting a business, they did something that you didn't expect, how do you know you're wrong?

The first thing I do, is I go to management team and I say, “What happened? Am I wrong?” What Mike George would say-- and so I saw him in New York a few times, and I went to Westchester and I talked to Liberty about this. What Mike George would say is, “No, we think we've got it. We think we figured it out. It was just a lot of bad things. We had a haircare product that had some issues. Some women were saying their hair was falling out for goodness sake.” This was a big driver of their beauty business at the time. They say, well, we had to pull that, we were leaning into that. They just had a lot of issues all at once. I hear Mike and I say, “Okay.” At that moment, when he tells me, “It's fine,” and I like Mike, and we were to get it back on track, then it's sort of an, “Okay, well, now I have to watch this again, but I'm expecting it to be fine.” Then sure enough, it was a 2Q report in 2016, that was really brutal. Then, you saw this just sort of steady climb.

The thing about retail which really sucks is, it's so merchandising dependent. You can't just walk in and make money. I mean, it's very competitive and merchandise matters. You have to really focus on it, which is going to be one of the things we talk about with why I’m back involved. If you take your eye off the ball, it's going to hurt. It's not something where you can fum-- I think cable, you can fall asleep at this point, it'll be okay. In retail, you really have to watch it. It's a tough business. Even for Q, which has customers that love them and are going to [audio cut], you have to take care of them, you can't sleep.

I hear 2016, I hear what they're saying. The numbers are brutal, the stock is brutal. Basically, my decision just to give him the benefit of the doubt, and sure enough, it did start to improve, and it improved from 2016 through 2017 EBIT **[unintelligible [00:10:42]**, it wasn't as good as I was hoping it would be, but it's fine, as long as we're seeing improvement. Then, 2018, the numbers got better all up until the fourth quarter of 2018. That's when the hammer really fell. I think it was February of 2019, when we got that report, and it went from a 1% to 2% to 3% grower recovering off that 2016 level, and the business just took a dive. I stuck around for the first report in February. It was their first-quarter report where things continued to be rough. What I was hearing them say, which I really appreciated was, we don't really know what's going on. There's a lot of moving pieces, but we don't really know. At the moment, they say, “We don't really know, and there's a lot of moving pieces,” I sold everything. It wasn't an indictment or a challenge on Q. It was a, okay, now in my mind, it had changed and it was pretty clear that I was wrong and that I had expected this to recover, I had expected it to get back to where it was. It was pretty clear two quarters and that it just wasn't there. I didn't have confidence that-- if management couldn't tell me what the problems were and how they were going to fix it, then I couldn't have confidence to underwrite it.

And that actually is going to get into another topic, which I like talking about, which is the never sell mentality. If you would have asked me in 2012 when I underwrote it, I would have said, “Yeah, this is a never sell stock.” It's 10% free cash flow, buying back on its stocks, it's the good business never sell. Well, in 2019, it became a sell stock. For me, the price isn't as important in the sell decision as it is, is your thesis correct? Or is your thesis wrong? If your thesis is wrong, it almost doesn't even matter what the price is, you just have to sell.

Bill: That's interesting.

Mike: So, I sold it. I sold, I forgot about it until my friend Bill Brewster started publishing on Twitter about it. And he sucked me back in. [crosstalk]

Bill: It's a bad account to follow. [laughs]

Mike: Yeah, who would follow that guy?

Bill: I don't know.

Mike: Yeah, it's been interesting. I had not forgotten about it. I followed every quarter including-- they just had the second quarter when you started posting about it. I saw their capital action and I thought, “Oh, my God. I can't believe-- I should have known that they were having a good quarter.” Not that I would have done anything, but I should have expected business to be better now in a COVID time. I kicked myself because I know the business pretty well. I thought, “I should have been on top of this.” I was too focused on Globa and the LBRDK deal, and I was focused on Formula One. I had my eye off the ball on Q. Then, it really was your tweet. I saw you posted QVC is ownable again, and I thought, “You know what? He's exactly right. We should walk through that process again, see what's going on.”

When I did, I came to the conclusion that the story had changed. We can get into that if you want to, we can stay away from it, if people are probably tuning you out now. [crosstalk]

Bill: No, I like it. I like it, man.

Mike: I see the podcast numbers dropping.

Bill: No, that's fine. I think people like this. Do you kick yourself at all for not buying in March, given how close you are to the name?

Mike: No, because it's a use of capital and an opportunity cost conversation. So, yes, QVC would have been the better performer of everything I bought. But March was not an easy time to buy stocks. It was just not easy.

Bill: It was crazy.

Mike: It was crazy. In that moment-- that was the second one of those that I've lived through. I have a very specific plan when something like that happens. Even though it doesn't necessarily feel right, and everybody says the answer is to buy the crap. You don't buy quality by crap. I buy quality, and it's the reason why-- you talk about this a lot, and you're right to do it. I don't think it gets discussed enough. When people tell me like, “Oh, it's very easy.” Efficient allocation of capital is simple, you just go find a thing that you think is going to have the best return and you just buy it. In my mind, that's dead wrong. Absolutely incorrect.

The number one thing you do is you figure out what you can mentally deal with. What is going to keep you from not going insane is what you-- Once you figure that out, you just stick to it, because if it goes against me and I own crap, in my mind, I'm going to kill myself and I'm going to sell it. By the way, probably at the bottom. I've watched so many. My former boss was so bad at this. Just understanding this, his own psychology and was going to make him crazy. For me, if I own Charter and I buy it at 400 and it goes to 300, I don't care. Yes, would I rather own it at 300? Sure. If it's my best idea, I love it, I know it's not going away, buy it at 400 and wait, it'll go to 600. Yes, it's clearly better to buy it at three but I didn't know at the time if 400 was going to 350 or 250 or 100. What I did know as I liked the price at 400 and I knew I could stomach it if 400 went to 200. To me, that's the key for every investor, regardless of what your strategy is or what you own. It's having the right psychology around what you own, so that you don't get washed out when things get tough.

When stocks are going straight up, it's easy. It doesn't take any mental effort. It's when things really go against you. I mean, go against you hard that if you're not wrong about the business, and you're not wrong about your thesis, it's really difficult to get these cues from the market telling you that you're dead wrong, and not just emotionally cave. Most people do, I shouldn’t say most people do.

Bill: No, they do. You can just look at studies.

Mike: Yeah, if you make a mistake, it's like, I'm willing to be wrong about my thesis, but I don't want the market and the price action to force me out of it, if I'm not wrong. If I'm wrong, that's fine, I'm a big boy, I can lose money. It's not a problem. I often do things that are not popular, and not all of them are going to work. That's okay with me, I'm mentally prepared for that. What would kill me is, if I bought Charter, I didn't understand it. It went from 500 to 350, and I just blew out of it because I thought, it's levered, it's a terrible business, who would want cable? That would kill me. The psychology is more what I focus on in March, and what I'm going to be comfortable with, and that was buying stuff I knew cold, Formula One, Charter I knew cold, the Liberty story I knew cold. Really with Q now, I feel like I know those, at least as well as everybody else but I also understand myself well enough to know, if they go against me in the near term, it's not going to stress me out. I'm not going to make a bad-- [crosstalk]

Bill: That's how I was. I had followed QVC since 2018. I got real interested at the Liberty Day. I got interested because I was sitting there and Mike George comes up to present. All these guys just start looking at their Bloomberg phone, at their terminal, they're on their phone, they go, “Oh, fuck this. I don’t want to be here.”

Mike: [laughs] Start sleeping.

Bill: Man, there's one lady didn't turn her volume off. I just see this clicking of pictures every single slide, and I looked around at the room and none of the guys in the room were interested at all. I noticed three women were like very perked up. I just thought to myself, this is interesting that here's an entity that everybody is going to basically the Church of Malone, and they could care less about this entity.

Mike: Yeah, that’s right.

Bill: I thought that was an interesting psychology. Then the other thing that I thought was funny as I was going through these old transcripts is, Maffei was asked whether or not China-- or COVID was a problem in any of his businesses. I think it was Swinburne, who's a good analyst. I'm not trying to shit on him or anything like that.

Mike: Yeah, it was Morgan Stanley TMT, you're right about that.

Bill: He totally forgot Qurate. Greg was like, “Well, I mean, I do have one business. It's completely dependent on China.”

Mike: [crosstalk] Yeah, exactly. It's important, by the way, our products come from China, it really does matter.

Bill: Yeah, that's right.

Mike: I would say this, investing is not easy. It's not, and anybody who tells you it's easy, has no idea what they're doing, in my view. If they think it's easy, they don't understand the risks they're taking. That's my personal view. I don't expect things to be easy. I expect it to be difficult. I do, in general like the mentality, if nobody's interested, that's probably an interesting place to look. It. Unfortunately, you're going to sift through a lot of stuff you really would rather not own. When you find something that you wouldn't mind owning, I mean, you can get some gems. Buffett describes himself, I'm 80% Graham and 20% Fisher. If you ask me how to describe myself, and my style, my style is probably 80% Greenblatt and 20% Buffett. I very much prefer-- I like going to the-- what's the analogy, he is going to the swap meets. I like digging through and trying to find gems that I think people-- it's fun for me. I think people are missing. I enjoy that a lot. I get less excited when everybody's excited. It's just a natural-- I'm oddly optimistic about everything. When everybody agrees with me, I start to think we're all wrong. I don't know why that is. It's just a natural tendency of mine. It's like betting at the track is, yes, if you're taking the best odds, you're probably going to win. It doesn't matter if you win if the odds are messed up, you win and you win very little. The one time you lose, you lose everything.

In my mind, I prefer what you're saying, which is to be alone, and for nobody to like it. When people started liking Charter in 2019 and 2020, I started liking it less, unfortunately.

Bill: Yeah, man. No, I get-- [crosstalk]

Mike: I wish I would have liked it more, but it makes me nervous. I don't expect this to be easy and I think the real money is made when you're finding things that other people are--

Bill: It's not the market that we're currently in, but I agree with you. One of the things that fucking drives me nuts as SaaS is, the error that I have made consistently is underestimating a long-term mindset and inflections and operating leverage. I'm happy that I was smart enough to understand it when 2018 happened in Charter, and I could look past what was happening and what was on **[unintelligible [00:20:18]** because on the current valuation, I didn't really get it, but once I did some math on the far-out years, I really got it. With SaaS right now, the thing that it feels like is, one, I'm not competent to enter that game. Even if I was, the bases are so small, that I feel the error rates in the out years are so high. The question that I've been asking myself is, should I play more of those games in less concentrated bets? I mean, we can just go to a position sizing. For anyone that followed you on Twitter, at one point, you were 44% in Q. How do you think about sizing a position that big, how much of it was-- well, this is a transaction that I really like versus the business that I like.

Now that you're sitting holding Q, I back my position down to 10%. Again, this is not financial advice, this is entertainment purposes only. I can tell you at 10%, it's not the easiest business to hold. I know I want it in my portfolio. I know I want it big enough to make a difference, but I really wonder whether or not, seven is maybe more appropriate for my tolerance.

Mike: Well, I think that gets back to the psychology. I mean, it really is, and I think it's more about how much confidence you will have if the price goes against you. Everybody's confident when stocks go up, it's a Veblen good. Everybody when stocks are going up, and everybody thinks, “It's the greatest thing in the world.” When prices back off, everybody's like, “This is a total disaster. What a piece of crap.” It's really how you deal with the down. In my mind, if you say, well, I love the idea, but really the most hit I could take to my portfolio is, let's say, I don't want to have a drawdown in my entire portfolio from one position of more than-- my old boss used to say more than 100 basis points. Let's say that you said, now I'm willing to take 300 basis points of pain on a single position. My overall performance gets hit by 3% if I'm wrong about a position. Then I would say, well, for Q, could Q go to-- who knows where it is now, 650, I'm choosing to ignore it because it's going against-- [crosstalk]

Bill: Yeah, it's been a rough month. Come on, Q. Come on, Greg Maffei.

Mike: Well, it's been a [crosstalk] month. It's been rough two weeks, you're talking about month.

Bill: That’s fair.

Mike: I don’t want to see what happens for the next. It was hitting highs two weeks ago. [crosstalk]

Bill: Yeah, that's true. I guess it felt like a month.

Mike: Yeah. Luckily, it's a position, EBITDA is a little bit up on it, but that's not the way I look at it. The way I look at it is how much do you think it could go down? Let's be honest, could it go down 50%? Sure. Yeah. Could it go to $3? Definitely. Could it go to one times free cash flow? Yeah, absolutely.

Bill: [crosstalk] -would buy so many shares.

Mike: We can get into the thesis of why I think it's interesting here. Let's just forgetting what the thesis is for a second. Does the market have to agree with my thesis in the short term? Absolutely not. Any stock can go anywhere at any time. I think to myself is 50% down, is that reasonable? Well, it's very possible. Is it a reasonable? I don't think so. But is it possible? Sure. For me, you say, well, okay, what's my current positioning in it?" I stupidly sold the press to take a tax loss at 93 and I can't buy them back for another couple of weeks. I'm now down to just the common, and the common is probably a 20% position for me, I haven't update-- I'll update my numbers and post them on Twitter later today, since it's the end of the month, but it's probably gone-- given a 17% correction in the stock, I would guess it's gone from a 28% position to a 22%. You say well, okay. Wow, that's 600 basis points off of your performance." It's like, "Well, I'm actually willing to lose 1000 basis points of performance on this if I'm not. That doesn't bother me. I am perfectly willing to take that much of a mark to market loss. I'm even willing to take that much of an actual capital impairment, if I'm wrong on this security, and we could talk about why, and it's my personality.

For me, the process of investing, Twitter likes to devolve into this, is it growth? Is it value? What bucket do you fit into? I don't really know what any of that means, personally. For me, it's a very simple concept. I'm giving you a pile of money today. My expectation is that you're going to give me money back over time, and that money can come in a lot of different ways. It can come in a lump, that's actually my personal preference. That's why I like liquidations. The returns are not amazing, but you get all of your money back so quick. Then, you get these little options that maybe they hit, a few of them do and they're great, but you're not **[unintelligible [00:24:56]** in it. So, who cares? It doesn't matter.

Bill: Sorry, not to interrupt. Will you hold those? Do you basically just hold a basket of these basic-- like long-dated options that are perpetually-- well, perpetual until they go under or whatever, right? But, yeah--

Mike: I wait until the liquidation almost in every case, but there are some cases where I've been a little early to the liquidation party like CBA Florida was an example of that one. If I think it's going to liquidate-- actually, I was pretty certain CBA Florida probably would liquidate, and it was trading for 50 cents on the cash dollar, I just sort of go all in. I hope that it takes less than two years for that to work itself out. In this case, it took exactly two years for it to work itself out. The returns ended up good. With CBA Florida, my IRR on that one over two years has been 14%. I have not only all my money back, but I've realized that return now and then I have this little stub, I think could be worth another 20% on my basis that I'm now-- I have negative basis on.

Bill: It's a nice position to be in.

Mike: Yeah, I mean, those are great because-- and a lot of them actually will give you money back within months. You could get 80%, 90% of your bait back, and then you have this little stub that could be a double or a triple. I love those because you don't have to do a lot of work. It's very simple. You see their balance sheet and how much money they have. They've already announced of paying it back to you. You can figure out, I pay this, I'm getting this much back, and I think this stub is worth X, Y or Z. Your overall ROIs on CBA Florida is actually going to end up being pretty good, it's going to end up being a double, but-- not quite a double, maybe 80% return. It's going to take years for that to play out, but it's going to be a good return. Most of these aren't that high. Maybe you make 20%, maybe you make 30%, it takes a couple years. But because you get so much money back, your IRRs are phenomenal. If I could do nothing but those, I would do those all day long. It really takes no diligence. You're just, do I believe that these audited financials are correct? Do I believe that these guys are crooks? No, I believe that the audited financials are fine. I believe these guys are not crooks, then you just sort of plow in. I would make that 100% of my portfolio if I could find the right one.

