


B BETTERINVESTING™
Empowering Investors Since 1951

Economic Moats Can Help Your SSG!

Puget Sound Chapter B.I. Investor Education Conference (IEC)



Presented By:
Craig Braemer CFP® CFA®
Director, San Francisco Chapter
October 21, 2024

WWW.BETTERINVESTING.ORG

1

1

B 2

PRESENTATION DISCLAIMER

- The information in this presentation is for educational purposes only and is not intended to be a recommendation to purchase or sell any of the stocks, mutual funds, or other securities that may be referenced. The securities of companies referenced or featured in the seminar materials are for illustrative purposes only and are not to be considered endorsed or recommended for purchase or sale by BetterInvesting™ / National Association of Investors™. The views expressed are those of the instructors, commentators, guests and participants, as the case may be, and do not necessarily represent those of BetterInvesting. Investors should conduct their own review and analysis of any company of interest before making an investment decision.
- Securities discussed may be held by the instructors in their own personal portfolios or in those of their clients. BetterInvesting presenters and volunteers are held to a strict code of conduct that precludes benefitting financially from educational presentations or public activities via any BetterInvesting programs, events and/or educational sessions in which they participate. Any violation is strictly prohibited and should be reported to the CEO of BetterInvesting or the Director of Chapter Relations.
- This presentation may contain images of websites and products or services not endorsed by BetterInvesting. The presenter is not endorsing or promoting the use of these websites, products or services.
- We may be recording this session for our future use.

National Association of Investors™, BetterInvesting™ and the BetterInvesting™ Icon are trademarks/registered trademarks. All rights reserved. © 2024 BetterInvesting™.

2

B

Agenda

- Why should we care about quality and economic moats?
- What are economic moats? Or just Moats!
- Stock Selection Guide (SSG) Sections 1+ 2 (Quality) = business models = potential economic moats.
- Moat details, concepts and ideas.
- Summary

Questions, reach me at Craigbraemer1@gmail.com

3

B

4

Warren Buffett on Quality and Moats

- “When we own portions of outstanding businesses with outstanding managements, our favorite holding period is forever.”
Source: Letter to shareholders, 1988.
- “It’s far better to buy a wonderful company at a fair price than a fair company at a wonderful price.”
Source: Letter to shareholders, 1989.
- “Long ago, Ben Graham taught me that ”Price is what you pay; value is what you get.” Whether we are buying socks or stocks, I like buying quality merchandise when it is marked down.”

Source: Letter to shareholders, 2008.

Source: Berkshire Hathaway Annual Reports

*Securities are for
educational purposes
only*



4

B **5**

Concept Has Performed Well in Most Time Periods

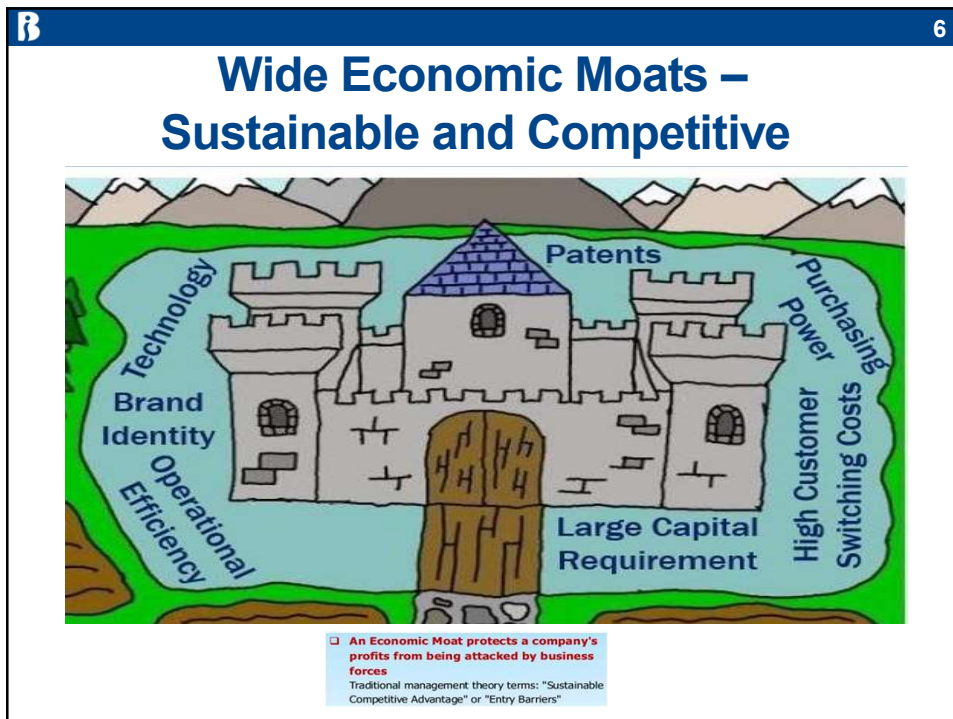
Performance History: Average Annual Total Returns* (%)

