



THE  
MANUAL  
OF  
IDEAS

## Value-oriented Equity Investment Ideas for Sophisticated Investors

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*"If our efforts can further the goals of our members by giving them a discernible edge over other market participants, we have succeeded."*

TM

### Investing In The Tradition of Graham, Buffett, Klarman

Year VII, Volume IX  
September 2014

When asked how he became so successful, Buffett answered:  
"We read hundreds and hundreds of annual reports every year."

#### Top Ideas In This Report

<b>Harbinger Group</b> (NYSE: HRG) .....	118
<b>Regional Management</b> (NYSE: RM) .....	154
<b>Western Union</b> (NYSE: WU) .....	170

#### Also Inside

<b>Editorial Commentary</b> .....	4
<b>Interview with John Burbank</b> .....	7
<b>Interview with Arnie Van Den Berg</b> .....	12
<b>70+ Superinvestor Portfolios</b> .....	22
<b>20 Superinvestor Holdings</b> .....	94
<b>Screening Superinvestor Stocks</b> ....	174
<b>10 Essential Value Screens</b> .....	184

#### About The Manual of Ideas

Our goal is to bring you investment ideas that are compelling on the basis of value versus price. In our quest for value, we analyze the top holdings of top fund managers. We also use a proprietary methodology to identify stocks that are not widely followed by institutional investors.

Our research team has extensive experience in industry and security analysis, equity valuation, and investment management. We bring a "buy side" mindset to the idea generation process, cutting across industries and market capitalization ranges in our search for compelling equity investment opportunities.



Replay at [ValueConferences.com](http://ValueConferences.com)

# THE SUPER- INVESTOR ISSUE

- ▶ Screening 800+ Holdings of 70+ Superinvestors
- ▶ MOI Signal Rank and Top Superinvestor Holdings
- ▶ 20 Companies Profiled by The Manual of Ideas Research Team
- ▶ Proprietary Selection of Top Three Candidates for Investment
- ▶ Exclusive Interviews with Arnie Van Den Berg and John Burbank
  - ▶ 10 Essential Screens for Value Investors

Superinvestor holdings include...  
 Apache (APA), Armstrong... (AK),  
 Carter's (CRI), Chan...  
 Harbinger Group (HRG),  
 Life Time...  
 Newfield Explora...  
 PetSmart (PETM...  
 Spirit Airlin...

### New Exclusive in the MOI

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- ▶ Christian Ryther Re...
- ▶ Omar Musa Shares Case Study...
- ▶ Eric DeLamarter on the Source of Investment Edge

Inside:

**Exclusive Interview:**  
**Arnold Van Den Berg,**  
**Chairman,**  
**Century Management**

*With compliments of*  
*The Manual of Ideas*

Watch a video recording of this interview in The Manual of Ideas Members Area at [www.manualofideas.com/protected](http://www.manualofideas.com/protected)



*“I started noticing that most of these guys who had done a good job were talking about Benjamin Graham. I started reading everything I could get my hands on about Benjamin Graham.”*

## Exclusive Interview with Arnold Van Den Berg

We had the pleasure of meeting with Arnie Van Den Berg, chairman and chief executive officer of Century Management, based in Austin, for a conversation about his investment approach and path as an investor. Arnie argues persuasively for a simple, disciplined approach to investing. His remarkable story inspires and challenges us to become better in every facet of life.

Arnold Van Den Berg founded Century Management in 1974. He has no formal college education. It is through self-study, dedication, and more than forty-five years of industry experience that Arnie has gained his market knowledge. Prior to starting Century Management, he worked as a financial advisor/consultant for Capital Securities and John Hancock Insurance.

*(The following is an edited transcript of a video interview and may contain errors. The transcript has been lightly condensed for clarity and readability.)*

**Oliver Mihaljevic, The Manual of Ideas:** There’s so much to learn from you about investing — how you turned \$250,000 into a \$2 billion business. There’s so much to learn on life — how you survived the Holocaust, kept on believing, kept on living. How did you become interested in value investing?

**Arnold Van Den Berg:** I was working for a financial firm, and they were selling life insurance and mutual funds. As soon as I heard about mutual funds and started learning about them — the market had been going up, this was 1968 — I got excited about the mutual funds. I was losing interest in the insurance business because I didn’t believe in the products they had, and I was looking for another way out. I really thought that I had found my dream, something I wanted to do the rest of my life. I didn’t know too many people with money, but I had some high school friends and people I knew from my insurance business.

I got them started in mutual funds, and no sooner than I got started — it wasn’t more than six to nine months — and the market started on a sickening slide in 1969. It went down and down and down. Finally, it hit a bottom in June 1970. It rallied up into 1972, and then it had a major slide down from 1972-’74. This was a period of six years where it was just like torture — drip, drip, drip every day. I saw these mutual funds just fall apart, and it really upset me because I had all my friends in it, and they didn’t have much money to begin with. I didn’t have much money, so it was really a soul-searching time.