When you put out money, and you're getting money back, for me, the decision is pretty simple. If it's a lot of money coming back very quickly, my diligence timeline is like--[crosstalk]

Bill: Yeah, compressed.

Mike: --it takes me a day. If on the other hand, what you're saying is, no, you got to put out a lot of money today, and you're going to get paid over the next 20 years. Charters was 600 bucks, they're going to be $30 in free cash flow this year. It's 20 times free cash flow. By the way, I'm not saying-- I don't know if that's expensive, cheap, it depends on who you ask. I wouldn't sit here and argue that it's mispriced. It's severely mispriced, it might be a little cheap or a little expensive, but probably not severely mispriced. If you tell me that I'm paying 20 times cash flow, so I'm going to get my cash flow back over 20 years, you said it's fine, because the cash flow is growing. When I have that long of a duration to get my bait back, for me, the diligence process becomes pretty-- [crosstalk]

Bill: Yeah, you better be right for a long time.

Mike: You got to be right. I really need the right people in every investment I make, but it's not just that I say, "Oh, these are the right guys. They're telling me it's fine." I actually have to understand the industry. Charter, for me, I wouldn't have gotten there, not in size, except I spent two hours with John Malone at a shareholder meeting. Believe it or not, shareholder meeting, and I think was 2015, there was four people in the room in--

Bill: That's insane.

Mike: --Denver, Englewood. You might be able to find the recording somewhere. John goes on a two-hour tear about the thesis of Charter, the cable industry, the merger with Time Warner convergence, the growth and connectivity, the opportunity for Charter. My mind just went poof. It blew my mind. I'm sitting there taking notes. Courtnee Chun is a friend and is the head of portfolios, the chief portfolio officer at Liberty. She leans over, she's like, “John's on fire today.” I was like, “Yeah, guy’s on fire.”

Bill: [laughs]

Mike: It was brilliant. You read Cable Cowboy, and Brian Roberts talks about how he sat next to John on a plane ride, I think, from Tokyo or something. He got an MBA, essentially on the flight, John gave it to him. That was my MBA in cable. After that ended, I called my **[unintelligible [00:29:09]**, it's like, “This needs to be our biggest position by a lot,” not by a little bit, but by a huge amount. If you're comfortable with 5%, this needs to be 10. This deal is going to work. I have to have that level of comfort with something if you're asking me to make a 15-year commitment to it. I have to believe myself. I can't trust somebody else. For me, it's the duration, which is another way of saying devaluation. Devaluation if it's high, doesn't mean I won't do it. It just means I really have to get it. Then you walk me through SaaS, we can even get into media if you want--[crosstalk]

Bill: Yeah.

Mike: --even more about media than about SaaS, but you say SaaS to me, I look at these companies, I don't know, 30 times revenue, 40 times revenue. I don't even bother trying to understand the business and you could say, well, that to me, is stupid, you should, because this is where the puck is headed. You have so much understanding of not just that business, but everybody else in that industry. Not just today, but you got to tell me who the new--

Bill: Yeah, how it evolves.

Mike: --interest will be over the next 10 years. Good luck, dude. I hope you're right. I know my pea brain will not get me there. I know it. So, what do I do? I go out on my garage and I make a shelving units. I don’t bother-- [crosstalk]

Bill: Which are very nice, by the way.

Mike: Oh, thank you. [laughs]

Bill: You did a great job, man. When you posted the picture, I was like, “Wow, he's got a skill,” you sort of short sold yourself on that.

Mike: [chuckles]

Bill: You have a workbench?

Mike: I have. I've set up a workbench for myself. I've got a miter saw, I’ve got a table saw. I'm gearing up on it. My family's been a beneficiary of it. I've really enjoyed, it's a lot of fun.

Bill: Dude, it's legit. It's a great retirement habit for you.

Mike: That's a good one. I like very manly retirement activities. I'm a big hunter, I love hunting. I'm getting into carpentry. Lawnmower repair or small engine repair is interesting.

Bill: That's dope.

Mike: I would rather do that than try to figure out the next-- forget 30 years, you got to figure out the next 50 years of that stuff. I don't know. By the way, it may work. I don't know. It's not that it's going to work or not going to work. So much of it is on the come, and I don't understand what on the come means. There's enough we can do. I can lose money in other things. I can lose money in QVC. So, yeah, there's enough we can do to--

Bill: We're going to get you on QVC to sell your furniture.

Mike: Yeah. [laughs] There you go.

Bill: It's going to have to be a little too high priced, but with the Easy Pay, we're going to be good.

Mike: So funny. Just an anecdote, one of my dad's best friends is a urologist. My dad splits time between Denver and Taos, New Mexico. One of his best friend's lives in Taos, he's a retired urologist. He's actually a carpenter as well, but he's pride and joy is his honeycomb. He makes honey and he'd be a great podcast guy. He'd walk you through all the ways you can keep black bears out of your bee nest or honeycombs. He's like, “Honey is crack cocaine to the black bear.”

Bill: It's crack cocaine to me.

Mike: [crosstalk] --this whole thing. Yeah. [chuckles]

Bill: It's good stuff.

Mike: He jokes. He says, “I'd be happy to sell you some of this honey.” It's $12,000 a bottle, which is just my cost, by the way--

[laughter]

Bill: That’s a funny joke. I like that.

Mike: That’s me with carpentry. I'm happy to do it for cost. I need to run an advertisement for Westchester-based former hedge fund partner/stock analyst making cabinets for $80,000 a cabinet.

[laughter]

Bill: I like it. Happy to do it, custom, early custom.

Mike: I was talking to Toby Carlisle the other day about it. One of the fun things about doing the podcast with him is, I've become good friends with him. The thing that just drives me nuts when I see people going at him and his returns on Twitter-- like what you said about, and I'm not trying to put words in his mouth. This is my perception of what he's saying, but what you said about the amount of duration view that you have to have and how cheapness protects you, I think if he ran a discretionary portfolio, I think his bet is a statistical bet right now, which is why I call him the Walter Schloss, and I'll have him on, if he wants to dispute anything that I'm saying. If he ran a discretionary portfolio, he would do what you're saying, like sift through some of this cheaper stuff and find-- Look, you can say what you need to about QVC to make yourself to have a hot take. But Maffei is a legit capital allocator. John Malone is a legit businessman. Barry Diller knew what he was doing when he got into this.

Now, does the future look like the past? No, I don't think anybody sitting here is going to say it does. Man, that security is cheap. To the point about the 10% that I hold, and it's emotionally difficult for me. Every time I think about it rationally, I get to the same place that you are, because I'm like, "Alright, if they cut this thing in half, and I am remotely close on this business, and remotely close on the guys that are running it, it's going to be really hard to lose debt to take a permanent impairment." You got to know what you own.

Mike: I think so. That's right. I mean, that gets to the psychology of just knowing what you own. We talked about the business, is it different? There are two legs of the thesis. I've bought into the first one, and I am excited to see if the next one is also right. The first leg of the thesis for me was that the story changed, and it's not-- what you'd say is, well, look, their numbers are good because of COVID. The story changing has nothing to do with their numbers being good for COVID. The story changing has everything to do with their capital allocation. What they've done historically was to repurchase shares, which is-- I would have been happy to promote. I would have told them that that was the right decision. They stopped doing that in 2019 because the numbers were coming in soft. What they want to do smartly was just build cash and see how it went. See if they could actually right the ship.

All of a sudden, 2Q comes, and they tell you a couple of things. They say, we've righted the ship, and then you ask them online, offline, they'll tell you that COVID has been a bump. It's more like a steroid injection for something, it boosted something we already saw. What do they decide to do? Well, sharing purchases have not worked. I mean, you look at where the stock is and you look at where they bought all their stock. Sharing purchases aren't working, so what did they do? They give you on a $10.50 cent stocks what I paid, they give me $4.50 cents back effectively in cash. One you could keep as-- the preferred was $3 that you'd keep that if you wanted to, you can sell that if you wanted to, and basically create another dividend, which is what I chose to do. If you want to yield, you can keep the yield, but they gave you 40-ish percent of your capital back, which was basically a year's worth of cash flow that they stranded on the balance sheet that they didn't pay.

What they told you is, "We'll keep doing this, we may decide to buy back stock, but our plan is to return capital back to you." I look at that I say, okay, net of the $4.50 cents that I was getting back on a $10.50 cent security, I'm basically in this thing for $6 on a trailing basis pro forma for the dividend, their free cash flow. I tabulated at $2.75 cents, some people say you can't include grant, whatever. The guy at the lowest possible end is at 2.50. You can make a scenario where it's more like $3, $3 and change, pro forma for the preferred. Either way, I'm paying three times for that. The bet I'm now making is that within three years, I'm going to get all of my money back. That's essentially about it. That is the new thesis, that I get all my money back. What happens to me in year four, doesn't really matter that much. At worst, if it doesn't go away in three years, it's going to be a very inefficient investment in the worst case, but I'm getting my money back. That is an outcome that I go big in. If I feel comfortable that I'm not putting my capital at risk, and that it's actually going to come back to me, I start pushing chips on the table. If I know the business, and I know the people that I can even go bigger, which is part of the reason why I went bigger, but the duration of that is tiny. I don't have to be right about the business. If the money is coming back to me in three years, doesn't really matter if I'm right on the business or not.

Bill: You got to be right for three years, right?

Mike: As long as that comes back to me-- Correct? Yeah. I have to be right for three years.

Bill: That's right.

Mike: The second leg of the thesis is that, in fact, the business is on the right track. These guys are correct, that they actually had fixed it. There's some reasons to believe that that's true. I certainly obviously want that to be true because I own a lot of stock, but I really like the people at-- [crosstalk]

Bill: Yeah, it'd be nice to see them turn it. This has been hard for them. I don't want to be like a cheerleader for them, but they've gone through a lot of shit with the HSN acquisition. It seems like they've righted the ship on Zulily, everybody dunking on them, and I don't think that they necessarily deserve that. It would be nice to see them-- Not that I need to sit here and be like, "Oh, poor Greg Maffei. He had a nice pay year last year." But--

Mike: Don't worry about Greg.

Bill: That's right, he's going to be okay.

Mike: Don't worry about Greg.

Bill: But it would be nice.

Mike: They'll still be able to afford toilet paper, don't worry about Greg.

Bill: Yeah, well, it's like rooting for a superstar to come back and win again.

Mike: Yes, from a Wall Street perspective, I agree with you. It'd be really nice if they could get some respect just for their own egos. For me, it goes a little bit deeper. I don't want the business to go away because I don't want Mike to have to fire half the people there. I lived through that with a retailer in it, it was awful. I mean--[crosstalk]

Bill: You want to talk about that?

Mike: -just call it out like it. We can segue. It's great, we're talking about retailing, we can segue but it's awful.

Bill: If you don't mind, giving a little bit of background and just talking about being on the board and having those discussions, and we'll see where it goes. Also, real quick, I don't mean to cut you off after I just said that. To anyone that's listening, I know I said it in the beginning, I mean it now, this is just two people talking about why they take investments. Do not go out and buy anything that we're talking about. This is not advice. I'm just trying to get the peek into somebody's mind that I have a lot of respect for. So, that's the purpose of this conversation. I never know who's listening, so I just want to make sure to say that. Don't buy stuff you see on 13Fs, don't see these fucking gurus and go out and buy stuff. Don't do any of that. If you want a peek into how people think, that's the purpose of what I'm trying to do here.

Mike: Yeah. And you're doing a great job, by the way.

Bill: No, trying. I got a good interviewee.

Mike: [laughs] We're making it easy for each other.

Bill: [chuckles]

Mike: The backstory, some of big context guy for me, context really matters. It's not just the data point. It's what goes into the data point underneath, that really does matter for the Zale story, which is what I really-- I don't tell it very often because it's aged, but there was some interest on Twitter, so I'm glad we're talking about it. The backstory is, I started working for an activist fund based in Greenwich called Breeden Capital. Richard Breeden was the chairman of the SEC in the 90s under Bush Senior, started a hedge fund in 2006. Actually, a good friend of mine was hired to be the head of research and trading for the fund. Richard’s a lawyer, administrator, politician, not an investor. He smartly hired a actually a guy who worked for Michael Price, which is who I interned for, is responsible for my entire career. He worked for Michael and then I went to work for Richard. He needed an analyst, and I was in flux. I was at a small, event-driven hedge fund called Kellogg Capital, which is the Peter Kellogg's family fund. Spear, Leeds, Kellogg guy, which some people listening might actually Spear, Leeds, Kellogg, it's a business school, Goldman acquired for $5 billion in the 90s, maybe the early 2000s.

Anyway, so I was there, I was a little bit in flux. Bob hired me at Breeden. Breeden’s mandate was 10 stocks, very concentrated, long-only. It was activism, and the activist angle was governance. He was considered a governance expert, he was going to use governance to improve returns. It's our job to go find securities that underperformed where we thought we can improve the governance, we thought we can improve decision making. The very first investment I ever made there was Applebee's.

Bill: That’s interesting.

Mike: Yeah, I focused on consumer at most of my career. I find consumer businesses are just easier for me to understand where the consumer is the ultimate customer. They're just easier for me. There was a roadmap happening in the mid-2000s. By the way, it's still playing out of asset-light, refranchising. There was an innovation that occurred in the 2000s of royalty based leverage. You could borrow money to a certain EBITDA multiple, which obviously you can still do. For restaurants, that's not a high number, because restaurants tend to have some volatility. But-

Bill: Yeah, then you can lev it up a lot.

Mike: -if you have a franchise royalty stream, you can-- Exactly. What I saw with Applebee's was their casual dining was taking a digger, it was weak. Applebee's was in that camp, they had relatively weak results, but if you peel back the onion, I think it was something like they were 60-40 company on versus franchised, or 70-30. They had a big franchised network. I looked at it, I was like, “Look, you're trading for seven times EBITDA. If you do a refranchising, you're going to be worth more literally overnight, your cash flow is going to improve. By the way, the operators are all doing a better job, their margins are higher, their same-store sales are higher.” It makes sense. You put an entrepreneur in charge of 10 restaurants, the guy's going to run them like it's his livelihood, as opposed to somebody in Kansas City who's just checking in on a weekly basis, or a monthly basis. That was our whole thesis when we bought it. We ran for the board. I don't know if they did-- [crosstalk]

Bill: Sorry, just real quick. Operationally, like-- it's one thing on a spreadsheet to sit back and be like, “Hey, just re franchise.” Living through that as the investor, and assessing the person's capability to delegate-- I guess, if they have that many restaurants, they're probably good at delegating, anyway. The franchise model, it's a different way of running a business. How do you assess whether or not that person is capable of releasing some of that control?

Mike: Man, when I looked at the management team of Applebee's, for me, it was pretty easy- [crosstalk]

Bill: Yeah, that make sense.

Mike: -to say, “Look, you're already doing this, just do it more.” I'm not asking you to recreate the wheel here. I'm asking you to-- Take the restaurants that people want to buy and put them up for sale. Interestingly enough, RBI, so Burger King did this in a way at the time, I thought it was insane, but it turns out they're brilliant. Not only were they not insane, I was dead wrong, what they were doing is brilliant. They're actually transferring these for little or no money with just a growth commitment and development committee. That's really the strategy because you don't get the multiple on the sales proceeds. All the brands were like, “Well, I'm going to sell them for five times EBITDA. I'm not going to sell them for four.” It's like, “No, you're missing it.” If you can grow revenue, you're going to get a multiple. If you get a multiple, nobody cares. RBI figured that out. At the time, I was like, “You're not even selling these, you need to delever.” “No, what we need to do is grow.” That was actually exactly right, which I've got some insights on that.