Month End as of 02/29/24	1 MO	3 MO	YTD	1 YR	3 YR	5 YR	10 YR	LIFE 04/24/12
MOAT (NAV)	4.22	10.35	2.36	24.09	11.11	14.58	13.12	14.54
MOAT (Share Price)	4.13	10.23	2.22	24.09	11.09	14.54	13.09	14.53
MWMFTR (Index)	4.26	10.50	2.43	24.74	11.73	15.15	13.70	15.11
Performance Differential (NAV - Index)	-0.04	-0.15	-0.07	-0.65	-0.62	-0.57	-0.58	-0.57
S&P 500 Index	5.34	11.98	7.11	30.45	11.91	14.76	12.70	13.88

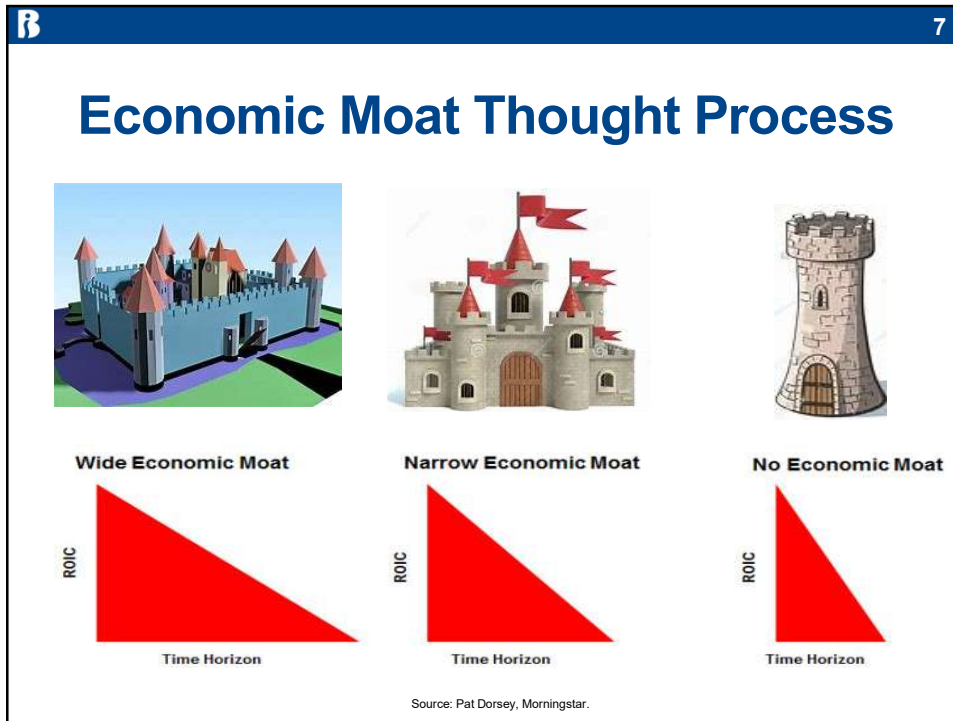
Source: Van Eck, Morningstar Direct. Returns in table annualized for periods greater than one year.