I started thinking, “How could it happen?” I used to listen to these money managers, they were so intelligent and so sharp. How could this happen? The more I questioned, the more I learned, the more I was thinking about it, I started studying the market, and I came across surveys of what the different funds did, and who did well and who didn’t do well. I put to side the funds – this fund did well and this fund did well and this fund did well, this one didn’t do well. Then I started seeing a pattern. They were all people who believed in Benjamin Graham, they were value investors. While their portfolios went down, they didn’t do anything like the majority of them (some of those mutual funds were down 50% and 75%). Some of the funds went out of business. One fund was up 100%, the next year it closed. It was just a disaster. The average investor suffered a great deal. The market went down 48%, the average stock went down 75%. It wasn’t totally the mutual fund’s fault, it was just the environment.

I started noticing that most of these guys who had done a good job were talking about Benjamin Graham. I started reading everything I could get my hands on

about Benjamin Graham. Buffett wasn't that well-known at the time. He had already been successful, he was leaving the business. The more I read about Benjamin Graham, the more it made sense to me. Coming out of a Jewish home, you learn to buy things at a discount, so that made a lot of sense. I remember I would go and buy a sweater or a shirt and my mom would ask me, "Arnold, did you get it wholesale?" I said, "No, Mom, I bought it —" She'd say, "Oh no, you're thinking like a goy. You've got to buy it wholesale."

When I started hearing about Benjamin Graham, that you've got to buy it at a discount from present value or intrinsic value — that clicked with me, "This makes a lot of common sense." I didn't have an education, but I did have some basic common sense. I grew up in a home where people talked about business all the time, so I thought, "If I can buy it cheap enough, it's going to survive the market." I studied everything I could get my hands on and then, coincidentally, I had a friend of mine who lived in my apartment. He used to like to study the market, so we'd get together and we used to call each other 'Tiger.' He says, "Tiger, I met a guy that you've got to meet. This guy is just phenomenally successful in the market. He's the research director of a brokerage firm, and I told him about you." He said, "I've only met one person that's more fanatic about studying stocks than you and that's him, so I told him about you and he said, 'Well, I'd like to meet you.'" He arranged a meeting with us.

He was an ardent Benjamin Graham fan; and he sent me on the course. He just validated what I already thought. He said, "You ought to study this and study this." As we got to talking – we had lunch – he gave me a couple of ideas for stocks and so I'd study the stocks. Then I'd call him up, and I'd be digging into the company and asking him questions. He said to me one day after I was drilling him with questions, he said, "Arnold, my god, you really dig into these companies, don't you?" I said, "Well, I want to learn." He says, "I have a number of other ideas. If you'd like to run them down and do the legwork on them, I'd be happy to work with you." I thought, "Geez, that's great." Here was a guy who was knowledgeable, experienced, and successful, and he sort of became a mentor to me. We started doing research together. He was already very successful. I was driving an old beat-up car and he drove a brand new Mercedes and had his own plane.

One day, I'm standing out in front of an apartment building where I just moved in and I saw him drive by. I said, "Hey, Mark." He was driving a convertible. He looks over and says, "What are you doing here?" I said, "I'm living here." He says, "I'm just moving in." I said, "Oh man, that's great," so I'd go over there every night. We'd meet for dinner, we'd talk about stocks. I finally decided I'm not going to do mutual funds, I'm going to start my own company. I had this idea to start my own company and I had no money. That was the only problem.

One day I was sitting down with a friend of mine and he had also been a client of mine. I told him about this dream I had about starting my own firm and he said, "Arnie, that's great. I think you could be good at it." I said, "Oh, thanks, Bob." And he says, "Where's your office going to be?" I said, "I don't have an office. I'm working out of my home. I lived in a studio apartment. He said, "Arnie, you can't be an investment counselor out of your studio apartment. Where are you going to bring the clients?" I said, "We could meet for lunch. I don't know. I mean I don't have any place to go." He says, "You've got to get an office." I said, "I would love to get an office. I just don't have the money." He says, "How much would it cost to lease a place and furnish an office?" I said,

*"Coming out of a Jewish home, you learn to buy things at a discount, so that made a lot of sense. I remember I would go and buy a sweater or a shirt and my mom would ask me, 'Arnold, did you get it wholesale?' I said, 'No, Mom, I bought it —' She'd say, 'Oh no, you're thinking like a goy. You've got to buy it wholesale.'"*