The Applebee's story was taking what you're already doing, and do it more. You have don't have to do it full, but just do it more. You naturally can scale down overhead at corporate, you don't need as many your divisional managers, you can change their scope, you can either lower them or you can make them more efficient, etc. As your SG&A doesn't need to be as high if you're managing a franchise organization, then if you're managing a large footprint of company-operated stores. The franchise model is a compelling model, financially but I also think operationally it works really well. That's why McDonald's does it. That's why Wendy's does it. There's an efficiency to having an entrepreneur and owner-operator in there, as opposed to just having a bunch of suits running it from a distance. That was the thesis, and instead of doing our refranchising plan, they put the business up for sale. We ended up running a proxy, it was hostile. I can't remember if we ended up filing proxy. We settled. We got two board seats, and, of course, I haven't been on either one of the Applebee's resales boards, but my boss was on both. I became an advisor to both boards. They were already running a sales process at the last minute, it was a really weird time. We were probably six months too late. I think I paid something like 18 bucks a share. We sold it for $25.50 or something. I was really hoping we could sell it for more, and the multiples were low in my view.

What happened, funny anecdote, this is just the last thing I'll give you before we launch into Zale. It was the meeting the Sunday at Akin Gump in New York City. It's always a Sunday meeting because it's a Monday announcement about the deal. We spent my whole Sunday at Akin Gump's offices. I wasn't at the board meeting, I was off the side, and my boss would come out for a break and talk about it and go back in. They approve the sale, and what got the sale over-- Management at the last minute comes in and says, "Don't sell it. We'll do the refranchising plan, and we'll cut the cost." I was like, "Yeah, because I think it's--" [crosstalk]

Bill: Yeah. We could have done this a long time ago, guys. [laughs]

Mike: Yeah, of course. You should have figured that out six months ago, if you had said this, the stock would have worked, we wouldn't have to be here, but here's where we are. What got the business sold, at least in my view, and I wasn't in the room. In my view, what got the business sold was it was Lehman Brothers. Lehman Brothers are in the room, they were **[unintelligible [00:45:52]** on securitized royalties at the time and leveraged against them. When was it? It's probably 2017--

Bill: Not 2017. They weren't around then. Yeah, big difference.

Mike: Oh, 2007. Sorry, 2007.

Bill: No worries. It's just Lehman Brothers in 2017, don't go together.

Mike: I'm retired and I'm old. Days all blend together.

Bill: That's right.

Mike: Now it's on a t-shirt, I don't have offices anymore. In 2007, two of those securitized royalty bankers were in the room and they said, "Look, guys, the market's open for you, you can do a deal at staple." The market's closing. It's closing every day. You remember the Jim Cramer, the funny video, where he's like, "The Fed doesn't understand what's going," on the CNBC. This was around that time. You've got staple financing, but the window's closing, if you want to do this, you need to do it now. And then, boom.

Bill: Wow.

Mike: [crosstalk] -hit the bid from IHOP at 2550. I was bummed, but then at the time, then we saw what happened later. I was like, "Geez, that was a great sale. Good job." I was bummed at the time. Okay, so that's the context. We got on the board--

Bill: Dude, real quick. Isn't it crazy how life works that way?

Mike: It really is. If you could only divine the future life would be so easy-- [crosstalk]

Bill: My boy that lives on the beach in LA. One of the smartest guys I know, always saw the world differently, and he self-made and retired at 34 or 35, but flipped to oil companies. Man, that last sale, I think it was like 2015 or 2016, he was sweating bullets because he bet everything he had twice. Well, he's a monster.

Mike: Wow. My kind of a guy.

Bill: I like him. I'm going to try to get him on, but he doesn't like podcasts. Anyway, he was just telling me, he's like, "Dude, the prices that people are bidding right now, it's crazy, and like a crash is coming. I know it, and he was worried he was going to get locked up in stock. It's wild. How one transaction like that at the right time get now can change everything, right?

Mike: It makes all the difference in the world. It really does. That's why I say, we were probably three to six months too late. At the time, we really caught it at the end. The market just as you know, evaporated and then everything melted down a year later. Yeah, luckily for us, we got it done. If I would have been maybe three or six months earlier-- [crosstalk]

Bill: Yeah, that's right. Whatever. Who cares? [laughs]

Mike: You can see this in the proxy. When you read through proxies, deal proxies, especially you go to background this transactions. If you pull up the old Applebee's one, you can see it. The party A, party B, party C, we're all bidding, they all dropped out. A significant number of them were private equity firms-- [crosstalk]

Bill: Financing is drying out.

Mike: They all dropped out. Why? Well, if you can't get a securitized finance exactly right, the returns are based on financing-- I mean, in part. If they can't get the financing, it becomes a lot less attractive.

And IHOP, which was this **[unintelligible [00:48:41]** was the one that ended up closing it because while they wanted-- [crosstalk] securitized financing, they were thinking of it-- [crosstalk]

Bill: That's interesting.

Mike: --strategic purchase. Exactly. We got it done. Now we've had a success, we've transacted a business, we've gone on a board, we got it sold, this is great. So, then my next investment idea was Zale Corp. When I looked at sale, and this was early in 2007, when we were sort of--

Bill: Okay. So, you're going through the process on Applebee's. Okay, are you talking to Lehman about the market’s closing up at this point, or not quite yet?

Mike: No. By the way, it seems so obvious that you should have just had this conversation because it might have changed your view of the market, but you have to understand, in 2007, no one thought that 2008 was possible. It was not in my brain space. In 2019, no one thought COVID-19 was possible. Now, it's all we talked about. Same thing for September 11. Nobody thought a terrorist attack on United States was possible. Then now, everybody knows it's definitely possible. World definitely changed. There were so many things I was not focused on in 2007, so many risks that I was not underwriting in 2007 that I underwrite on a daily basis, just in my back processes now as a result **[unintelligible [00:49:58]** way. I find Zale-- which by the way, now one of those processes-- [crosstalk]

Bill: [laughs]

Mike: - jewelry company in recession. Number one. That is the number one thing I want-- [crosstalk]

Bill: That actually is investment advice. [laughs]

Mike: [crosstalk] -recession. Don't do it. Do not go to jewelry retailer. Don't do it. I find Zale, and what I see is, it's really a two-horse race nationally. It's not a duopoly necessarily. It's not the right way to think about it because there's a lot of fragmentation in the industry. There's two big players. There's Zale and there's Sterling, which is big. As I see these two players, both of them, Sterling was public in the UK, but you can get their financials. You see Zale had been a pretty material outperformer early in its life and it had been a pretty material underperformer more recently. Not bad, sales were still growing and it was an industry actually forever, that was a good industry. People got married regardless of economic cycles. Even though I don't love generally products that are sold, not bought.

You think of jewelry as a product that a guy shows up to a jewelry store, he has no idea what he wants. And so it's incumbent on the salesperson to tell him what he wants. The difference between this and a timeshare, for example, which is another product that's sold, and I thought this is actually necessary. You actually need to show up if you're going to propose--

Bill: Yeah. I think so, for most people.

Mike: [crosstalk]-necessary for most guys. If you find a woman that does not require a ring or a even want a ring--[crosstalk]

Bill: Or a man, in 2020, your partner general.

Mike: Or men, yeah, absolutely. They don't require a ring, whoever they be, good for you, but most people do. My thought was, it's an industry that had grown pretty-- You could look at jewelry sales in general, they were pretty good. Weddings are the key to their business, and wedding business has historically been-- not resilient, but not been quite so bad. I look at the industry, I look at us, Zale, I look us underperforming. Oh, by the way, Sterling actually made a bid. Now, it wasn't a formal bid, but it was in the papers, like the Journal reported that Sterling had made a bid, stock, I think was high teens. Sterling had made a bid in the mid-20s. I'm thinking, oh, okay, so I've got a business that's underperforming, by the way, there was an interesting part of their business that I became really attracted to, but so that I see its underperforming its peer, its peers bidding for them, they spend the bid, gives me a backstop.

Then, I look at the underlying business, there's two businesses inside of Zale. There's the jewelry company, which is the obvious one, and there's an insurance company. Now, I don't love insurance. I've owned insurance, I understand it some of it, I don't understand all of it. In general, I don't like it. This insurance business, though, is gold. I guess pun intended, what they insure is the ring, so they insure a 14-karat gold ring with a diamond on it. Up until the early 2000s, they had three tiers of products. They had a three-year warranty, a five-year warranty, a seven-year warranty, and people would almost, almost always choose the seven-year. You look at Sterling, Sterling sold a lifetime warranty. You'd be like, "Well, okay, so what's the difference between a three-year, five-year, seven-year, lifetime?" The answer is nothing. 14-karat gold ring doesn't break. Oh, by the way, you have to-- as part of your contract on this warranty as insurance product, you have to come into the store every year and get it cleaned for free and checked. If you don't bring the diamond in, it voids the warranty. So, you pay upfront for this warranty.

Bill: Dude, how many people do that?

Mike: It's not a huge cost, if you pay $1500 for a ring?

Bill: Really?

Mike: Actually, everybody. Think of it, it's a guy who comes in and spending 1500 bucks on a ring or $2,000 on a ring. The salesperson says, "For a $100, would you like a lifetime warranty?" When I proposed to my wife, it was the CEO of Zale, who sourced my ring from a guy called Theo Killion, who you should have on at some point, and he's amazing. He does board seats and consulting. He got me my way [crosstalk] ring.

Bill: Yeah.

Mike: I had this ring in my pocket.

Bill: No doubt.

Mike: [crosstalk] -happened, I'm like freaked out.

Bill: Yeah, burns a hole in your pocket.

Mike: [crosstalk] -I don't want this thing, get it away from me. Yeah, "Please get it away from me, I do not want this." Guys have that emotion, a lot of them do. One of the things they think is, "Yeah, if I'm already spending two grand, should I spend an extra $100 to make sure that if something happens, I can bring it back and get--" [crosstalk]

Bill: My question was how many people follow the terms of the insurance and actually come in and get it cleaned?

Mike: Oh.

Bill: Yeah. So, your breakage is huge?

Mike: No, none of them do, but it doesn't matter, because the thing is that-- Yeah, the breakage is big, but nobody ever came back anyway. If they come back as a customer-

Bill: Yeah, it's just a cash cow.

Mike: -service, you'd help them. It's a cash cow.

Bill: Yeah. That's smart.

Mike: I liked that business, but there was a nuance, because Zale offered a three, five, seven-year product, Sterling offered a lifetime. It was obviously cheaper if you do a lower duration. Zale figured out, and I don't know who it was in the corporate. It's probably Rodney Carter was the CFO at the time, it's probably him or somebody, in his group, "So, why don't we just do lifetime?" What happens when you switch to lifetime? Well, your price goes up. It was a 20% or 30% price increase going to lifetime, just to match where K was already. The auditor said, for gap accounting purposes because you're changing the duration of the warranty, even though nothing changes on claims, whatever, you can no longer recognize--

Bill: Maybe your expected loss would be higher, wouldn't it?

Mike: Well, that's what they said. They said, "Until we know what your expected losses, you need five years for this to season before we're going to let you recognize full revenue." As you just said, it's not just revenue, it's pure profit. What they did was, they said, "Okay, I used to be recognizing this on a 12-month or a 16-month basis, or an 18-month basis-- [crosstalk]

Bill: Yeah, now it's like [crosstalk] or whatever.

Mike: Your entire product is going to be recognized over 16 months, over five years. Now, when they're reporting same-store sales, they're taking a ding for all of the warranty sales, even though the warranty sales are higher. Not only that, it's pure profit. You basically had a business that **[unintelligible [00:56:01]** numbers, it really was on a cash flow basis, earning $2, but their reporting were like $1.50. I mean, it's very material, and their same store-sales were 4%, but they were reporting 2%. Yeah.

Bill: “Come, sit down,” and then people puke it. They're like, “Yeah, huh.”

Mike: Yeah, they would explain it, but the headlines were awful. [crosstalk]

Bill: I could see myself in something like this.

Mike: Yeah, exactly. Right. I'm not a total idiot.

Bill: No, [chuckles] I don’t think so, unless you talking to one. You may be.

Mike: [crosstalk] So, that's in there. I see this idea, okay, this business is more valuable, it's getting more valuable every day, but it looks less valuable. It's right down the middle for me. Then I see it's underperforming, margins are low. My thought was, “Oh, and by the way, their competitor was bidding for this big.” Okay. Let's go on the board, which is in general, I would say for the average investor, huge mistake, never go on a board. If you can avoid it, don't-- [crosstalk]

Bill: Why is it just-- you'll get to it, but that's interesting.

Mike: Illiquidity. That dovetails in a lot of that what I think the current market narrative is and why I think it's dead wrong, but are part of the current market narrative. That's what we did. So, let's go on the board, they invited us on because of the Applebee's experience. They had just hired a new CEO, a dear human being called Neal Goldberg, who brought in Theo Killion who became the interim replacement. And then ultimately, Theo Killion was the one who dug us out of our hole. Brought in a new CEO, invited us on the board. This guy, Neal Goldberg was great, came from children's place. He said, “Mike, it's real simple. Part of the problem, the reason why we're underperforming is, I think our stores are cluttered. Too much inventory. I want to pull inventory out. Once I clean them up, then I want to take some of that capital and reinvest it into the inventory that I want that I think will actually move.”

I'm not a merchandising guy, so I hear that, I'm like, “Brilliant. Okay, great. Let's do it.” By the way, what you're doing is you're pulling capital out of the business on a net basis. In my little pea brain-- [crosstalk]

Bill: Yeah, cash flow is going to come back.

Mike: -27, I'm like, “This is amazing. We're going to permanently pull capital out of the business.” What do I think when he said, “I want to get the inventory out.” What he means is, “I'm going to mark it down and move it right," and that [audio cut] mark it down. It moves, it hurts your margins, but it generates a lot of cash if you don't replace it. I'm all for it. I'm voting, yes, yes, yes, yes, yes. What do I do with it? I put on Twitter, I got greedy. Well, here's where I got greedy. When he pulled that capital out of inventory, rather than saying, "Let's just wait. Let's just pay down the revolver. Let's just see how it goes. We may need that money later." I said, "No, no. Guys, this is a misunderstood story. We're going to sell it. Plowed into share repurchase, keep your leverage up, plowed into share repurchase." I mean, this was the late summer of 2007. I think we got on the board in the fall, actually. So, is the end of 2007, started 2008. Well, before the Lehman crash. Well, before-- the market, there was turmoil, but it was we weren't near-crash territory yet, that came way later anyway. I'm like, buy stock back, by 20. What happened? They did that at my brilliance, and then we had an Investor Day in Dallas. I get the stock ripped to 28, as everybody saw the comps are growing and believed in the merchandising strategy. We were buying back stock and it's amazing. Then what happens? Boom, 2008, the crash. Our comps went from plus two to down 20.

Now, here's a problem. In the jewelry business, another thing I learned and this was true in 2007, 2008. It may not be true today, I really don't know. I'd sworn off jewelry-- [crosstalk] I'm off.

Bill: You've PTSD, you never gotten back.

Mike: I'm not doing it. Don't ask.

Bill: [chuckles] That's fair.

Mike: What I learned about the jewelry business is, in fact, when you walk into a Kay versus when you walk into a Zale, Kay has shit everywhere. Every box is full of shit. Bright, sparkly, boom, boom, boom. Neal would say, "That looks terrible. Why don't we clean-- why don't we have great product and very clean." To me, that resonates, but what it doesn't resonate to? The 25-year-old guy, who''s going into buy a ring. He wants to see every option. When he walks into your store, and there's only four options versus when he goes to Kay, even if he ends up buying what you had for sale, he wants to see all the options because he doesn't know and he wants to be walked through every one of those options. Then, arrive at the decision to buy. At Kay, figured that out. If you stack it in the store, you may not sell it, but it'll lead to another sale. Overall, your inventory will move quite a bit faster-

Bill: That makes sense.

Mike: -and so they were eating our lunch this whole time. Their comps never went down to the degree. We were down 20, they might have been down six or seven. In a business where you only turn your inventory one time, it fucking matters, man. It was brutal. They didn't have leverage, we had leverage because of my brilliance of buying stock back at $20 and $22, and $23 and $24 share.

Bill: Then you don't have revolver capability to go out and invest in inventory and shit, and then it gets tired.