Securities are for educational purposes only

5



6



7

B **8**

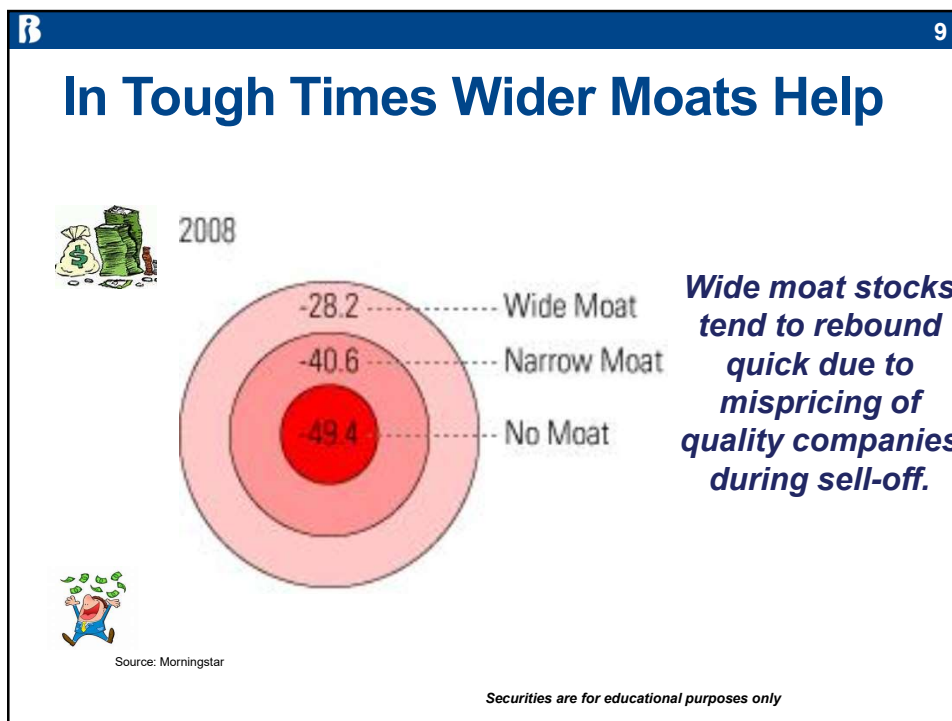
Moat Performance – No Moats Lose

Market Performance by Moat Rating and Moat Source ■ Top Performer ■ Bottom Performer

	Number of Companies	Median Annlzd 5 Yr TR (%)	Mean Annlzd 5 Yr TR (%)	Median Annlzd 10 Yr TR (%)	Mean Annlzd 10 Yr TR (%)
Morningstar Coverage Universe	1,503	13.7	13.2	7.3	6.8
Moat Rating					
Wide-Moat Companies	209	15.7	15.6	10.6	11.0
Narrow-Moat Companies	643	15.5	16.0	8.6	9.0
No-Moat Companies	651	10.5	9.6	3.3	2.9

Source: Morningstar Magazine, August / September 2017.

8



9

B **10**

Wide Moats = Sustainable Competitive Advantage = Quality Stocks

- An economic moat (competitive advantage) allows a company to fend off competitors and earn sustainable excess economic profits.
- My belief: wide / narrow moats = higher margins.
- This shows you potentially the better quality stocks.
- Section 2 of the Stock Selection Guide (SSG) is our **Quality Section**.

Spend time on quality to:
Improve returns.
Retain more good stocks.
Determine if a company is past its prime.

10

B 11

Moat and Margins

- The potential of wide moat stocks are intriguing.
- Wide moat stocks should have higher margins over a longer time period.

Moat Rating	Number of Companies	ROIC TTM (%)	ROIC Trailing 3 Yr (%)	ROIC Trailing 10 Yr (%)	Operating Margin Trailing 10 Yr (%)	Net Margin Trailing 10 Yr (%)
Wide	209	12.5	13.5	19.0	21.1	14.1
Narrow	643	9.0	9.7	14.8	14.7	9.0
None	651	5.1	4.8	8.6	7.6	4.4

Source: Morningstar Magazine, August / September 2017. *Securities are for educational purposes only*

11

B 12

Quality Analysis - SSG Style None vs Wide Economic Moat

Evaluate Management	No Moat												Trend
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	5 Yr Avg		
% Pre-Tax Profit on Sales	8.5%	6.2%	3.7%	6.1%	5.5%	2.9%	-26.5%	7.4%	6.0%	0.5%	-1.9%		
% Return on Equity	26.9%	25.2%	16.0%	36.3%	19.3%	9.2%	-175.5%	44.2%	32.7%	2.5%	-17.4%		
% Debt To Capital	58.2%	64.7%	62.0%	51.7%	43.4%	54.0%	76.5%	65.3%	61.0%	59.1%	63.2%		

Evaluate Management	Wide Moat												Trend
	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	5 Yr Avg		
% Pre-Tax Profit on Sales	57.5%	61.6%	21.2%	61.6%	60.8%	64.8%	53.1%	63.7%	62.1%	64.8%	61.7%		
% Return on Equity	11.1%	13.0%	8.0%	17.8%	19.5%	21.9%	22.0%	24.8%	35.1%	40.1%	28.8%		
% Debt To Capital	0.2%	0.0%	0.0%	0.0%	0.0%	0.0%	32.5%	35.9%	32.8%	32.5%	26.7%		

12

B 13

Our Quality Growth Companies

- HAVE STRONG FUNDAMENTALS
 - Consistent sales growth
 - Consistent earnings growth
- HAVE EXCELLENT MANAGEMENT


Source: Ann Cuneaz and Ken Kavula, Course of Study for Beginning Investors. "Selecting the Best Companies"

13

B 14

Use the SSG to Find Excellent Management or Quality

- Use Section 2 of the SSG to determine quality.
- Two profitability measures –
 - Pre-tax profit margins
 - Return on Equity (ROE)
- One balance sheet analysis - Debt-to-Capital.