“I haven’t thought about it because I don’t have any money. I can barely pay my own rent.” He said, “Oh no, you’ve got to have an office.” I said, “Bob, I don’t have any money. You don’t understand.” He says, “No, I do understand. I’ll tell you what, let’s go back to my office.” I said, “What for?” He said, “I want you to make a budget, I want you to tell me how much it’s going to cost to start an office and I’m going to lend you the money.” I was just amazed. Just like that. I said, “You really mean that?” He says, “Oh yeah, Arnie, it’s my pleasure. C’mon, let’s go the office.” I went to the office, he pulled out a pad – let’s see, chairs, furniture, rent. I tried to keep it really low because I didn’t want him to think I was taking advantage of him. Finally, we came up with about \$2,500 – \$500 for rent. Furniture — I bought a desk out of a guy’s garage. He was a CPA, had an office in the garage. Nice desk for \$125, a couple of bookcases for \$30 apiece. The \$2,500 in today’s money would be about \$15,000-\$17,000.

*“Then I went and looked for a place to rent... It was dilapidated, cost 41 cents a square foot, so this is like getting a Cadillac for a Chevrolet price. We were just really excited.”*

Then I went and looked for a place to rent and I had a friend of mine that was an accountant and we were going to share an office. We both went and looked at the rent. At that time, Century City was just decimated. There was a big real estate bust there, and whole buildings were empty. There were buildings, beautiful, brand new buildings that were empty. I knock on the door of the leasing agent and I still remember his name. His name was Curtis, he was just a great guy. I told him, “Look, I want to start this investment company, but I don’t have much money. Do you have some office that doesn’t have to be the nicest place in the building, just a little office I’d like to rent?” He says, “Arnie, I’ve got just the place. This was the executive president of this big company. Beautiful office with walnut panels and all that.” I said, “Curtis, I couldn’t afford it.” He says, “Wait, let me show it to you and then you decide.” Anyway, the rent was \$500, which would be about \$5,000 a month or something like that today, so it was a lot of money. My buddy was going to pay \$280 because he got the biggest office, I was paying \$220. Then he said to me, “I’m going to give it to you guys at a price you won’t believe,” so it was 41 cents a square foot. I was in another building when I was in the insurance business. It was dilapidated, cost 41 cents a square foot, so this is like getting a Cadillac for a Chevrolet price. We were just really excited.

It took a lot longer to get the business going than I thought and every month I’d be behind on my rent. I’d knock on Curtis’ door and he says, “What’s up, Arnie?” I’d say, “I only got about \$200 for the rent this month. Can you spot me until next month?” He said, “Sure, don’t worry about it.” Every month I had to go to him and tell him, but we always paid him and he was always cool about it. I stayed in that building for about four or five years and that’s why I named the company Century. It was Century City in California, so I named it Century Management. That’s basically how I got started. It was just a dream. That’s all I had going was a dream, but it was powerful.

**MOI:** Well, the rest is history, as they say. As I was listening to you, I certainly can relate, having to talked to a lot of investors who had that fire in the belly ...

**Van Den Berg:** I still have the fire in my belly.

**MOI:** I’m glad to hear that.

**Van Den Berg:** You don’t lose that when you’re a value investor. I was giving a talk to a group of doctors and they asked me — this was when I was 65, I’m 74 now — “What are you going to do when you retire?” I said, “Why would I retire?” He said, “Most people retire.” I said, “No, no, you don’t understand. I

go into my office and I pick up dollar bills for 50 cents. I'd rather be doing that than chasing a little white ball around the golf course in the hot sun. What could be more fun than picking up dollar bills for 50 cents?" Once you become a value investor, it's like an addiction.

**MOI:** Absolutely. You alluded earlier to your education and self study. You have no formal education beyond high school, and it's interesting when we look at how the world has perhaps changed. When we see value investors who want to go into the business these days, there is this notion that you've got to go to the right school, that you've got to have an MBA, CFA, and so on. Give us a sense of what the keys were for you. What was critical in your self study?

**Van Den Berg:** I have a different view on education because I never had a formal education, and even in high school I wasn't a very good student. When I was going to high school, my main focus was on gymnastics — I was a rope climber. That was the main focus because I had this obsession. I was very weak and skinny. I lived in a pretty tough neighborhood — people getting into fights — so I was self-conscious about my physical strength. The weaker you are, the more they pick on you. Nobody wants to pick on the guy that's bad; they always want to pick on the weak kid. That really bothered me, and so my brother was going out for rope climbing, and he invited me to the gym one time. I saw these guys with these big physiques... I thought, "this is what I want to do." That became an obsession of mine, and that's all I focused on.

It took me years to build up my strength because I'd work out two years and some guy would walk in off the gym and he'd beat me up the rope. I would just almost go home and cry, I was so discouraged. But something in there told me to keep going because I was getting stronger. I had an experience that changed my life, and this relates to education. I didn't realize what that experience meant to me until later on when I went to a psychiatrist and he explained what [had] happened to me mentally.