Mike: No. What banks do when it starts to rain? They ask for their umbrella bank. What happens? Well, I spent a lot of time in Dallas, obviously. We're creating plans of like Armageddon plans. What do we do if this never gets better? How do we make sure we don't become insolvent? I spent days and days, I learned, it's a very important lesson in there. I learned in those days, they were pretty dark. I mean, the stock I think got to 30 cents or something. I mean, from 20 to 30, just quarter of a billion dollars-- [crosstalk]

Bill: Jesus, what a 12 months for you. You go from looking-

Mike: I mean, it's crazy, just--

Bill: -like a hero on the buyback to looking like zero on the share price. That sucks.

Mike: The running joke in my family is that, if I do something that looks brilliant, just wait.

[laughter]

Mike: Just wait.

Bill: I try to avoid the brilliance part. So, I know a lot of people-- [crosstalk]

Mike: Yeah, but it also means if I do something really dumb, like the next one is probably going to be good. Follow me into the next one.

Bill: Yeah, that's interesting.

Mike: So, wait until--[crosstalk] I'm like practically **[unintelligible [01:01:56]**. Anyway, so--

Bill: [laughs]

Mike: I shouldn't have said that.

Bill: He's been all right. He got back in his lane. He's good in consumer stuff.

Mike: No, yeah, he did. I will tell you, he's one of the smartest people I've ever met. I mean, the guy is fucking brilliant. He is, frankly, might be too smart, but he is-- the guy is sharp, and he understands things I will never get. [crosstalk]

Bill: The only criticism that I've heard of him that I think might hand, like carry some water is, as an allocator-- He may not be as good of an allocator as he is an analyst, but most people that know of him or know him, put him among some of the best analysts I've ever liked seen.

Mike: Yeah, that's right.

Bill: I don't know that he can come at him for that.

Mike: No, in fact-- it's not like I know him.

Bill: Yeah, no, I know, you're just a guy commenting on a career.

Mike: [crosstalk] -it's not like he is my friend. In my experience, and I would put his analytical ability up against anyone's. I mean, if you were just talking a specific stock and a business and going through it line by line and understanding it, he'll blow anybody away. I'd put him up-- [crosstalk]

Bill: Yeah, especially consumer, and I've heard real estate too, he's really good. I know Howard Hughes isn't working too well, but I mean, that came out of GGP and that was a massive homerun.

Mike: Yeah, in my estimation that was probably the second-best investment of my lifetime generation. It could have been the second-best investment of all.

Bill: Number one, your boy, Maffei with Liberty Sirius or with Sirius XM?

Mike: That was John and Greg. It's the number one, and I don't think anything will ever touch it. I don't know. Every record-- [crosstalk]

Bill: Yeah. Francisco says that, too.

Mike: You want to blow your mind. That deal was brought to DirecTV. DirecTV was going to do the deal. CEO couldn't get it over the line. So, he gave it to Greg and John-

Bill: Holy shit.

Mike: -and Greg and John are like-- Yeah, no brainer. Yeah, that's it. Imagine, Sirius is worth multiples of what DirecTV is worth today. I mean, that story is very-- [crosstalk]

Bill: Why can't they get it over the line, do you know?

Mike: The board didn't want to do it. The board did not want to do it. They didn't want to do it. The board said no. CEO said, "We should do this deal." Board said, "No." By the way, that's exactly what happened with Blockbuster and Netflix. I don't know if this, but Netflix tried to get to get bought by Blockbuster, Blockbuster passed. I haven't checked valuations recently, but I'm pretty sure that was a bad pass. [crosstalk]

Bill: Yeah, that was a bad pass. Icahn had a big part in that, in Blockbuster's [crosstalk] there too.

Mike: Yeah, that's fair. But Sirius XM in my opinion is the best, but I've been had the second best. I mean, GGP was-- I mean, it was massive class. I mean, that will not be repeated. That was very similar to what John did originally with Liberty in the early 1990s. Then it was just epic. You can't take away from his brilliance, you can take issue with some of the things he says or does but the guy is brilliant, and by the way, I'm never going to do any level of success in my life like that kind of [crosstalk] financial.

Bill: Who, Ackman?

Mike: Yeah.

Bill: The dude is public, we're allowed to say stuff about him. I got mad respect for Ackman. I don't talk shit about him. I'm an Ackman, actually. I don't even mind that he went on CNBC and cried, that's how much I like him. [laughs]

Mike: I never missed the CNBC back then. Especially if you get Icahn on with him, it's like the best.

Bill: I did think he got misframed on that. People came at him for-- I don't think he was talking his book, but I'll argue that with other people in a different one.

Mike: N, I don't either. I agreed with him.

Bill: Yeah.

Mike: I actually think he's at the bottom personally, but we'll see. We'll see, maybe we'll find out if they'll get retested.

Bill: That would be wild.

Mike: The Zale thing, to wrap that up, so I'm in there, numbers are tanking, Neal is let go. It is a really shitty deal, but the board, let him go. They put Theo in there. I mean, we interviewed so many people to come in, and the economics people wanted, it was the worst. When a business starts that kind of decline, what happens? Everybody panics. The worst thing that happens, and you can't see this from the outside as an analyst, but when you get inside, you can see it, it's pretty fucking clear. The best people leave.

Bill: Yeah.

Mike: Smartest people who are there, the people who you really don't want to leave, they are gone. Why? Because they're great. They've got 50 other options waiting for them. Who stays? The worst people. The people that have no other options, the people who you really don't want to stay who you would have liked to fire, but now you have to have somebody answering the phone. So, you've got the worst people around. This is a generalization, it was not everybody. There are some really good people that stayed, but on average, the smart people go when things get really, really tough, that's what happened at Zale when things were getting tough, the smart people left. They left before things got really tough, and that crash. Once the crash happened, nobody left because everybody wanted a job, but then when it recovers, the smart people leave. You start thinking like, “Oh my God, how am I going to replicate this? How am I going to get this business back on track? I don't have the right people. I don't have the right inventory." It was so bad. It's an epic fire drill of nothing was working.

Luckily, for me, and this is why people matter. Theo, his background, he was a human relations, human resources guy for Tommy Hilfiger, some really good brands, work in private equity. I never would have thought an HR guy could be the CEO of a company, although it does make sense especially if it's a people-based organization, which Zale is a jewelry store, but jewelry requires selling, it requires a lot of people. He became CEO, and that guy single-handedly, with the CFO and a COO, his head merchandiser, they just systematically turned that business around. They got the inventory right. They needed money. We needed to repay some debt and we needed money to get the--

Bill: To what, you raise equity? That fucking sucks, man. Then you get diluted, your share buyback gets reversed at the lows.

Mike: This is where my brilliance killed us. I mean, this is where my brilliance just killed the whole thing. If we would have had that money-- This isn't totally fair, because you never know-- [crosstalk]

Bill: Yeah, Monday morning quarterbacking yourself. I do like how you beat yourself up, though. It's a good lesson.

Mike: It's the lesson learned., What we should have done, we should have given up, I should have given up some upside for some conservatism in a business that-- frankly, when things go bad, they go really bad. Conservatism matters. By the way, you learn like your debt duration matters. When Charter puts up their 12-year average duration, it's like, that's terrific. That's an asset in my view, that's not a liability. That's an asset.

Bill: I know, man. Dude, the way that they manage, leverage and liquidity, it's like watching a symphony work. It's incredible.

Mike: Yeah. They do an amazing job. Hats off to them. I didn't understand or appreciate the importance of that until it was staring me in the face, then you learn at that moment, that's all that matters. Your liquidity is all that matters when it starts to matter. We had some very tough conversations. Point is, Theo pulls it out. Frankly, I don't even know how he does it, but he pulls it out with his team. They get comps stabilized. Golden Gate Capital actually is the one who gave us $150 million term loan at 15% plus--

Bill: Woo. Oh.

Mike: --warrants, that I think struck at like two bucks or something that, took 40% of the equity

Bill: Oh, what a monster deal for them.

Mike: If you find somebody from Golden Gate, by the way,-

Bill: That's your third-best deal.

Mike: -that might be their best deal of all time.

Bill: [laughs]

Mike: That might be the best deal of all time. Took it from me, thank you very much.

Bill: Yeah, that sucks.

Mike: Yeah. They gave us the money and then they orchestrated. Now, obviously, my boss **[unintelligible [01:09:06]** hates me right because he's like, "Thought you were a genius, turns out you're an idiot." I was like, "I'm not sure either one is true."

Bill: That's resulting.

Mike: Absolutely, but it was fine, and I stay employed there, and I get some other investments in the book. Burger King being one of them actually before-- [crosstalk]

Bill: How do you know Francisco?

Mike: No.

Bill: You have overlap like crazy.

Mike: That's what I told him. He actually found me probably through Formula One or something, or maybe I don't remember. I think he found me, but we were talking through DM, I was like, "Francisco, we're the same person." We were literally the same exact human being. [crosstalk]

Bill: Dude, he's a good analyst. I like him.

Mike: [crosstalk] He's a very sharp guy. Anyway, they get deal on the track, and my firm got out all of their money back, plus 10%, but it took them eight years, seven years. [crosstalk]

Bill: Yeah, [crosstalk] brain damage, it was garbage.

Mike: It's unbelievably inefficient. If I wouldn't have been so aggressive or push them to be aggressive, I think they might have gotten the 30 plus. I mean, that dilution I think is what ended up with the stock being in the 20s and not in the 30s. I think the original underwriting wasn't terrible, I got punched in the face on the recession, but then I just got aggressive and that was a mistake. A huge mistake.

Bill: A reason that I think we connect as people and why I've really enjoyed getting to know you is, when I watch you tell that story, I can actually see the pain on your face.

Mike: Yeah, but it still hurts.

Bill: I can tell that it's for the right reasons, too. You don't like that people lost their job. It's a human feeling, and that's what I appreciate about talking to you.

Mike: That’s right. Forget QVC for a second. Let's say I lose 10% of my net worth, like, who gives a fuck? Right. I'm rich. I'm fine. Don't worry about me. Don't worry about Greg. What I worry about is the people who are working at St. Petersburg or HSN. I worry about the people in Westchester-- [crosstalk]

Bill: Yeah, they [crosstalk] shit like that.

Mike: That’s their job.

Bill: Yeah, no doubt.

Mike: I want them to-- there's a good insight I learned in 2013, it's brought a lot together. I learned don't invest **[unintelligible [01:10:53]**, I learned it first from Zale, that when you go into a recession, a real recession, when you go into a recession, that the Fed isn't just pumping massive amounts of capital into everybody's lap every day. When you go into a real recession, an average business becomes toxic. That's what happens. A great business becomes average.

Bill: Huh. Yeah, that makes sense.

Mike: If you own great businesses, all of a sudden, they're average business. You own some average businesses, all of a sudden, they're incredibly toxic, and you learn. In my mind, when I say don't go on the board, but I mean, is if you're going to buy average businesses, you want liquidity because if it goes bad, you don't want toxic, stay away from toxic, at least.

Bill: No, I agree.

Mike: It's not an investment advice-- [crosstalk]

Bill: No, I agree.

Mike: You don’t want toxic. Life is too short. [crosstalk]

Bill: What I would say, the other side of that man is like, if you're going to get concentrated in average businesses, I would think a lot about that because Graham and Schloss and all those guys had 30, 35 bets at all times. 10 on average businesses is playing a freakin dangerous game, if you ask me.

Mike: In my mind, I can't own an average business. Unless I know the guys and I like the guys. Again, your duration is incredibly short because I don't know. I can't define the future. I have no idea. That’s really, for any business. Some businesses, they feel like, “Yeah, do I think QVC is going to be around three years from now?” Yeah, I'm making that bet pretty big, and I have a lot of confidence in that. But five years? I don't know what it will look like. By the way, that's not to say it'll be terrible. It could be amazing. That's the other leg of the thesis is, look, if what they're telling you, and I trust them, and I believe they know what they're talking about. If what they're telling you is that the business was on track, that there was just so much disruption from the integration of age in their business, and they took their eye off the merchandising ball, now it's back on. Now they got a shot in the arm from COVID and they can get back on track, that's not a crazy thesis. It's not crazy to think that that actually could be true. I do think they would know. So, if you think that's true, I mean, then this is going to be one of the better investments I make in my life. I don't know if that's the case, but it's out there. It's possible.

Bill: Well, that's what I think we connected over. It's like, okay, well, both of us saw duration, we both saw a capital return, and we can both fathom and upside, but neither of us is underwriting it or pitching it. I think it could exist.

Mike: Yeah. Well, it does. I'm going to pronounce his name wrong. Mauboussin Michael had-- [crosstalk]

Bill: Mauboussin, I think, sir. Come on now. It's okay, I might have messed up too.

Mike: Mauboussin, sorry. I know. Again, pea brain. He put out a research piece that was just sent to me by Shai **[unintelligible [01:13:23]** from 1999 talked about option value, and putting option value as a component of business value. I think it's a very useful idea. It's hard, but I think it's useful. The way in my mind with QVC, the way I think about it, and really with these little liquidations we were talking about, really what they are, is there an average return of capital with free options, and the options are all worth something. How much? [crosstalk]

Bill: Yeah. They have no implied volatility in them.

Mike: Exactly.

Bill: If you think about it from an option perspective. We're fucking SaaS. It's like all options and they're all out of the money, and everybody thinks they don't exist. And it's like, guys, I understand it's--

Mike: They have huge valuations on out of the money options. I get very uncomfortable with that. [crosstalk]

Bill: I prefer selling those than buying them.

Mike: That's correct-- Same. With Q, my view of it is like, I'm getting a business and a return of capital, and I'm getting a free option. In fact, what they're saying is true, and that's free. So, it doesn't really matter what it's worth, but I happen to think that could end up being worth a lot. We'll see. I don't think we'll know the answer to that until this time next year. I think we'll have a better indication in 12 months. I don't think we'll really know the answer probably for a couple years. It's not a zero percent probability. I don't know what the probability is, maybe 20%, 50%? It's not zero.

Bill: Yeah. All right, so you're talking about duration and cash coming back, so how do you get into Formula One? Because that is not a cash coming back thesis.

Mike: Well, no. I think your text this morning put it perfectly, is Formula One more of like a venture capital, kind of investment or can you actually underwrite it? If anybody's interested in this, anybody can get it for free. I wrote Formula One on VIC in May of 2017. I used to be a VIC guy, I'm no longer because I just didn't have enough good ideas to keep my membership live, but I wrote it up under Clark, it's my middle name, clark0225. You can get the whole thesis there. I think that's aged okay. I don't think it's been not aged terribly.

When I first saw Formula One, so I own Liberty Media, when they did their bust-up into the three trackers between Liberty Sirius and Liberty Media, Liberty Braves. Sold the Braves. I kept Media because it was described to me as Greg's sandbox. That's the way John talked about it. Well, let's see. It's like a SPAC. Let's see what Greg can do. I kept Liberty Media, and I saw the Formula One deal and I listened to the presentation, I was like, "We're paying what 20 times EBITDA for this? What?"

Bill: [laughs] But it's a sport. [laughs]

Mike: By the way, it's one of my friends is on Twitter under @BwkCapital. He hit me up, he wasn't on Twitter at the time. He hit me up, and he was like, "Have you seen Greg's Twitter?" It's a picture of Greg at Formula One. So, I'm thinking like, "Oh, my God. Did Greg just buy an NFL football team for just ego rights? What are we doing? Oh, my God." So, I saw that, and I'm like, I don't know. I like to think that I give them the benefit of the doubt every time. And the truth is, I don't because I just can't get them out of my own way. I see that and I'm like, "Oh, man, what are we doing?" I see the multiple, I'm like, "I don't get it."

I smartly talked my boss into selling every share of Liberty Media at 20. Genius. So, then what happens like, two days later, the stock goes to 30. He's like, "What the fuck did you tell me to do?"

Bill: [laughs]

Mike: I was like, "I don't know. I really don't."

Bill: "You pay me for my judgment." [laughs]

Mike: Who is listening to me at this point? Who is listening to this guy? Everyone's going to ask you the podcast, why do we follow that guy?