Evaluate Management	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	38.5%	38.3%	37.6%	40.5%	40.4%	41.0%	38.4%	25.8%	31.8%	38.3%	34.7%	UP
% Return on Equity	18.0%	15.8%	14.8%	18.1%	20.4%	17.9%	19.8%	13.2%	14.1%	13.1%	15.6%	DOWN
% Debt To Capital	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	DOWN

14

B 15

Financial Reality of Moats

- A weakening moat should show up in margins and in the stock price over time.
- No moat stocks can do well in the short run due to growth.
- Wide moat stock's BIG RISK is expensive valuations.

Evaluate Management												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	20.0%	23.9%	20.4%	16.2%	36.8%	32.9%	27.9%	23.9%	28.3%	25.7%	27.7%	DOWN
% Earned on Equity	14.2%	16.0%	13.1%	10.2%	22.4%	25.9%	20.6%	16.9%	19.6%	19.3%	20.5%	DOWN
% Debt To Capital	5.2%	4.7%	4.8%	5.1%	4.1%	13.8%	20.8%	18.8%	19.7%	27.1%	20.0%	UP

15

B 16

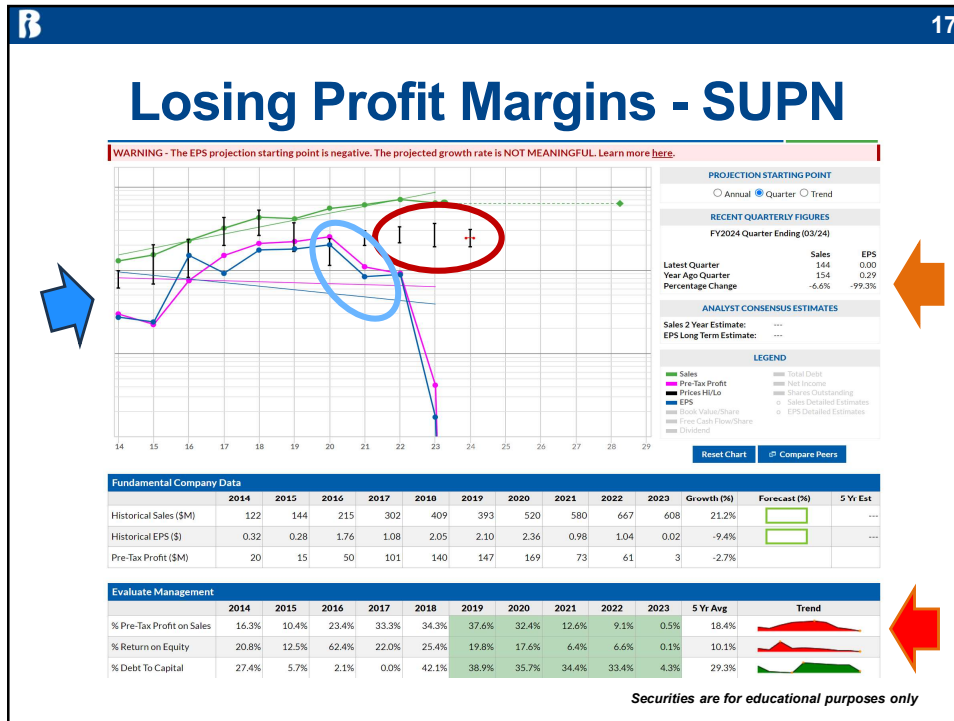
Example of Losing an Advantage

Evaluate Management												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	20.0%	23.9%	20.4%	16.2%	36.8%	32.9%	27.9%	23.9%	28.3%	25.7%	27.7%	DOWN
% Earned on Equity	14.2%	16.0%	13.1%	10.2%	22.4%	25.9%	20.6%	16.9%	19.6%	19.3%	20.5%	DOWN
% Debt To Capital	5.2%	4.7%	4.8%	5.1%	4.1%	13.8%	20.8%	18.8%	19.7%	27.1%	20.0%	UP

- Intel was a leader in their industry, but the industry changed.
- Today, Intel continues to struggle, laying off 15k employees

The chart is from 2003-17. Gold is the market return and Black is Intel.