I wasn't making any progress, so the coach said, "Arnie, there's a new style in rope climbing, and it's completely different than the way we're climbing. It's a technique, it's an art form, and if you master that, you don't need to be as strong, because it's part technique." I thought, "This is great. Where do I learn that?" He said, "I don't know it. It's brand new, but there's a young guy at Venice High School, and he has mastered it. He's the city champion. Go down and watch him." I took the bus two or three hours to get there. I got there an hour early and waited for him. The meet starts and he doesn't show up. I'm just really depressed. I went all this time and didn't see him. All of a sudden, he comes running in, gets on the rope, shoots up that rope, and I'm just in awe. I was so worried that I would forget how he did it that I kept playing it in my mind. Then I'd wake up in the middle of the night because I was worried that I wouldn't remember it in the morning. I'd get up in front of the mirror every night and I would practice the technique, the way you move and so on and so forth.

Within six months I started making tremendous progress. One day, I woke up, I bounced out of bed. I felt so strong. I said, "I am going to break my record today. I just know it." I called the coach. I went up that rope, it was like a dream. It was effortless. I broke my time way down. The coach had to look at his watch, he couldn't believe. I had a feeling that it was a breakthrough, a mental breakthrough. I said to my coach, "I'm going to be the next Northern League champion." He said to me, "Arnie, you've made a lot of progress, but there's a lot of guys ahead of you." I was a little embarrassed, but I walked away and

*"One day, I woke up, I bounced out of bed. I felt so strong. I said, "I am going to break my record today. I just know it." I called the coach. I went up that rope, it was like a dream. It was effortless... I had a feeling that it was a breakthrough, a mental breakthrough."*

*“[Conrad Hilton] started with nothing. He went into the real estate business; he lost all his money... Then he saw a picture of the Waldorf Astoria, which was just one of the most amazing hotels. He took the picture, cut it out, put it under the glass on his desk and he wrote upon it ‘The Greatest of Them All.’ Fifteen years later, Conrad Hilton bought the Waldorf Astoria.”*

said, “No, I know I’m going to be it. That’s it.” I set the school record that year. I won the league — tied for first — and then the next year, every year I won the league after that. It was just such a turnaround that nobody could believe it. I even placed in the national AAU, 9th in the nation, and I was in high school, but this was climbing against seniors in college. That was really the turning point.

Later on, I went through a divorce, and I had a lot of problems, and getting my business going — depressed. I went to a psychiatrist and I told him this story. He said, “This can be explained from a psychiatric standpoint. You got that image in your mind and you played that over into your subconscious. Once it gets into your subconscious, it programs you into that kind of person.” He said, “That’s what we teach in sports psychology. We have people visualize what they’re going to do, and their subconscious helps them.” I never knew about the subconscious mind. The minute he told me that, I knew he hit a truth. He said, “If you will do the same thing with your business, the same thing’s going to happen.” I went home that night, I was on fire. I cleaned out my apartment, threw out everything, put my desk in the middle of the room. I said, “I am going to start my business and I am not going to stop until it’s there. No matter what happens, total commitment.”

I started reading everything about the subconscious mind, and I programmed myself. I used to hypnotize myself every day for 20 minutes. I learned hypnosis. I used it on my son for his sports. Tremendous breakthrough. The thing I try to teach young people is, no matter what it is, if you put it in your mind, and you visualize, and you see yourself successful, it will make it happen.

If I can take a moment to give you the best example I’ve ever read — Hilton Hotels. This is an incredible story. This guy [Conrad Hilton] started with nothing. He used to swim in irrigation ditches when he was a poor kid in New Mexico. He went into the real estate business; he lost all his money one time because he was overextended. He was in hock, he borrowed money from a bailman to get a meal. Then he saw a picture of the Waldorf Astoria, which was just one of the most amazing hotels. He took the picture, cut it out, put it under the glass on his desk and he wrote upon it ‘The Greatest of Them All.’ Fifteen years later, Conrad Hilton bought the Waldorf Astoria. His sons were interviewing him and saying, “Dad, how could you be so successful? How could you have done this? It’s just amazing.” He said, “My dad told me to work hard and my mother told me to pray hard, and it’s the combination.” They said, “We know a lot of people that work hard and pray hard. That doesn’t happen.” He said he couldn’t give them an answer. He said, “I don’t really know.” He said six months later he was flying to the Waldorf Astoria’s 25th anniversary of the purchase of the hotel. He said he was sitting there — it still gives me chills — he was more in awe than anybody there. He knew that he was living a dream. He says, “This is what had awed me. I realized that I had the answer for my sons. It all starts with a dream.” And then he talks about how the subconscious mind guided him, and the rest is, like you say, history.