Bill: Oh, I love it.

Mike: I tell him to get out of it. He's like, "Well, I think you missed it." I'm like, "Well, I obviously did miss it, I think something is going on, but I don't understand. I'm like, "That's fine." He's like, "Well, you know those people, why don't you figure it out." By the way, my old boss is [crosstalk] Chase Carey.

Bill: Oh, this cracking me up.

Mike: Yeah, I know. I can't believe-- [crosstalk]

Bill: Wait, did you just say that you know Chase Carey?

Mike: I met him several times and really like him, but that's [crosstalk] my old boss, too. Chase went to same school that my boss went to, and they were both on the board at different times. They were both on the board of the college. They know each other that way. I'd say, they know each other, I'd like to say they're friendly. I think they're friends, but I met Chase through him, and Chase is just-- I mean, he's exactly what you would expect. Rupert Murdoch's number two to be. He's perfectly even keel. Steve **[unintelligible [01:17:31]** describes him as the best negotiator he's ever seen, which was critical at Formula One.

Bill: Yeah, he set that entity up.

Mike: Yeah, by the way, he's just the nicest, sweetest guy. I actually think Ross Brawn is probably the nicest sweetest guy, but Chase is right there. I mean, they're just good people.

Bill: Does Chase say you know a lot? If you're talking to him in private, does he always say you know? Because that's the thing on the conference calls that drives me nuts.

Mike: No, he does not. He's [crosstalk] in a monologue, comes up all the time, in private. The conversations are much better when it's one on one.

Bill: I like him. Sometimes I'm like, “No, Chase, I don't know.” I'm trying to find out.

Mike: [chuckles] I'm looking for you to tell me.

Bill: That’s right, please.

Mike: Yeah, you're right. You're not wrong about that. It's difficult to listen to it. It's like for me with Tom Rutledge. I love Tom, but their calls are so boring.

Bill: Yeah, I agree.

Mike: [crosstalk] Oh, my God, I want to fall asleep.

Bill: I actually like Winfrey more. I love listening to Winfrey.

Mike: Yeah, Winfrey is great.

Bill: I think he tells the story perfectly.

Mike: Actually the best presentation I think it was from like a Leveraged Finance Conference in 2017, or something. They were talking about wireless, in my mind, that's the best presentation Charter has ever given. The best presentation I've ever heard on Charter was John, but then the best presentation Charter gave is when Chris was discussing the [audio cut] that’s just very cogent. That just lines up well, it's well thought out, it's very rational. [crosstalk]

Bill: Yeah, if people want to know Charter, I would read Winfrey's. I think he lays it out a little bit better. Anyway, back to Formula One.

Mike: Winfrey's Great. In Formula One, I just sit there stewing on the fact that I'm an idiot and sold it at 20, it's 30. Liberty does a primary offering in the summer, early 2017, something like that. Key for me why I could invest in it was this offering document when they did their primary offering. For the very first time, they laid out what the opportunity was. I mean, you could pick it out. They didn't say, this is the opportunity, but they laid out very simple. We have cumulative global audience of a billion views and you can put that up, that's second only to the NFL in the world. It's bigger than Premier League. It's bigger than the NBA, it's bigger, bigger. They have 500 million fans, global audience of a billion. Then you can compare, we can get, it's publicly available revenue data, not only for Formula One, but from Premier League, from the NBA, from NFL. And you can see pretty quick if you take the amount of revenue generated at Formula One by global audience of a billion, it's about $1 50, it's all worked out, or maybe $1.35 **[unintelligible [01:19:59]** have this. If you compare that, the next highest is the of a major global sport is the NFL. It's closer to $6. Then, you look at the NBA, the NBA is $8. Premier League $8.

Now, in my mind when you just take nothing else, Formula One makes for everybody who watches it makes $1 50 and the NFL makes 6 and the NBA makes 8. That's a huge gap. So, the question is, should that be a huge gap? Can that gap narrow? How would it narrow? How do you explain that? Now, part of it is explainable. The difference between the NFL and the NBA is very explainable in my mind. One, you can't monetize the incremental viewer nearly as well. If you have the Superbowl, you get amazing rates. The rates are huge. Except you have so many viewers that on a per viewer basis, they're not as good as the NBA Finals, let's say, for example. You have almost as good monetization or still good monetization, but much fewer viewers. They have so many viewers, of course, they're not going to monetize them all that high. So, that explains a big chunk of it. You could say, “Well, Formula One's similar, right?”

They have 20, this year, I think, it's 18 races. Hopefully, knock on wood I should be doing. I don't know why I did air quotes. Knock on wood. They'll have 23 races, which is the rumored calendar for next year. 20 some odd races a year. Those are like Super Bowls every two weekends. It probably is closer to something, it should have a discount. The question is how much? Then you go through and you ask like, “Okay, well, where are we underperforming?” Well, couple areas. The biggest one, the most obvious one is sponsorships. At the time, nobody had really talked about it, but now I think there's a lot of research that's been done on Formula One sponsorship gaps. Even Greg's talked about it. I think the UBS left is a sponsor when Liberty bought it, there's now no financial sponsor. There is no sponsor in banking or in wealth management even. It doesn't make sense because Formula One is like Rolex. It's very high and it should be--[crosstalk]

Bill: Yeah, some high net worth stuff.

Mike: [crosstalk] -should be management sponsor. Yeah, absolutely. There is no non-alcoholic beverage sponsors. We don't have a coke sponsor or Pepsi sponsor. Coke’s actually come in at the fringes. They're now doing sponsorship with McLaren. They're on the McLaren car, but they're not a sponsor-- [crosstalk]

Bill: It's pretty insane that they don’t-- Yeah, sponsor the brand. That's nuts.

Mike: No, it's true, and that's the opportunity. You're seeing, it's taken forever. I would have thought it would have come a little quicker. But you're seeing it Aramco, it's the Saudi energy sponsor. So, you're seeing new sponsorships. Big ones. Amazon Web Services is a global partner. They call it not a sponsor, global partner. There are a huge gap. That's just the tip of the iceberg. There are huge gaps. Not just global, but then all of the inventory they have regionally. If you watch a race, which everybody should, Formula One is amazing. You watch races, you can see a lot of it's projected. You can see projections from the camera onto your screen, which can vary based on whether you're watching the United States or China or you're watching it in Europe, you can project, so there's all kinds of regional sponsorship, whitespace opportunities. There's now digital opportunities for sponsorships. There's opportunities everywhere. So, that's one.

Two, the broadcast revenues were a big opportunity. They have a mix of free to air and cable, Sky. That mix can change. The thought was that it wasn't quite as competitive bidding that's changed a little bit because Sky negotiated its new contracts. **[unintelligible [01:23:16]** has now stepped up. So, that's improving a little bit. OTT, I always thought was an opportunity. Merchandising was an opportunity, Paddock Club is an opportunity.

Bill: Yeah, Paddock Club does seem like one. Sorry, I don't mean to cut you off. I always wonder-- I know that they're separate entities, but the idea of marrying some of Live Nation and Formula One and really making those big time global events, like, man, that just seems to make sense to me.

Mike: No, I agree. I mean, there's opportunities all over the place. That just [crosstalk] Live Nation.

Bill: Why the fuck doesn't Rihanna perform like the Saturday night before a race or something like that? Just make something like a huge out of the weekend.

Mike: Yeah. I don't know.

Bill: Where it goes eventually.

Mike: Good question. They have good acts show up in Austin. So, I've been to two races at COTA, Circuit of the Americas in Austin, Texas, and they've had good acts there. I never actually stayed because I'm so tired. I just want to watch the race. So, I always went back and like, hung out in Austin, but they did have big events around it. But you're right, there's a lot of opportunity there to improve the--

not the on-track performance, but improve attendance. More people to show up and give them something else to do, but then also potentially some broadcast opportunities around it, like the Super Bowl, broadcast-- [crosstalk]

Bill: Yeah, that's right.

Mike: Beyonce or whatever. It's opportunity.

Bill: Then you get such a buzz.

Mike: I see all these things, I'm like, “Okay, so there's some opportunity.” $1.50 might not be six, but could it be three like, is that reasonable? You just sort of model it like-- it's more of a VC, except I do have 500 million fans and I've got 70 years of racing and I've got a real business here. The simplest way to explain it and just to say, “Well, is it structural or is there opportunity?” Simple way to explain it is, the entire business was run by one guy. One guy. He did everything. But one guy, and he just turned 90, I think yesterday or the day before he turned 90. We have a similar birthday, mine was on Monday. He just turned 90 years old. The guy's brilliant. He built Formula One, but can one guy handle a multi-billion dollar global operation by himself? Seems to me, if you get a real team in there, there's probably going to be some opportunities. So, that was the whole like, could they close the gap? Okay, so then the next two legs of it, are people going to like it?

Well, I started watching in 2017, I ended up enjoying it really though, I think the game-changer for Formula One was *Drive to Survive*.

Bill: Yeah, that was huge.

Mike: I think the context that Netflix gave you or gives you now for Drive to Survive is massive. You can really see the personalities and so. When they show up to race, you know the backstory, you know the contract negotiations. You know all the players are and you can really start to buy into them, and you can see the drama. Formula One, Christian Horner, it's drama, it's pageantry.

Bill: For those who don't know, it's very similar to *Hard Knocks* on HBO for the NFL. You get to know the people behind the brand.

Mike: Exactly. It's just phenomenally funny. I've actually gotten my friends to watch *Drive to Survive*, and they have now become reasonably serious Formula One fans in the United States. In my mind, that really was sort of the game changer of like, “Yeah, you can get into this.” I was 38 when I started watching or 37. I was pretty much college football exclusively. And now it's like, “Oh, I watch college football, but I'm also a pretty big Formula One fan.” I figured out that that brand could resonate with people and it still had opportunity to grow. So, the second leg of the stoll.

Then the final leg of the stool is valuation. At the time, I think the shares were $30, and $32 today, so it's basically done nothing. I mean, was great, then it was terrible, mount back. The company does before all of this work had gotten done, and there's even one more thing I forgot to talk about, which is team payments. For all this work I've done, I had them generating about $1 a share and free cash flow. And now because of a reattribution they did earlier in the year, it's about two times levered a little over two times levered on 2019 EBITDA. Well, 30 times earnings, that's not great. It's not wildly inappropriate for-- you don't own a team, you own a league. It's a popular league. That's a whole different ballgame than owning a team. The economics are very different. Then, your rights are very different. Well, but it's not necessarily attractive at 30 times.

Then, the question became, "Well, what happens if you get your $50 to $3?" It's like, "Oh, well, if nothing else changes, you go from earning $1 to $3," right? Like, you brought it through, you tell me maybe these are the numbers for 2017. I don't think they've changed all that materially. You triple your free cash flow, like, that's not terrible. Now, as soon as the old team splits, the Formula One teams get about 70% of the gross profit. Formula One keeps about 30%, a little more. NFL, that's more like 50-50. The question is, "Well, could it go to 50-50?" Well, if it grows, sure. If you double the revenue, could Liberty get a bigger share or the brand get a bigger share of revenue? Absolutely. Now, I don't know what the new Concord agreement, the revenue split say, says something. I don't know if anybody's read it. If you have read it, please DM me on Twitter. I'd be curious. But I haven't read it. Is it possible? Yes, it's possible, it's possible to approach that over time. Well, what happens if you get to $3, and you get half of the gross profit instead of 30% of the gross profit? It's like, "Well, $6, $7 a share in free cash flow." It's like, "Well, holy shit," like now we're starting to talk about some very real numbers.

It's an option. It's not to say that it's definitely going to happen, but it's an option. I don't know necessarily. Is it priced in perfectly at 32? Is the option worth more? Well, I can tell you that if this thing only does $1 and free cash flow for the rest of my life, it's probably going to be okay, I'm going to lose a little bit. If they do 6, 7, 8, 10, this will be one of the better investments I ever make. It does have more of a sort of venture capital payout. It's a little more unknown if we can do it, but I'm resting my hat on the fact that I think if we can just get the pie to grow, then it's going to be amazingly well. It's going to work out amazingly well. And I think *Drive to Survive* really is what got me into the, "No, no, this can actually grow. We can grow organically." If you're growing organically, that's the lesson I learned at Zale. If you're growing, all of your problems are solved. Valuation problems are solved, people problems are solved. If you're growing, things are good. I'm hanging my hat on that, and I also just love Formula One, I just love in my mind being like, "Oh, I own this." When I watch it, I'm like, **[unintelligible [01:29:28]**, yeah.

Bill: Yeah. I actually told my mom that. She was looking for an investment. I was like, I think this is something that you'd like. I think it's got some upside and I think it's got some sex appeal. She likes that stuff.

Mike: It's nice to be able to see what you own, your product that you own on TV every two weeks. It is nice, and they have a good race, you can feel good about it. But, yeah, I'm a pretty big fan. That's more far afield from the things I normally do, but I felt so compelled that I liked it so much that I went big. Now, unfortunately, it's not that big because I've sold a lot of stuff to buy Qurate, but my hope is, is that I'll be able to buy it back. [crosstalk]

Bill: How do you think about sizing that? If it's got more of a VC payout, would it not make more sense to have it a little bit smaller and then let it grow with the payout?

Mike: That's right. At one point Charter was 75% of my invested assets. I don't think you can make Formula One quite that big.

Bill: You have massive balls.

Mike: Yeah, I think about them a little differently from other people. I really fundamentally believe that nobody gets rich off their eighth best idea. I think that's true. I have a lot of confidence that my ideas are good ones. Most importantly, that if I'm wrong, that I really won't lose all that much. If you think that your ideas are good, and it's not going to be a disaster if you're wrong, then you should swing back. When it's raining gold, the biggest crime you can make is to stick out a thimble, you should go find buckets. Don't try to capture little pieces, really go after it. Formula One can't be that. I think the biggest I ever had in Formula One is about 15%, which for me is a rounding error. That's a starter position. 15% is just kind of like dipping my toe in just to see if I like it or not. [crosstalk]

Bill: Well, the thing that I think-- now that I do this podcast, people ask me, not this one, but Value: After Hours, people ask me, "How would you get started? Who would you study?" I think that one of the-- what I have been grateful for is, I've had a market that's bailed me out of some mistakes when I've been young, and in my investment career. I think that with a more punishing market, there's a chance that I maybe would have been a little bit too big in the wrong ideas. If you zero out a wrong idea, it's really hard. I've benefited so much from being open on Twitter and talking to people. When I pitched Francisco on Qurate, he basically looked at me and he's like, "Dude, what are you doing? One, I think it's a really good idea. But if you're going to do this, you can't size it at 2% because you might as well just buy more Charter. The impact of your portfolio if you're right is going to be nil." And then talking to you. I mean--

Mike: I'm a drug pusher, like, "Go. Buy more."

Bill: No, but it did though, and I needed that right. Some of it was giving myself the permission to actually believe in my own analysis on something that the narrative was so strong against, which goes to one of our questions, what's the most in your face narrative that you're currently ignoring? Or, I guess, that you've ever ignored, but I got to think Qurate'spretty freakin high on that list.

Mike: Yeah, nobody likes to Qurate. My history with Qurate tells me, I think a lot of people probably were in my seat where they saw it, they thought they like something that nobody else liked, they thought it was a good business. They thought it was misunderstood. They own it, and they got really burned, myself included. They own it, and they lost money. I do think people get emotional when that happens. They think, "That's just a piece of shit. I will never own that." Everybody knew. You're telling your clients like, "What's your best idea?" They're like, "Oh, I really love this QVC." Everybody looks at you, like you have a third eye. Then, you're like, "No, but trust me, I'm smart. I really know." Then, it goes against them, and they look like idiots to themselves, their clients are like, "Who are you? What are you buying? Everybody knows QV." It's like this, "Oh, you made me look dumb." And so people take that personally and then they just, “I hate it.” Like, “Bill, don't tell me about QVC. I hate it, I will never own it. I don't care if it triples.” In my mind, that's what's happened, and that's where you are.