16



17

A Wide Moat Is Similar to a Solid SSG

- Moats help identify sustainable competitive advantages.
- By doing this work it can help:
 - Support holding good quality stocks longer.
 - Helps to understand your SSG numbers.
 - Provides information about your stock.

Sections 1 & 2 of the SSG are how we analyze a company's business model or moat.



18

B 19

Solid Moat - What Do You Think?

Evaluate Management												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	32.2%	39.5%	38.3%	37.6%	40.5%	40.4%	41.0%	38.4%	25.8%	31.8%	35.5%	DOWN

- The last 5 years are down. Interesting?
- The last year has recovery.
- High pre-tax margin business model.

Knowing your company.
Doing additional analysis to understand their business can help with wide moat winning stocks like ISRG and long term issues.

Securities are for educational purposes

19

B 20

Wall Street Worries about Profit Margins and Earnings Growth = Opportunity

Evaluate Management												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	32.2%	39.5%	38.3%	37.6%	40.5%	40.4%	41.0%	38.4%	25.8%	31.8%	35.5%	DOWN

Opportunity - Know your company.
 ISRG dropped from \$198 to \$115 over two years.

Securities are for educational purposes only

20

B
21

Solid Moat - What Do You Think?

Evaluate Management	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	20.9%	21.2%	28.1%	28.4%	31.6%	35.6%	29.3%	29.3%	31.0%	28.5%	30.7%	DOWN
% Earned on Equity	25.6%	22.6%	25.8%	29.0%	33.6%	37.1%	29.0%	31.3%	40.9%	35.0%	34.7%	EVEN
% Debt To Capital	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	12.1%	24.0%	35.1%	40.4%	22.3%	UP

- Margins peaked in 2012. Recovering in 2021.
- Debt is rising. Cash is held off-shore.
- High absolute profit margins and ROE.
- I'm a leading consumer products company.
- I'm widely held in BetterInvesting – I'm Apple. Wide Moat Stock.

Securities are for educational purposes only

21

B
22

Is This Additional Analysis Useful To Your SSG?

- It makes you to think about a company's business model.
- Competitive advantages identified by this research can protect high profit margin companies.
- Is a high margin or wide moat company sustainable? This is important.
- Morningstar might be able to help.

22

B

23

Question time

- Are you doing this additional type of analysis with your Stock Selection Guide today?
 - Yes
 - No

23

B

Morningstar and Moats Can Help

- Moats fall into 3 buckets: Wide - Narrow - None.
- There are 5 categories to identify a moat.
- They focus on long term business models.
- Morningstar identifies wide moat stocks and that **moat is expected to last for 20 years.**

By learning more, I might understand a stock's long term potential and if it has a sustainable competitive advantage.


I like the potential of wide moat stocks and their performance.




24

B 25


Morningstar's 5 Sources of Sustainable Competitive Advantage




Switching Costs




Intangible Assets



Network Effect



Cost Advantage



Efficient Scale

Source: Van Eck

25


B 26

Moat Analysis – Network Effects Has Strong Performance

Market Performance by Moat Rating and Moat Source ■ Top Performer ■ Bottom Performer

	Number of Companies	Median Annlzd 5 Yr TR (%)	Mean Annlzd 5 Yr TR (%)	Median Annlzd 10 Yr TR (%)	Mean Annlzd 10 Yr TR (%)
Morningstar Coverage Universe	1,503	13.7	13.2	7.3	6.8
Moat Source					
Switching Cost	314	16.4	16.5	9.3	8.9
Network Effect	112	17.1	18.0	10.0	11.7
Intangible Assets	491	15.9	15.7	8.9	8.9
Cost Advantage	358	15.9	15.7	8.9	8.9
Efficient Scale	200	13.2	13.3	9.0	8.5

Source: Morningstar Magazine, August / September 2017.

Securities are for educational purposes only 

26

B 27

Definitions of Competitive Forces

Economic moat is a sustainable competitive barrier against competition.

- **Network Effect** – When the value of a product or service grows as its user base expands. Each additional customer increases the product’s or service’s value exponentially. *It is perhaps the strongest type of economic moat.*

- **Switching Costs** – When a company has pricing power by locking customers into its unique ecosystem, they have high switching costs. Payroll processing is an example.