When you read these kinds of stories — and I have a whole drawer full of them — I really inculcated my mind. I saw myself as a successful money manager. It took many years — every month I’d wonder where the next check was coming from. I’m going to tell you one more interesting thing. I had the faith after a while that it was going to happen. One day, my wife was doing the budget; she was doing the bills and she got tears in her eyes. I said, “What’s the matter?” She said, “Arnie, I see how hard you’re working day and night, and every month

we get more behind in the bills.” I said, “I know that.” She said, “I’d like to go to work, help you out and get a job, help you pay the bills.” I said, “No, I’ve already been to a shrink, and I know if you go to work and the kids don’t have somebody to take care of them, you’re going to end up like me at a shrink’s office, or the kids will.” I said, “We’re going to keep it on. Give me one of your checks.” She said, “What for?” I said, “Give me a check.” I wrote out a check to my wife Eileen: “\$250,000 for something you may like,” and I said, “don’t cash it this week, but one of these days you’re going to be able to cash it.” About a year or two years ago, she needed some money and I said, “You mean to tell me you spent all that money I gave you?” She says, “I still have that check.” I said, “It doesn’t do you any good because I changed bank accounts, but let me have it.” I have it framed now. If you put it in your mind — that \$250,000 at that time, I was \$20,000 in debt and I was grossing \$8,000 a year — there was no basis, but I had that belief. This is the key to everything.

*“When I became a champion rope climber, everybody thought I was a natural. I looked like a natural, but that wasn’t a natural ability. That was created. I don’t have any talent for money management, that is created. You create it within you.”*

If you’ve got a young guy that wants to start his business, I don’t care about his education. He’s got to believe that he’s going to do it, and if he believes it, it’s going to happen. There was recently a book written called *The Biology of Belief*. The guy [Bruce Lipton] proved that your belief can change your genes and your DNA. That’s how powerful belief is. It’s the substance of all religion, and if you look at anything in my family, my folks getting through a concentration camp, my mom says it was her faith that allowed her to survive. Belief is important. They don’t teach that in school. They teach that you’ve got to have an MBA, you’ve got to do all this stuff. No. William James wrote, “When you tap into your subconscious mind, it has not only the wisdom of your whole life experience, but all the wisdom that was ever created. By committing to that process, you have the ability to tap into that resource.” It’s all through energy, and so by having a clear picture of what you want to do in life and committing yourself to it, you can’t miss. Even if you don’t have the talent, the mind creates the talent for you.

When I became a champion rope climber, everybody thought I was a natural. I looked like a natural, but that wasn’t a natural ability. That was created. I don’t have any talent for money management, that is created. You create it within you. I don’t look at people’s resume — whether they went to the best college or not. That doesn’t really tell you. It’s [about], does the person have the conviction that they’re going to stick through thick and thin, that they will stick with it no matter what happens and never give up? Period. You got that, you’re on.

**MOI:** When you reflect back, it sounds like there was a point in time when you were able to gain that conviction. Does that evolve over time? Can people improve on it? Give us a sense of that dynamic.

**Van Den Berg:** You have to keep repeating it — affirmations: every day and every way I’m getting better and better. I have forty years of little articles, quotes, and excerpts I’ve kept in a file; it’s about 50-60 pages. What I tried to do was take a concept like Conrad Hilton’s. He wrote it in his book, *Be My Guest*, but I got it in four pages, so somebody could get the idea without having to read the whole book. I’ve got the best that’s ever been said about how to use the subconscious mind.

You can ask Scott [Van Den Berg] what we did with the subconscious mind. He was a champion shot putter. He fell out of the ring, and he had a sprained ankle. The coach and the doctor said, “You’re out for the season.” We had an important championship nine days later. I said, “Isn’t there something that can

be done?” The doctor said, “He can’t step on the tendon because it’s going to ruin it, so I’ve got to put him in a cast.” I said, “Okay, if you put him in a cast, and he can still shot put.” He looked at me like I was nuts, and he said, “He’s going to have a lot of pain. When you have a sprained ankle, you push down on it.” I said, “I’m going to anesthetize him under hypnosis. He ain’t going to feel anything.” He goes, “Look, I’ll put him in a cast and you handle him from there; I’m not into that.” Well, we did. We put him in a cast, we went to the hotel. The next day, before the championship meet, I put him under hypnosis. I kept him under hypnosis the whole meet, and he went out and won the meet. He threw six inches from the best he’d ever thrown — under hypnosis with a taped cast and a sprained ankle. That is the power of the mind.

*“The world has changed, but people haven’t changed, and the mind hasn’t changed. I believe if there’s a young guy that wants to start a business, if he’s willing to pay the price, if he’s willing to make the sacrifice, if he’s willing to do without some of the frills people think are necessary, he is going to make it. You can’t help but get paid [if you do good].”*

When you see and experience things like that, you become such a strong believer. It’s like a muscle. You don’t have it at first, you’ve got to practice it, and you’ve got to believe it. Then when you start experiencing it... I can tell you stories. Just an example to give you: I had a friend call me one day, and he said, “Arnie, my accountant wants to meet you as a future client.” This was when I first got started. I said, “Oh great. Who is he?” He said, “He was an accountant. He’s the auditor of my firm, and he heard me talking to you. I was complimenting you on your stocks, and he heard me as he walked by, and he said, ‘Is that your broker?’” He says, “No, I have a friend of mine that’s an investment advisor.” He says, “I’m looking for one, will you introduce me?”