By the way, that may mean it never rerate. So that may mean people just not liking it, maybe it’s forever in the penalty box. If I'm right about the first part of the thesis that all my capital is coming back to me in very short order, in my mind, it really doesn't matter. It doesn't matter what anybody else thinks. I mean it doesn't matter if the stock goes to two. If I'm right about that, nothing else matters, then everything else was just, it's gravy, or it's not efficient.

Bill: Yeah, what changed it for me is to your point because somebody had asked, he's like, “Well, what's different between your thesis? This has been the same for four years.” I'd say, “Yeah, you're right. The difference is now there's actually the option, they’re preferred, you can do what you want, but you got cash coming back to you now.”

Mike: That's right. Yeah, it's different.

Bill: That's a way different ballgame than owning more and more of an allegedly shrinking ice cube, which may be shrinking, to be fair.

Mike: No, it may be. We're going to find out that's the good news, but the preferred is trading like it should. It's trading right around par, which is telling you that they have changed the cost of capital. They took out $100 million in free cash flow, they stuck in an 8% yielding security which is 12 and change times. That's what the yield on the multiple, 12 and change times. So, they got 100 million of your cash flow now yielding eight, versus the common, which is yielding 33%, that is a structural change to the cost of capital of the business, is a structural change to your return as an investor, like I was able to sell 100 million in my cash flow for 11 times earnings. Now I own the rest of it. I own the, whatever 900 million or a billion that's left at three times. For me, that's great.

In my mind, it's a very real change. I'd like to say that I'm pliable, that I'm open to change. I think that's key to the investment process, to recognize that you're wrong, but recognize also that QVC doesn't care if I own it or not. It doesn't care that it burned me in the past. It doesn't care that this emotional stuff doesn't matter. It makes no difference. It also doesn't matter to me, getting back to the narrative question, a dollar earned from Microsoft is worth the same to me as dollar earned from QVC.

Bill: Oh. Oh, no. He did not say it.

Mike: I know, I'm sorry. I should use the different one.

Bill: Oh, my gosh. [crosstalk] Microsoft.

Mike: If you're giving me a dollar--I know, I'm sorry. Microsoft is amazing-- Everybody owns it, I should go out and do something different.

Bill: Oh, I'm flummoxed.

Mike: I should give myself another-- if you're Formula One, something else I own, to attack myself, you give me dollar from Formula One, that dollar spends exactly the same as the dollar you gave me from QVC. It spends the same. I can buy more with the dollar that Formula One gave me than I can with the dollar that QVC gave me. So, I am indifferent where the dollar comes from. What matters is how many dollars I'm getting. That's the key. If you don't know, then you should expect more quick. If you do know, then you can go out a little bit if you're going to get paid. If you have confidence in that option, if you know what that's worth, you can pay more for it. Just in a lot of businesses, Microsoft is a great example. I don't know what the Azure option is worth. I have no idea.

Bill: Yeah.

Mike: Some people do. I don't, and that's okay. I don't feel like I need to know. I don't know if that option is trading cheap today, or is trading expensive, what I do know is if you're putting a value on that option, or at least the value that the market is putting on that option, you're going to be fuckin right. Or, it's going to hurt you. If you're not right, you're going to lose a lot of money. So, that option can't be worth zero. For QVC the option could absolutely be worth zero. That's the difference. Okay, so that's one narrative. The second narrative, I see people say it and I'm like, "Oh,--" [crosstalk]

Bill: Oh, we're going to go to never sell? We're going to go never sell?

Mike: Yeah, never sell kills me.

Bill: "Oh, come on, now. Chuck Akre, I'm upset with you." What's up, Chuck? Thanks for listening.

Mike: I know. By the way, he's earned the right to do whatever he wants.

Bill: Chuck's a monster.

Mike: He can do whatever he want. I don't care what-- Chuck say anything he wants, he can do whatever he wants.

Bill: Nice guy, too.

Mike: Oh, I've never met him, but he comes across as **[unintelligible [01:37:08]**. I'm not going to tell Chuck he's wrong. Public markets, you have several advantages in public markets. In my opinion, it's my opinion, one of the biggest, if not the biggest, is the liquidity. That matters. I can decide tomorrow, that I'm wrong on QVC and I can get out of it. I can decide that I sold Charter, I can decide tomorrow that I was wrong selling it, I can get back in it. Coming in and mentally saying I am never going to sell. In my mind is like you just gave up one of the biggest advantages that you had. In my mind, it's dumb. You absolutely can. When you see something get to-- think of it like your house. This is a example I use with my in-laws. They not finance people, they're physicians. I say, well, how do you think about tax? Think about it like your house. You own your home, I bought a home in Fort Collins in 2018. I have an idea of what it's worth, it doesn't really matter, because I'm not going to sell it. I think probably it's worth a little bit more than what I paid for it. I think about that a lot, but it doesn't make a bit of difference that it's worth a little bit more because I'm not going to sell it. Now, think about your home. Okay, let's say pick a number, round number. You paid $500,000 for your home. Now somebody comes and offers you 550 it's like, “Oh, okay, that's fine. But I love it here. My wife, we got kids. I'm not moving for 50 grand.” [crosstalk]

Bill: Yeah, that’s right. You give me 2 million, I'm out.

Mike: Boom. That’s it. That’s the whole [crosstalk] point.

Bill: That’s how I feel, too, man. That's how I feel, too.

Mike: That’s the whole point. Go on.

Bill: Yeah, I know.

Mike: By the way, you tell me, Charter is going to be 30 bucks, and you say it's worth 20 times. I'm like, “Okay, I get it.” I don't necessarily because cheap, but I don't necessarily think it's expensive. I see why somebody would make that bet. I get it. You come in and you say Charter at 50 times earnings. Hit fucking big, dude, run. Run away. Don’t walk. Sell to that person. By the way, the pushback on me would be, “Look, Mike, you're right, but my house is an I never sell asset. I treat this as a never sell asset. And it's a way to just keep my psychology right. And that's fine. I have no pushback on that. That's great. Keep you psychology run-- [crosstalk]

Bill: Yeah. Or, helps you fish in a better pond, right?

Mike: Yes, all of those are good things.

Bill: If you're going in with never sell, maybe you're fishing at a better business level. I can understand that.

Mike: All of those are good things. I came out of Zale with people matter, I came out as a with business models matter, which is now that-- **[unintelligible [01:39:22]** likes to say that a lot. And so that's what I say, but it really is saying quality, and quality matters. And you're dead right. But there is a price. 10 years ago, when you talk stocks to somebody, somebody said, “Well, I have a three to five-year view.” That'd be a very fundamental long term guy would say, “I have a three to five-year view. I don't care about stimulus. I don't care about the election. I have a three to five-year view.” I feel the narrative now isn't I have a three to five-year view, it's that I'm never selling. We talked about it. We'll see if that's right.

Mohnish’s view is like, “Listen, you look at the guys who have great returns, they have great returns because they just bought one thing and they never sold it.” So, you can afford to lose a lot of money and nine things and you make by-- it sounds very venture capital money, but you make money into one thing and it covers all the sins, and it's like, yeah, but, man, how do you know? What if all 10 of them are wrong? How do you know? I don't know.

Bill: Well, this is where I've gotten with the David Gardner research that I've done from Motley Fool. I think what he does well is he is very quick to identify these things. He's an early adopter on both the product side and the stock side. I believe he's got more of a spray and let it run approach. So, over time, the right tail will take care of his returns, but he also says like, I will hold it to zero, because there's some of these stocks that he owns that 6X and then get cut by 80%. Then maybe 3X and he doesn't know.

Mike: Yeah. Look at American Tower. America Tower is classic example. America Tower is the greatest thing in the world. It's 50 cents, dude. If you have a psychology where you can hold it at 50 cents, then you should own it and you should never sell it because selling it at 50 cents would have been the worst decision you could have made. I'm just saying, everybody's pushing that agenda, or that's an overstatement. That agenda is getting a lot-- [crosstalk]

Bill: Certainly on Twitter.

Mike: -credence. I look at that, I'm like, the only reason it's working-- I think her name is Helene Meisler. She's a strategist trader that I follow because she follows Tony Dwyer and I really love Tony Dwyer, who is a market strategist. I don't know anything about market strategy and I don't do anything about market strategy, but I love hearing about it. Some people like politics, I like market strategy.

Bill: Yeah. Well, it's like a finance porn.

Mike: Yeah, exactly. Helene has this pinned tweet, in my opinion, is the best pin tweet. I'm paraphrasing, "Nothing like price to change sentiment." This is what we were talking about earlier. The reason why I say never sell is because they're looking at when they sold Netflix at 300, now it's 500, and they're like, "Oh, my God, I was an idiot. I should have just never sold," and it's like, maybe we'll see. And it was nothing like price to change **[unintelligible [01:41:41]** it. Yes, the price is up doesn't mean you're right, doesn't mean you're wrong. It just means the price is up, that's all it means. Does not mean anything else. It's the same with when my stocks go down. Price doesn't mean anything. Ultimately, I've got to be right about the business, and I've got to get my capital back. If that happens, fine.

Bill: Yeah. By the way, shout out to Jerry Cap, the leader of the never sell movement.

Mike: Oh, yeah. He's an animal-- [crosstalk]

Bill: The way that he frames it, I think is smart, where he said, "It's not about a single trial. It's about a method of life." I do understand that, but I personally cannot get past what you said. If somebody is going to offer me $1200 a share for Charter, there is no way that I am not going to sell it to them. None.

Mike: No.

Bill: And it's going to feel great when I do it. One day, maybe I'm sitting on a nice house, and I say, “Boy, I could add a little bit nicer house.” The goal of this game to me, is to get to the house. Then the rest is, whatever.

Mike: No, it's true. I think that's right. My push back on the never sell would be, at what price would you sell? Or is it no price--

Bill: Yeah, there has to be some.

Mike: There's no price. That's the question. For me, for Charter, in 2018, when we had the meeting of, “You're a fucking dope, you're dead wrong about this, the stocks down 40%. You're an idiot. How did you miss it?” At that point, I want to say the shares were like 275 or 300, or something, down from 400. At that point, if you would have asked me, “Mike, would you sell every share--” Even on your numbers, which you're an optimist and your numbers reflect your optimism on Charter, even on that, would you sell at 600 that time and shares were 300? I would have told you, “If you give me a look at 600 in the next two years, I’ll sell you every share that I have.” What did I do? I sold every share that I had, this one I said two years ago. Are the numbers better? Yeah, but it's like plus-minus. I mean, I was thinking 30, and they're going to do 30.

In my mind, you have that, and again, nothing like price changes sentiment. The price goes up and you think, “Oh, I'm a genius. I should just keep holding this.” And it's like, maybe. The books I really have enjoyed reading recently are books that talk about market cycles, and they talk about-- Like *The Great Crash*, by Galbraith is a great book. Everybody should read, it's written in the 50s. There's a book by Maggie Mahar, which I talked about on Twitter called *Bull!* and it's a bull market book from 82 to 2004, really peaks in 99. Book from Leon Levy, there's great books that talk about that psychology of that market. What happens is when prices go up, people tend to like things more. In fact, the opposite is what should be happening. The higher the price goes, the less you should like your house, you like your house at 500. But at 2 million, you should fucking sell, dude, like I will be there moving your stuff out for you, if somebody offers you $2 million for your $500,000.

I do think when you put in those terms, people tend to get it. In my mind, the people who are saying it, maybe they just haven't seen what happened. The answer was Zale is you should have run. By the way, Ecolab, which I own for a while, and they bought Nalco. I love that business, you should have sold that, too. You should have sold everything in 2008. It wasn't a thing you should’ve own. You should have been cash. That was the only thing that was at any value. I mean, that's a really scary talk. If you haven't seen it, I'm not sure you really appreciate how bad it can be.

Bill: We almost saw it in March, and then everything got bailed out.

Mike: We got close. There was a day, I think, maybe two days, I'm getting this from web, I didn't physically see it. I did talk to some guys at Oaktree on Formula One debt actually, and they were talking about it. They're buying Formula One debt at like 80 cents on the dollar-- [crosstalk]

Bill: Yeah, man, the debt blew out. Blew out.

Mike: Yeah, blew out.

Bill: I was buying TransDigm north of 11%. I was like, “Alright, I mean, this is a pretty good business to pay this kind of--"

Mike: Makes sense to me. Give senior position, get a double-digit return on your money, sounds great.

Bill: No, it looks stupid.

Mike: Yeah, exactly. It sounded like, there was a day or two where it looked like this is going to crack and then what happened, Fed comes out and they said, “It literally is not going to happen.” Take cracking off your-- we will buy high yield bonds. Boom. Okay. Now, what do you do with that? You just start buying. That's what you do with that. You just start-- That’s when I flipped from being like, “Oh, my God, this sucks,” to like, “Oh, you got to own everything.”

Bill: That's what I missed. People said it, and I had bought quality and I stayed in quality. I guess, I don't know if I'm mad at myself, or if I think that was the right thing to do. I mean, it obviously was wrong. But I still think I do it again if I had the shot.

Mike: Well, that I tell you, it's not right or wrong. I do take issue with people who say, “Well, this was clearly the right decision.” It's like, it's not about the right decision, not the right decision for you. That's the key. It's your psychology. When people talk about circle of competence, what it really means is not just what you know, it's what you can handle. If you don't know yourself well enough to know whether you can handle or something, just don't do it. Just don't do it. You will not be worse off. You tell yourself like, “Oh, I missed it. I missed it.” There's some things that I missed, and that kills me. But the vast majority of stuff like, “I don’t give a fuck that I missed SaaS. Who cares?” Maybe I should have had a view on Amazon, but I would have missed-- you would have told me about it, I'd be like, “I don't know.” I would have missed it. Don’t beat myself up about that stuff. It's the things like I know that if QVC worked after we talked about it, and I didn't own it in size. I’d kill myself. I have known this business for a lot of time. I know the people. I know what they're doing. It makes sense. You’ve got a free option in there. It's right down the middle for me, man. It doesn't matter to me if it's down the middle for everybody else. It's down the middle for me. That's the key. If it doesn't work, yeah, okay, stuff doesn't work. It doesn't work all the time. I’ve got plenty of losers.

Bill: I talked to my mom about that, and she's like, “What's our stock doing?” I'm like, “Mom, it's a business. People are inside. They're selling things. We need to work on conversion. Worry about it that way.” It's interesting when you're public.

Mike: Now, the answer in the short term is what happens with QVC, it will be interesting to see what they say on earnings next week. If that even matters, by the way, it may matter or may not. I don't know. But in the short term, in my mind--

Bill: What do you think they could say that would make anyone believe anything in that entity?

Mike: I don't even know. That’s a great question.

Bill: What would make catch a bid? They could come out and release everything. People would be like, “All right, this one time.” Okay.

Mike: The smartest people are in short stocks, what they tell me is, they say, you'll know you have a good short thesis because in your mind, you're thinking, “What can they say that gets the long only to sell it?” It's not about what happens. What happens is irrelevant. What matters to you, if you're short selling is the big holder selling because that's what's going to push the fucking stock down, which is what you need if you're short that obviously. Then say, “Well, what's going to get those guys to sell? Let's invert this. What's going to get a long only to come in and say, “You know what? I got to--" [crosstalk]

Bill: Nothing, man. They won't do it.

[laughter]

Mike: [crosstalk] I don’t know. I really don’t know.

Bill: That’s why--

Mike: [crosstalk] -they do it.

Bill: That's why I think of it like there's only so much money that Maffei can plow back into the stock before it must go up.

Mike: Well, that's right. In all honesty, I think about the only thing you could say, that would get people to say, “Oh, okay, you were right. Is it they announced a sale?” If they announced that they're selling the business, then, yeah, okay, then it's going to be in your face. There's a private market value for this thing that's north of, what do you think the stock is now? Four or four and a half times, five times EBITDA, something like that? [crosstalk] -selling six time EBITDA--

Bill: Yeah, I thought you were saying share price, I was like, “Well, maybe--” [laughs]

Mike: Yeah, I don't want to [crosstalk] Also, my face will just get really scary-- [crosstalk]

Bill: Yeah, [crosstalk] -sad again.

Mike: -my eyes will sink in. [crosstalk]

Bill: People will start to watch price driving narrative.

Mike: Yeah, exactly. I'm intentionally not looking because, A, I'm sure it's terrible, and, B, **[unintelligible [01:49:06]** some. But, yeah, that's not the only thing.

Bill: I haven't worked a lot since that. I've tried to, but one, coming down off of a deal is hard for me. Two, I haven't wanted to be around things as much because I don't really want to see what's going on for a while. It's been nice. There are certain days that I have no idea what the market does.

Mike: Yeah, that's good. That's part of what I've been doing out in the garage, putting together carpentry projects, just staying away. It's hard to do. My LP is one, it's my wife. I don't have even people that respond to it. She didn't even care, she has no idea day to day. We did it. Part of it for me too, and not being able to care as I know that I've actually had a pretty decent year going in September and, of course, my October's has been a complete debacle. Even with that, it's still a pretty decent year. My hope and expectation when I underwrite something is, I'm shooting for 10% a year, that's what I'm shooting for. I don't know that I'm going to be able to do it over time, but I've been shooting for it. When I cross that threshold and get comfortably over it in a year, I feel like, okay, I can press it a little bit and see how it goes. Even if I landed, it costs me all that performance, like cost me-- if I was going into the end of September, I think I was up something like 16 or 17. That's part of the reason where I'm like, "Dude, I could lose 10% on QVC, I'd still be up five."

A year with COVID with unemployment, I'm up 5%, **[unintelligible [01:50:24]**. I don't mind so much pressing it, but it does give me the ability to step back and just say like, "Just don't focus on it." The price isn't going to tell you if you're right. That's the key. That's actually the distinction. People call it growth versus value. In my mind, it's a distinction of, "Are you a fundamental analyst?" As part of that, you care about what the price you're paying for something. Or, are you a momentum, and I want to use it. Well, people hate it when I do this on Twitter, they get really offended, but the word is speculation. It's not a bad word, by the way. Phil Carret wrote a great book called *The Art of Speculation*, which anybody should read. It's a great book. I've read it, I enjoyed it. I speculate often. That's what horse track betting is. It's speculation, you don't know. It's not fundamental analysis. Fundamental analysis gives me the ability to step away from prices. If I was purely speculating, prices are the only thing that would matter. When it turns out that somebody isn't, in fact, going to pay me more than what I paid for it, I need to get out. Fundamental analyst, I can step back and say, "No, I underwrote a business." The business is what I-- I don't own the stock price, I own the business.

I can step back, the price won't tell me whether I'm right or wrong. The business results, and the management's capital return will tell me if I'm right or wrong. The stock could go to $3, it could go to $30. I'm hoping for the ladder, but it's the business and a management team that's going to decide whether I'm right or wrong. It's not the price. It's hard for most people to do. I think that's why most people actually just prefer the speculation route because it's so much easier, like Puru, so much easier. Like, "Look, this business is growing. I bought it, it's up 20%, I sold it." Jesus, that's easy. Just do that. I cannot get it. You said this in your-- It's absolutely right. Don't knock it. It's just the strategy, and it's working right now. It'll keep working.

Bill: I think that there is a legitimate argument to be made. I mean, Damodaran made it in his last post, or whatever. I didn't think the post was fantastic, but some people that pray to the value church, or the fundamental church or whatever, I think it's the only way to make money, and don't. I guess what offends me sometimes is when I see guys that I think like, look, if you really want to buy Snowflake, and you're really going to own it for 10 years, then we can talk about what the economics look like 10 years from now. These guys have bought fastly, and now they're capitulating, like, get out of here, you're not long term, and I don't even care. Be a short term guy. Just don't tell me your long term because then you're fake.

Mike: For me, number one, 1,000,000% would just echo that. I mean, everything you said there is right. The thing for me is, it's not that there's only one way to make money, but as I look around, and you look at how the wealthiest people have made their money, they made a few ways. So, you're either incredibly intelligent, and you started a software business. You started Facebook, you started Microsoft. If you did that, hats off. That is a way to get incredibly wealthy starting a business or investing in real estate's a way to get wealthy. I've seen a lot of people who have been fundamental investors become really wealthy over time, of those I've seen more of them become do it in a way that's concentrated or at least they did it with a few bets, as opposed to a lot of bets. In general, Walter Schloss is a great example of somebody who went the opposite route, and it still worked out very well for him. What you don't see is a lot of great examples of speculators doing very well over long periods of time.

When you look at the Forbes 400, show me the speculators. By the way, you can point to some, there are some, like Soros, I think, is a pretty good example. I think a lot of what he does, he is famous for currency speculation. That's what that is, by the way, when you're buying currencies, it's a speculative bet, relevant speculative bet, and he's made a lot of money doing it. He's one example. Show me 10. Show me 20. It's not that you can't do it. It's just that I don't see it as much as I see the fundamental investors. Now, that could change. This is the trailing Forbes 400. There could be a different Forbes 400, when I hit my 70s, but no, for me, I just-- you look at how people have made their money, it's more the fundamental side. It's less the speculation side, but that doesn't mean it'll be that way forever. If somebody has figured out a way to crack the code. I mean, you read the Jim Simons' book, it's like, the guy figured out a way to crack the code. If you crack the code, hats off, dude. I wish I could. If I knew how to do that, I would **[unintelligible [01:54:45]**. I just do that.

Bill: Yeah, no doubt. [laughs]

Mike: [crosstalk] -that's all I would do, but I don't know how to do that. That's off the table for me.

Bill: That's what I have gotten to the point where I enjoy a lot of the Twitter feeds that I perceive to be more momentumy. I've started to listen, when they say like, "No, we look at valuation," and stuff like that. I mean, Puru is a guy that I used to dismiss a lot, and then he did a podcast, and I listened to him. I was like, okay, we're just playing different games. I appreciate the game he's playing. I don't know how real or not his results are. He says they're real, I have no reason to not believe them.

Mike: Sure, yeah.

Bill: People want to get into it, I'm not going to waste my time getting into that.

Mike: Who cares?

Bill: Yeah, that's how I feel. I guess that once I understood what they were doing, in general, some of these accounts, and then once I just got comfortable with myself, I was able to enjoy-- learning what I can from them. My way of looking at it is, if I can learn a little bit something about these businesses now, maybe I'll get a bite at the apple down the road, and that could be awesome.

Mike: You very well may. I do think the time that we're in is, this is time to sit and reflect and learn. I don't think this is the time to be aggressive, personally.

Bill: Yeah, I agree.

Mike: I think that strategy is the right one, this is a time to-- there's always something to do, sometimes that is reading and listening and being quiet and paying attention. Sometimes it's not being active, and that's kind of where my head is at the moment. That can obviously change at anytime. I think that thought and strategy is right, just read, listen, you may get a bite. I mean, there's a price on Visa, where that's the only stock I would own. It's not hate of the business. It's just that I don't understand well enough to pay the current price. It's the same with Nike, I don't understand it well enough to pay the current price, but at a price, I don't have to understand it that well, I'm probably going to do fine. I think studying and paying attention right now makes a lot of sense. I think that's where we are.

Bill: I used to think Nike had to be a Qurate’s multiple to have that statement, the statement that you just made makes sense. What I've realized is that you can buy class A assets, a class B minus prices, and have them fit the quality-- like what you were just trying to say.

Mike: Yeah.

Bill: Waiting for the class A asset to trade it just like bargain basement. I mean, maybe you get that in 09. I don't think that's a reasonable strategy to invest in, if that makes sense.

Mike: No, it does. Couple of thoughts. One, something as I thought about. Doing this podcast with you, I was thinking about, like, “What insights have I gained?” I’ve been doing this for 15 years? What did I learn that I felt was insightful or helpful that might help other people? Zale is a good topic. One of the other things I got from KKR in 2013, every other year, they used to do analyst days, and in the off years, they would do like teachings for their investors. I was invested in the-- not as in LP in a KKR fund, but I invested in KKR, the management company, and to promote public stock.

I went to one of their teachings in 2013, I don't think it was a slide, but they had one of their portfolio managers up talking about how for-- since 1986 or something, they've been doing deals, and they put every metric of the deals that they did up on a screen, up in a spreadsheet, up on the screen, and said, “What drove the performance? When something worked, when something didn't work, what were the factors?” They said, “We boiled it down to one.” I was like, “That's great,” because one thing I can remember. I can't remember four.

Bill: [laughs]

Mike: “Give me one.”

Bill: “That’s what I'm asking for.”

Mike: “Give me one, I’ll remember.” This is a bit of a paraphrase, but the guy said, “The number one factor for returns up to 2013 is growth, is the number one factor.” What they said is, you don’t need massive, it's not 30% growth, it's growth above inflation. So, think about it as 200 basis points above inflation. If you're growing 200 basis points above inflation, that resonated with me because I saw that at Zale. In my mind, I'm thinking if we could had just grown rather than, people would have stuck around, they would have felt like, “I've got some upward mobility.” Versus, if you're shrinking, I have to cost, I have to fire people, that's best people leave. It's virtuous. When you're growing and you're growing above inflation, and I don't really care so much of its price or volume, depending on the business in the industry. But, obviously, I think volume generally would be considered to be a better one because people always think, like with Charter, you got price in your back pocket. If you need it if you get the right business.

Bill: That’s why I prefer Charter to Comcast. [crosstalk] I just like the strategy more.

Mike: I agree, but that growth above inflation-

Bill: I mean, that's one reason.

Mike: -it's just so logical that that's your driver of returns when you own a business for five or seven years. There's studies, there's a podcast from Invest like the Best from the summer of 2018, a guy called Jason Karp who **[unintelligible [01:59:24]** -- he's a friend of a friend that invested in Hu Kitchen. He talked a lot about how growth solves a lot of sense. You can overpay, and this is a Munger thing, so you get **[unintelligible [01:59:35]** you can overpay, and if you grow, eventually, you'll grow your way out of that problem. Now, that has a limit, and we can talk about the limit, and I can tell you why I think people are missing where the limit is, but forgetting that for a second. Growth is incredibly important, and so that was one of the lessons that I took out that I got from KKR. In general, you're underwriting something, I think you would prefer for growth.

As I'm getting this to you, this is going to require an edit. I had this whole train of thought on why I wanted to get the growth conversation out and then go back to the conversation we were just having, but I just totally lost the space. Where I started off, I went on the non sequitur for KKR, but I was going to bring it back, and I'm just now forgetting [crosstalk] back to.

Bill: What were we talking about?

Mike: Yeah, did I do it to you, too? We were so enamored with growth solves all manner of-- [crosstalk]

Bill: That's right.

Mike: Listen, you talk quality, and quality matters. To your point about buying in the dip earlier, focusing on quality--

Bill: Oh, we were talking about multiples and how you can't have-- like waiting for the A class to trade at C class passes--

Mike: Oh, yeah.

Bill: -is not, yeah.

Mike: I became a GARP investor, which people don't use that term anymore, now you say it is business quality but it is essentially GARP. There is an upward bound to what I'm willing to pay for something that's great, and it's simply because I know I'm not smart enough to know for sure that I can pay the higher price and still get bailed out. I think people talk about--

Bill: You're sounding like Buffett.

Mike: I know, don't be surprised, I've read so much about that guy's. It's probably I just adopted. Then everybody says, "Well, it's no problem, because not only can I grow my way out of it, look at my returns on invested capital." Returns on invested capital, which is so amazing. Look at the business returns of this capital. I'm like, "Wait a minute Let's turn this into media." "Wait a minute. Can you invest all of the capital that you're--" [crosstalk]

Bill: Yes, man. That's the question.

Mike: Are you sure?

Bill: What percentage of the capital can you reinvest at that rate? Yes.

Mike: I'm not sure. I don't know. Now, okay, so you run your beautiful model, like I owned it for 20 years, and I reinvest all my capital at 40%. Look, I can pay 500 times earnings, I still make more money than if you pay 10 times earnings, and you only reinvested at seven. I'm like, automatically, you are right. Now show me the company that for 20 years can reinvest all of that-- [crosstalk]

Bill: Or, even half, dude. Even half.

Mike: Okay, so now do this exercise. Run it with half. What happens? You get smoked.

Bill: Yeah, your valuation has to compress like crazy.

Mike: [crosstalk] -45%, you get smoked.

Bill: No doubt.

Mike: The outcomes are wildly different when you can only invest half of the capital over 20 years, then you can invest all of the capital at those rates in 20 years.

Bill: Yeah, extrapolating early years into late years is a great way to get killed.

Mike: That's why I get panicky because I don't know. Okay, so now let's parlay that into medium. I'm a media guy, but I don't really understand how media works. I get the moving pieces, but I can't define the future of media. So, makes me very nervous when your business model is aggregating eyeballs to sell advertisements to, forever. It's an amazing business, by the way. The model is great. It works. The problem I have is, I don't know where the eyeballs are going. 50 years ago, the eyeball was all on newspaper. At that time, you could just bank on it, always being a newspaper, there were no other mediums. Now, mediums are popping up every single day. If I'm Facebook, and I have all of this advertisement revenue, and it's all coming because I aggregate these eyeballs on Facebook, I successfully acquire WhatsApp and acquired Instagram as well, and they're successfully-- I don't know what the next one is going to be. I know there's going to be a next one, that I am confident and that it will not stay Facebook and it will not stay Instagram for 30 years, there will be another one, whether it's TikTok, or I don't know.

In my view, the eyeballs are going to keep transition. They've been transitioning, they're going to keep transitioning, it's going to keep changing. I don't know where they're going to go. So, if you're Mark Zuckerberg, what do you do? I think the right strategy, which is the one they're doing, is you just buy everything.

Bill: Or copy.

Mike: So, buy it all. Or, copy it, yeah. By the way, copying sometimes works, sometimes it doesn't. I personally, I think you're better off just trying to figure out what's going to work and buy it. I guess that's a long-winded way of saying, if that's your strategy of, like, yeah, I get it. There's nothing recurring about the eyeballs that are coming to my website, they might go to somebody else's website. I don't know, by the way, 50 people are going to hit me on Twitter and talk about what a fucking dope I am because I don't really understand-- They're going to nail me on this.

Bill: Yeah. That’s going to happen. [chuckles]

Mike: They're going to be like, “No, you understand because--” My answer to that is, “You're right. I don't understand. That's what I'm actively saying is I don't understand, but my speculation would be that they're going to have to buy a lot of shit, or invest a lot of money into things to try to maintain that next edge, whatever the next thing everybody gravitates to. I don't like that business model. The reason I don't like it is because I don't know what that means. I don't know what are you going to have to pay for the next thing, is the next thing like Snap doesn't sell to you, are they going to take over the world? I don't know.

Bill: [unintelligible [02:04:19] or whatever.

Mike: I can't comfortably tell you that every one of those deals they do is going to be an Instagram or WhatsApp or even one out of five and so they're going to average of 40% return on invested capital, with the average of five, now run your model with a five and tell me what that was like--[crosstalk]

Bill: Devil's advocate would say they only need one.

Mike: Yeah, and they may get it, but I'm saying would you buy it? They have to. That's my point. You have to get it. If you don't get it, you're dead. So, that's just a model where I look at it and I'm like, I understand why people like Twitter as a stock. I get it. It makes sense because it's a really cool platform. What I would say is two years ago, I didn't exist on Twitter. I didn't really start engaging with Twitter until 2020. Then, that engagement-- now Twitter has a lot of my mindshare and a lot of my daily engagement. Who's suffered? Video has suffered as a result of that, maybe Instagram has suffered some as a result of my engagement on Twitter. The thing is, what if something else comes out tomorrow that's better than Twitter, and Bill Brewster is no longer on Twitter, but now he's on Reddit." Am I going to stay on Twitter? I'm going to follow Bill Brewster to Reddit.

Bill: Oh, I appreciate that. I'll follow you, too.

Mike: Well, thank you.