Long story short, I meet this man. He said, “I have a big CPA firm. I have a lot of clients and I’m looking for an investment counselor. I want to give you \$50,000 for three years, and if you do a good job, then I’ll recommend you to the clients.” Here out of the clear blue sky was a man that I would have never met on my own. I didn’t even know any accountants, and here I meet this guy. I do a good job for him. Three years later, he starts introducing me to people from the country club, and all of a sudden, I’ve got an entrée to people I could have never met based on my social status, my economics, my education, or anything else. They’re handing me their money because he believed in me. He believed in the discipline, he watched me for three years.

You say to yourself, “That’s a coincidence.” Well, when you have many coincidences like this — I can give you stories like that, even the way I met my wife, same thing — when you start to see these coincidences happen, it builds faith, and that’s what moves mountains.

**MOI:** Now when you reflect back, some would say certainly the world has changed and the investment business has changed, the importance of institutions perhaps, the disintermediation, various things. Give us a sense of how you think about that element and how that could affect, let’s say, the more practical things. Once you have that belief and you have the faith, but certainly the world has changed a bit, so perhaps you can reflect on how you see that element of it.

**Van Den Berg:** The world has changed, but people haven’t changed, and the mind hasn’t changed. I believe if there’s a young guy that wants to start a business, if he’s willing to pay the price, if he’s willing to make the sacrifice, if he’s willing to do without some of the frills people think are necessary, he is going to make it. You can’t help but get paid [if you do good]. There’s no such thing in the universe. If you serve people and you do a good job, and you love them and you take care of them like they are your family, there is no way you’re not going to make it. I don’t care who it is.

You need a certain level of intelligence, but you don't need to be very bright. I don't consider myself very bright. I never did well in school. I never did well on intelligence tests. My mother took me to one of the best child psychologists after the war because I had a lot of problems, and he felt that I was permanently damaged in the brain because of malnutrition. I almost died from malnutrition. I always had this image of myself that I wasn't very smart, and the way I did in school proved that I wasn't. But: Once I realized that if you dedicate yourself and you commit yourself, you can learn anything. I will admit this: whatever I learn takes me three times as long as anybody else. But if I spend three times as much time as anybody else, then I'm equal. I can learn it, just give me more time, more books.

**MOI:** Let's talk about also intellectual curiosity. A lot of folks today want prescriptions for how to invest, and certainly the clients demand categories, everything needs to be spelled out. Give us a sense of that elusive concept of flexibility in investing and in life.

**Van Den Berg:** If you took Benjamin Graham's basic rules and just modernized them because things have changed a little bit — it wouldn't take much change — they could do very well. Graham felt that with his simple rules, you might not do extraordinary, but you could do very well, and he proved it many times.

I'll tell you what really helped me. One day we were talking about a stock, and there was an acquisition. The company paid a lot more for that stock than I thought it was worth because I had multiples I'd developed through the Graham philosophy. I thought, "I wonder what these guys see in this company, because based on the Graham philosophy, they paid almost 50% more than it's worth." I started studying acquisitions. If these guys in the business — they spent their whole life in it — if I was going to buy another money management firm, you know I would know what to pay for it because I'd been in it for forty years and I'm certainly not going to overpay for it. If I'm willing to pay that much, as a businessman, I must be able to pay that much and still make money. That got me to thinking: I'm going to follow every acquisition. Whenever I read about an acquisition, I cut out the article in the newspaper. I'd get the Value Line or the Standard & Poor's sheet, throw it into a shoebox, and on the weekend I'd come and run every ratio — price to book, price to sales (now we use enterprise value to sales), price to EBITDA and all that... I categorized all these acquisitions, and then after a while I had so many, I said, "This was the acquisition price for a retailer, and this is the acquisition price for a manufacturer." Then I would compare it to the Graham philosophy. I added that onto the Graham philosophy... I would see over many cycles how low the stock would go, but this is how high it can go, because the ultimate price of a stock is what sophisticated buyers are willing to pay for it. That usually is about 20% more than what the stock is trading for in the market.

Now I had an overview, an acquisition file; I called it the Private Market Value Template. I would take every stock and say, "this is what they paid for it." I didn't figure this out. The other guys did — the people who were buying these companies. I started to realize that the highest the stock would go in the market is about 80% of what a sophisticated buyer would pay, because if you can control the company, you're willing to pay a little more because you can move the levers around. That became my sell point. Now I had a sell point that was about as rich as it can get, 80% of private market value. Then I reduced it, saying, "How much of a discount do I want to buy this company?" I started

*"Whenever I read about an acquisition, I cut out the article in the newspaper. I'd get the Value Line or the Standard & Poor's sheet, throw it into a shoebox, and on the weekend I'd come and run every ratio..."*

*“I worked out a ratio: If I have a company that’s worth \$30 — \$36 private market value — \$30 is the sell point. I look down and see how cheap it can get. It can get to about \$12. If I buy it at \$15, I’ve got \$3 on the downside and \$15 on the upside, so I’ve got a 5:1 ratio. That turned out to be a good ratio.”*

grouping the companies together and realized that big cap stocks, big companies, usually the cheapest you’re going to get is about a 50% discount from private market value, the medium companies about 60-65%, and the small caps about 75%. Then when I’d get a small cap company, I’d say, “Here’s the price of the stock. I’m going to buy it. My worst case is going to be 25% of that private market value.” Then I say, “I’m willing to pay a little bit more because I don’t want to miss it.” You run a risk of missing it.

I worked out a ratio: If I have a company that’s worth \$30 — \$36 private market value — \$30 is the sell point. I look down and see how cheap it can get. It can get to about \$12. If I buy it at \$15, I’ve got \$3 on the downside and \$15 on the upside, so I’ve got a 5:1 ratio. That turned out to be a good ratio. Look what happens if you pay \$17. You’ve got \$5 on the downside. You’ve reduced your reward if you pay \$17; you only have \$13 on the upside. You divide the \$13 by the \$5 and you’ve only got [about] 2.5:1. By paying up a little bit, you take the reward-to-risk from a 5:1 to a 2.5:1. I learned to be very disciplined. I had the private market value, I had my worst case, and then I’d buy at no more than 20% above the worst case, and that gives me 5:1. If I have a midcap, I might go 4:1 and if I have a really great Buffett franchise company, then I would only take a 3:1... It just came about through common sense, watching things in the market. Any investor can learn this. I do not know more than 4th grade math, but you don’t need more than 4th grade math to do these calculations. There isn’t anything when you do a financial statement that would take a lot of math. Benjamin Graham even said, “Whenever I see formulas that have a lot of sophisticated math in [them], I distrust [them].” That’s true.

Think about it: An immigrant comes over, starts a business and makes a billion dollars. Does he know calculus? No. He can barely sign his name, but they make money. You know why? Because they learn the basic rules of thumb. I have a hundred different rules of thumb. Scott always tells me, “Dad, one of these days you’ve got to publish a book called *Rules of Thumb*.” You don’t need all this high math, you don’t need all this education. You just need business sense.

I’ll give you something that my mom taught me. As I was graduating, I was popular and successful in my career in gymnastics, but I did very badly in school. I was getting worried about what I was going to do with my life. Everybody was going on to college, and I didn’t want to go to college. I figured it’s not for me, so my mom says, “Arnold, what’s the matter? You look a little depressed.” I said, “I’m trying to figure out what I want to do.” She says, “Well, what do you want to do?” I said, “I want to make some money.” I didn’t have any money, I was working at a gas station. She says, “Well, why don’t you go into business?” I said, “Business?” She says, “Yes, there’s only two kinds of people in the world. There’s the Yekke, and there’s the businessman.” I said, “What’s a Yekke?” She said, “A Yekke is a guy like your dad. Ask him any question about history, music, mathematics, religion, philosophy, he can answer. Can he make any money? Nothing.” She says, “Now you take the businessman. Take me — do I know about religion, philosophy, music, mathematics? No. Do I care? No. Do I know how to make money? Yes.” That was my career counseling. “You want to make money, you go into business.” I said, “That sounds good.” Then I thought, “What kind of business?” She says, “What difference does it make? Business is you buy something, you sell it, and you make a profit.” She says, “I only need three people — the person I’m going to buy it from, the person I’m going to sell it to, and then me in the middle who

needs to make some money.” That got me thinking about business, but it wasn’t until I saw the mutual fund business that I really got hooked. I was looking all these years for something to go into.

You know how I got into the insurance business? I read this ad, “Start Your Own Business.” I thought, “That’s for me,” so I went down and interviewed, and the guy gives me this big pitch about how great the insurance business is. You build your business (and renewals). I thought, “That’s great,” but I had a job. I was managing a print shop. I said, “I’d like to try this at night because I’m not sure I can do this. I have a pretty good job.” The guy says, “You’re going to work your full-time job and work at night, too?” I said, “Yeah, because I’d like to work more, and I can learn the business, and if I like it, I can switch.” He says, “You’re going to be great.” So he set me up. I went knocking on doors, and after about three months, I got the hang of it, and I was doing better than I was doing at the print shop, so I quit the print shop. Then I started selling, and as I started analyzing the insurance business, I thought, “This is not good for the people — the kind of policies they want you to sell. They make them a lot of money, but it’s not the best for the people.” So I started selling term insurance, but in term insurance you don’t make any money. That was another struggle I had. I was selling term insurance, not making any money... When I got into mutual funds, I said, “Now I know I’m going to give up the insurance business. I’m going to go into this,” and then the market collapsed, and here I am. It was a long, hard journey, but the point is you could do it.