Bill: [laughs]

Mike: I'm just saying when you can aggregate a large audience really quickly, what that tells me is somebody else can also aggregate a large audience really quickly. It makes me really nervous--[crosstalk]

Bill: Mm-Hmm. Part of my issue is so many SaaS companies, man.

Mike: I can't own it, because I don't know. By the way, if I did know, the model is so good, that I would just be all in on it. The economics are phenomenal. If you knew for sure, put it all on the table. Then, by the way, don't check stock prices, just put it on the table and run away.

Bill: Well, you know what's interesting? [crosstalk] No, this is perfect. Zoom, when you talk to people about Zoom, what do they say? They're like, one of the best things about Zoom is it just works. One of the things that like Silicon Valley is so in love with and I think for the right reason is reducing friction. If it just works and reducing friction is the ethos, and you have $140 billion market cap. I understand that enterprise software used to have high switching costs, but the difference is now it doesn't. Look at how quickly Zoom came in. I don't know why somebody can't replace it.

I can tell you why we're not on Zoom right now, I think this is a much better audio platform, and I want to do this podcast the right way. Is that going to matter? I don't know. Will Zoom iterate? Yes. But relying on that kind of invention over and over and over again, that's just a lot of money. I would have said the same thing 10x ago. So, I don't have standing to say this, but this makes me nervous.

Mike: Yeah. This is an industry where you win by pulling a rabbit out of a hat. By the way, when it works, it's amazing.

Bill: Huge.

Mike: It's amazing. Yeah, the thing is, it's not that it's not great. I'm with it that it's amazing. What I don't know is who's going to pull the rabbit out of the hat, and at what time. That I don't know. You say, "Mike, I'm going to give you a year ago, figure it out." I'm not that smart. I don't think I'll be able to figure it out. I'm also very skeptical and somebody else tells me they have it figured out. If you didn't have it figured out, why are you investing? Why are you not just creating it? If you really want to get rich, create. How much money did Zuck have when he created Facebook? You don't need capital. Just go do it.

Bill: I know, man. Then, the other thing is, okay, so you and I go out to do this, how are we going to do it? We're going to hire a Gartner. Who in that industry has the incentive to raise their hand right now and say, "Hey, guys, things are going a little bit nuts. Maybe we all just need to pump the brakes."

Mike: No, it's not going to happen.

Bill: Everybody's incentive is to sell a bigger story. I just hate those--

Mike: Enter the SPAC.

Bill: Yeah, right.

Mike: SPAC enters, stage left, and goes right to the center.

Bill: And I hate to be such a Luddite, and an old man about it, but that's just how I think-- Everybody's making so much money--

Mike: Nobody likes the guy who goes into the party and says, "You guys are wasted. Stop. Everybody go home." It's like, "What a fucking loser." But I'm a perfect candidate for that, because I am a loser, and I drive a minivan. So, I actually-- [crosstalk]

Bill: So do I, and so am I.

Mike: [crosstalk] [laughs] -in his minivan to the party, where everybody's getting wasted and getting rich and telling me what an idiot I am. That's actually my problem with the market generally. People say, the debate is, do valuations make sense? I think the smart people are having that debate. Where I shake out on that debate is that forgetting whether-- and it always devolves into my view on interest rates and inflation. My favorite is Twitter's view of inflation and interest rates. I'm like, guys, seriously. I am smart enough to know I have no fucking idea. Do not ask me about inflation. I would have told you in 2011, that we're going to see some inflation. That was almost 10 years ago, and I'm still waiting. [crosstalk]

Anyway, people have this conversation about valuations, I'm going to make it very simple. The people who are doing the best, in my opinion, are dopes. Just going to call it out there. The dumbest guy in the room is making the most money. Now, that's a sign. It's a sign. And they're going to be like, “I can't believe you said I was a dope, you're a dope.” And you're right, I am a dope, I own it. I'm saying that these people are not educated about the businesses they own. They're not educated about valuation. They're not educated about history. They're literally buying it and it's working. In my mind, that is a sign that the party has gone on way long.

Bill: Yeah. I think that’s right.

Mike: I'm actually encouraged when I see this correction that we're having, and maybe it'll end up being a crash, it only depends on who you talk to, but the correction we're having in my mind, I'm like, “This is great. What you want, you want some sobriety to enter the market, that's good for the market. It's good for people.” I actually don't think it's great when everybody makes money on speculating, and it's not a good thing for them. It's not a good thing for societies because it's going to end the way it's always ended. It's going to end in tears, people are going to lose lot of money.

Bill: If it doesn’t, man, forward returns are pulled to today. That's not good either. Then you got wealth inequality stuff.

Mike: Yeah, push that out. Forward returns are pulled in. I agree with that. Let's say that that's true. If you pulled the person who is making 50% right now for the year, do they think they're going to make 50% next year?

Bill: Yes.

Mike: [crosstalk] -is they do think that, right?

Bill: Yes.

Mike: What happens when it's the other-- It doesn't go that way?

Bill: I know, man.

Mike: Do they just say, “Well, I made my 50%.”

Bill: I can't wait.

Mike: I can sell.

Bill: It's going to be awesome.

Mike: When they sell, they all sell. Then the problem becomes, just pick one like, “Bill, Where are you a buyer of Nike? Where are you--? I'm going to buy that stock.

Bill: I don't know, I'll tell you what, I'll give you one that I did. I did Chipotle, and I think that I buy Chipotle 40% from here, as in 60% down, I think I'd be like, “Alright, I could do Chipotle.” No, I understand why people are like, “Alright, that's stupid. You don't get it.” But also look at what their stores have done since the Listeria problem. It actually is not as-- I understand they opened units, I get unit economics. I haven't done the most detailed models, so somebody might be beating me in that game, but like, “Man, you need a lot to go right, and you're selling burritos.”

Mike: You could take that same exact conversation and you could push it on 15 different securities and you would come up with the same answer. This probably gets into another fun conversation, which is the influence of passive. When you ask-- so you ask a guy, the real price-setting mechanism is the fundamental guy sitting here going, “I'm buying it at this price. I'm selling it at this price,” that's how the market is supposed to work. It was Professor Plum, Michael, I forget his last name. He really goes off on this. The guy's brilliant everybody should listen to him. It's really interesting when he talks about stuff. What he's saying is ETFs are never sell, they are never sell. That's partly why never sell is working. Why are they never sell? They can't sell because they've got inflows. They're allowed to sell. They don’t care what-- [crosstalk]

Bill: Yeah, works until the flow stop.

Mike: Correct. That's when I say is when the flow stop, who's the new price setter? Me. I'm the guy with liquidity ready to buy, so I'm setting the price. What’s my price? It's less.

Bill: Yeah, Mike's going to try to buy from you three times cash flow.

Mike: [laughs]

Bill: So, good luck. [laughs]

Mike: Yeah, I know.

Bill: You're not going to like the terms.

Mike: I hear the Mohnish Pabrai two times earnings seat is now open. So, I'm not hitting myself to be the--

Bill: That’s right. Yeah, he moved to compound town.

Mike: I understand that it's now available, so I put myself on the throne. Again, I'm underwriting 10% and I don't want multiple expansion to enter the equation. If you're doing that, and by the way, I'm a guy who's like, I'm underwriting 10% and I don't feel good about my ability to predict the ratio, more than three, but certainly more than five years out. So, if I'm not seeing that picture, is going to be attractive to me. So, now go take all of your companies and say, “Where's **[unintelligible [02:12:55]** buyer?” If I really understand it, I love the business, this is a classic example. Tell me when it's five years away from being 10 times earnings, basically then I'll say that that's my price. I'll probably be pretty reasonably conservative. I'll just straight-line what they're doing now. By the way, that's a lot lower.

In March, I was doing a little bit of this, but you had to do it some through writing puts because you couldn't really get there. The stocks didn't get quite that low. In March, it's like, Do you want to buy Visa? Do you want to buy UNP? Do you want to buy Berkshire? It's easy, 50 cents on the dollar. Boom. Just 50 cents on a panic, I've got cash, you don't, 50 cents on the dollar. That's my buy price. The answer is, I'm worried, people doing what they're doing, it feels great until you lose a lot of money and then it's like-- God, my mom, Bill, the 90s, my mom she was speculating on internet stocks, no idea what she owned, all of them went to zero. Now, I'm not saying that's where we are now. I'm just saying like, she thought, she could be a day trader, she thought she should make money. Now she won't touch stocks. [crosstalk]

Bill: I'll tell you where we are. My wife's friends are kicking the shit out of me and I'm having a pretty good year. I think I need to go back and really do a true accounting of why I am where I am. Some of it is increasing my beta exposure, but after taxes, I don't sell securities, again. It's not audited, whatever. I'm up roughly 300 basis points against the index. As somebody that came in owning banks and airlines, I'm pretty damn proud of the job that I did this year.

Mike: Take a victory lap.

Bill: It's funny, man, but I feel like a bigger fraud than I ever have. Which probably means that I understand how hard this game is and I never really appreciated it before. But, man, like my wife's friends are buying like, “Oh, Teladoc in March and--” I mean, good for them, but also, man, such first order thoughts like, “Oh, we should buy the e-commerce learning or the e-learning stock,” or whatever. My wife's friend in Central America bought that and it's getting ripped, and it's just all this stuff. I'm not sure how much of this is TAM being bigger versus pulling forward demand. If we're all trading on terminal value pulling forward, the demand shouldn't actually matter if rates are that low, but I think it's just safety. I think people like owning this shit right now at the foundation of what it is.

Bill: Yeah. Again, to me, it goes no farther than the people who are making the most money have the least idea what they're doing. That to me, that should scare people. We shouldn't look at that and go, “Oh, that's what should be happening.” We should look at that and say, “The people who are the most wasted are having the best time,” and that's not good. Your wife's friend in Central America shouldn't be killing it right now. That's not what should be happening. We're in a global pandemic, we've got unemployment at huge rate-- interest rates are zero, not because the world is great, it's because things are terrible. It shouldn't be happening, that people should be putting heavy, heavy risk on and getting rewarded for it, but they are. In my mind, you don't need any other argument than that. We're in full-on speculation mode.

Bill: Dude. You know what's crazy about how you just said that, and it's so true, is you said people shouldn't be putting heavy, heavy risk on. What people don't understand is, the higher the price goes, the longer your duration risk is. The more risk you're taking today that your thesis doesn't play out. But the problem is, the perception of the business, like the reason the price is high is because the business is perceived to be so stable, but that perception actually creates the risk that people aren't seeing. It's like you're going to sleep all the way into getting killed. Now, whether or not you want to go to QVC is totally different debate, like maybe Mike and I are morons, but we do see the world in a similar way.

Mike: We definitely are morons.

Bill: Yeah, that’s fair. That’s right.

Mike: [crosstalk] -about this as a whole different question.

Bill: That's right.

Mike: We're definitely idiots. You're right, the way, what you just said has been said, less eloquently than you put it, but it's been put as, the bull markets always sow the seeds of their eventual demise. That's what happens. It's people climbing the risk curve, that creates problems. It's excess that creates problems. By the way, it's not just problems in the markets, which it does create problems in the markets that people see. But it also creates weird incentives inside of businesses. If you're a business today, and you realize profitability does not matter. So, if I'm a CEO, and I'm like, I'm part of a transportation 2.0 business, that's like Nikola spin-off or whatever. For me, I don't have that profits, but I have to have is TAM and I have to have growth, that's what people are going to pay me for. It's the human condition is to go out and better yourself. It's an important condition, like capitalism works, but it's easy to take that to extremes. Again, that's why I mentioned the SPACs, that's what's happening is the SPAC is incentive is to go out and swing really, really big. That doesn't just permeate financial markets, that actually goes inside of companies. Companies are saying, no, mandate isn't to make money. The mandate is to sell. Sell, sell, sell, sell, sell.

Bill: Yeah, that’s right. And to grow like crazy.

Mike: Yeah, and grow like crazy. Let's go make some-- Again, it gets back to like, if that's the mandate inside of some companies, then how on earth are you going to get 40% ROICs on these businesses? Yes, you've seen historically, but you got CEOs us out there like, “No, you've got a new project, you think the TAM is big? Invest. All of those aren't going to work. I put a post, I was like, portfolio managers don't have common sense. To me, this is common fucking sense. It's not all going to work. Who has ever done anything that is always worked? Show me the one guy because I have not seen that person. So, I'm getting--[crosstalk]

Bill: No, it's true, man. And then [crosstalk] the other narrative that I hear that I think is-- there is truth to it, like every really bad idea is built on grains of truth. This narrative of, there's reflexivity in the share price, so the share price goes higher, so you get better people. So, the share price goes higher, and yada, yada, yada, Okay, I get it. That works. It doesn't work when your new crop of hires are getting stocks at 50 times sales, and then the share price starts to go down. And then they say, “Fuck this company, it's out of its best day. That can work the other way too.

Mike: It absolutely will.

Bill: When the higher the price goes, higher the probability that it stops working, by definition. Unless you think these things can compound infinity. I understand that some of them will, like I get it, the best companies of tomorrow will come out of the basket. But, ooh.

Mike: No, I'm going to go out on a limb here and I'm going to say that SaaS will be 200% of global GDP within 10 years.

Bill: There you go.

Mike: That's what I think.

Bill: I like it.

Mike: You heard it here first. **[unintelligible [02:19:14]** do it.

Bill: It should trade at a higher valuation, I get it.

Mike: Everybody [crosstalk] lot of companies they'll lose money to make story-- [crosstalk]

Bill: [laughs]

Mike: What you're saying is true. It's hard. I've seen it once, and it's brutal. When things get tough just, it affects an organization doesn't just affect the market. It affects the organization. I would say to the point about stock options, actually, in this case, it's really easy for a manager for a board, you have so many securities that are issued that you can pay out to your employees. If the strike, let's say, to use-- apparently I'm using Microsoft, I don't mean to, I don't own it, just maybe it's my sour grapes. But if you use Microsoft's example, stock's about 200, you issued stock to your employees at 200. Stock goes to 100 and stays there, like the board isn't going to let employees leave.

Bill: Yeah, you reprice them. Yeah, so the minority shareholders are screwed.

Mike: And you think about that, you're like, "Oh, okay, well, that's good, because I'm going to keep." But it dilutes you.

Bill: Yeah, that's right.

Mike: Remember my conversation about how I had to go raise $150 million at $2 a share. It's not a good thing, you shouldn't-- But that's what will happen, it's what should happen. Microsoft's fiduciary duties, keep the business going for its owners. It's not going to let us **[unintelligible [02:20:19]** we believe in it shouldn't, but you just have to know, like, yeah, it works really well on the way up, and it hurts really badly on the way down. I think the thing that I just can't get past, they can't all be winners.

They just can't. It's not possible. There will be pain. And then the question is, is it going to be that you'll make enough returns than your winners from here to offset the pain? I don't know. That's the bulk of me on this podcast is me walking you through all the things I don't know. And that's why-- [crosstalk] [laughs] I just don't.

Bill: I appreciate you doing it. I think we're going to wrap this one up, but I hope you come back. I'm really grateful for you for being the first guest, and I'm grateful to you.

Mike: No, man. Boy, I hope we started this podcast off right.

Bill: I hope. Everybody once again remembers it's not investment advice. This is Brewster's Billions, where we turn billions into thousands.

Mike: [laughs] If you want to know what not to buy, please go follow me on Twitter. You can see all of my portfolio every month. You can get some good short candidates. It's going to be a very good shortlist for you. I have a lot of fun with you as always. I hope this has been entertaining. I hope we started your podcast off on a good note. [crosstalk]

Bill: Dude. I hope, I recorded it. [laughs] I'm almost certain I did.

Mike: Can you imagine?

Bill: No. I did.

Mike: All right. No problem, we'll just do it again on Monday. Let's just do it again on Monday.

Bill: We saw the countdown, so I think we'll be good.

Mike: Oh, that's good.

Bill: All right, my man. Take care of yourself. Thank you for joining me.

Mike: Yeah. Thanks, man. Enjoyed it.

[outro]