**MOI:** It’s very inspirational. As I’m listening to you, I’m smiling. Somebody with your mindset, with your outlook on life and all that’s come before, what do you still find challenging in investing or business?

**Van Den Berg:** First of all, I would have never thought, if you’d asked me in high school what I loved to do, I loved to read and study. I’d study all the time, anywhere I’d go. I also have developed a discipline in yoga. I’m a yogi, and I do yoga almost every day. My main happiness comes from getting better no matter what it is, whether it’s in yoga, whether it is in anything I’m studying, whether it is in our business. I love working with my people. We have 42 great employees, they’re just really committed people.

We have some wonderful clients. I can’t even begin to tell you the clients we’ve got. I have clients going back 35 years. I have clients that are second and almost third generations now, so I’ve developed a lot of friendships with people who really believed in me. Last year I went to a seminar in California and I met one of my first clients. He’s been with us for 38 years and I hadn’t seen him for 30 years because I’m in Texas, but we talk on the phone, and he is a client of ours. I hadn’t literally seen him for 30 years. It was just a pleasure to see our old clientele. I used to meet with every client personally, but as the business grows, Scott [Van Den Berg] has done a wonderful job of developing a whole team of people who meet with the clients on a regular basis. They sit down with them, they review their portfolio, they teach them the principles.

It’s very exciting to work. Sometimes I walk down the hall of the company and I look around and say, “I feel like Conrad Hilton. I’m living a dream.” This is what I’ve dreamed about. It doesn’t get any better than this. It’s nirvana.

**MOI:** Arnie, thank you very much for sharing your time and insights.

*“My main happiness comes from getting better no matter what it is, whether it’s in yoga, whether it is in anything I’m studying, whether it is in our business.”*

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MKT price: \$ 36

IV: \$ 30 → MoS: 50%

entry price: \$ 15

$$\left[ \begin{array}{l} \text{upside} = \frac{30-15}{15} = \frac{5}{15} \times 20 = \frac{100}{30} \\ \text{downside} = \frac{15}{3} = \frac{5}{1} \times 20 = \frac{100}{20} \end{array} \right.$$

Worst case: \$ 3

→ Worst case valuation è nuova valutazione super conservative. Non è quindi semplice aumento del MoS.

↓ Given the woman situation (see top right corner),

Buy stock only at the worst case. If nothing then keep cash & bond until price gets to that level.

If price dropped \$ 1 to \$ 14 and \$ 2, then upside =  $30 - 14 = \$ 16$ . Worst case is \$ 2.

$$\frac{\text{upside}}{\text{downside}} = \frac{16}{2} = \frac{8}{1}$$

Rischio è di non trovare azioni che vendano a quel prezzo, però almeno abbiamo procedimento che considera età e particolare situazione economica. PERÒ, quelle che compri hanno rendimenti notevolmente superiori rispetto ad altri.

### Valuation process used

They look at a company 20 or 30 years back. Different companies need different ratios.

In 20-30 years at least 2 or 3 depressions. They take multiples when P/E super low (1, 1.5), then make averages and apply to the current book. Studying the worst years will tell you a lot about management. Inflation has a really strong effect on those multiples.

"Value Line Index" = almost 2000 companies. BT's the best index for the general stocks (S&P 500 has large cap). BT's done with median P/E instead of average P/E. As inflation goes up the multiples go down. He never found good indicators for future inflation. Close proxies for him are the price of gold and the commodity index.

When calculating worst case scenario never forget about inflation.

Temptation: "Only invest at the point of maximum pessimism." Problem is how to determine that. Remember that companies go through cycles. The only consistent ratios that they found were  $\frac{\text{EBIT}}{\text{sales}}$ ,  $\frac{\text{price value}}{\text{sales}}$ ,  $\frac{\text{price}}{\text{tangible book}}$  because earnings and CF fluctuated. Difficult to

determine the pessimism, but they have a method (27:00). To determine max pessimism just remember that in that situation stock crash deep down (my). That's another signal. Do not wait too long otherwise you'll lose that moment ( $\approx 10$  days). They invest (their entry price) when the price is 25% above the worst case price so they have more time to create the position.

Woman: Mrs Welshs  
65 years old  
inflation 12%  
Needed income  
Adopted worst case scenario.  
90% invested.