Source: Investopedia, Morningstar. Securities are for educational purposes only

27

B 28

Definitions of Competitive Forces

The key of an economic moat is how long a company will keep competitors at bay.

- **Intangible Assets** - A broad category that includes brands, patents, and regulatory licenses

- **Low Cost Advantage** – Ability to offer lower prices than your competitors for the same product or services.

- **Economies of Scale** – Lower cost advantage typically comes from size or scale or “The Largest Player” in a smaller sector. Spread the costs over your size.


Source: Investopedia, Morningstar. Securities are for educational purposes only

28

B 29

Morningstar's Moat and Star Analysis

Similar to our Upside-Downside Ratio

Fair Value
Learn More ▶

Morningstar Equity Research
 Rating since 10/01/2019

★ ★ ★ ★ ★

- There are more stars when the current price is far below Morningstar's Fair Value.
- If a stock price is way above Fair Value, you get fewer stars.

Economic Moat

None Narrow **Wide**

Morningstar Equity Analyst Report
 Latest report 10/04/2019

These economic moat analysis reports are typically 10+ pages long. Great way to learn more about your investment.

Access for free through some libraries or through Charles Schwab.

Securities are for educational purposes only Source: Morningstar

29

B

Morningstar's Price vs Fair Value Over Time

Price vs. Fair Value Advanced Basic Logarithmic Linear

Fair Value
25.00

Close Price
19.99
As of Mar 31, 2024

1 and 2 Stars

4 and 5 Stars

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD	
Price/Fair Value	1.17	0.66	0.90	0.90	1.01	0.63	0.69	1.16	0.76	0.80	0.80	Price/Fair Value
Total Return %	25.35	-44.68	6.64	-25.44	24.22	-37.84	-31.60	135.38	-18.72	0.64	0.22	Total Return %
Index Total Return %	12.50	-45.37	-5.80	-46.91	29.27	-69.07	-52.50	109.59	0.71	-25.80	-10.02	Index Total Return %

USD | As of Mar 31, 2024 | Index: Morningstar US Market TR USD

Securities are for educational purposes only ★

30

B

31

Economic Moats = Business Models

As an investor, I'm trying to find information that confirms or denies my beliefs about a company's moat by doing more research.



31

B

32

How Do You Look a Bit Deeper?

- Go online to company's websites.
- Review their home page to understand their firm message.
- **Finally, go to the Investor page.**
 - Typically titled "Investor Information" or "Investor."
- Look for an Investor Presentation.
- Review other documents.



32

B

To Find This Kind of Information

The screenshot shows the RPM International Inc. website. The main navigation menu includes: About RPM, Leading Brands, News, Stock, Dividend, Reports & Financials, and Investor Information. The Investor Information dropdown menu is open, listing: Investor Overview, Why Invest?, Frequently Asked Questions, Annual Meeting, Proxy Vote, Presentations & Webcasts, Request Information, and Email Alerts. A red circle highlights the 'Presentations & Webcasts' and 'Request Information' items, with a red arrow pointing to them. A yellow arrow points to the 'Investor Information' menu item. A blue arrow points to the RPM logo. A search bar is visible in the top right corner.

RPM International Inc.
 A world leader in specialty coatings and sealants

The Value of 168®
 Our founder's favorite number.
 LEARN WHY ▶

Securities are for educational purposes only

33

B 34

Starbucks – Moat Confirmation

China
 is the largest international market for Starbucks

Expectations for the next five years

→

5,000 STORES	200+ CITIES	2x STORES	~3x REVENUE	~3x OPERATING INCOME
--------------	-------------	-----------	-------------	----------------------

SPECIALTY COFFEE MARKET*

→ 15% CAGR

Did you know that this information is available on their website?

Starbucks leads in market share** and top of mind brand awareness**

RAPIDLY INCREASING MIDDLE CLASS IN MILLIONS *

Year	Millions
2005	66
2015	300
2022	600

2x increase from 2015 to 2022

*McK Global Institution, Chinese Academy of Social Science, Euromonitor

Source: Company website. *Securities are for educational purposes only*

34

B 35

The Main Concern as an Investor

Company with an Economic Moat ➔ Company without an Economic Moat

Return on Invested Capital

Time Horizon

Return on Invested Capital

Time Horizon

Would this additional work help you as an investor?

Evaluate Management												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	5 Yr Avg	Trend
% Pre-Tax Profit on Sales	20.0%	23.9%	20.4%	16.2%	36.8%	32.9%	27.9%	23.9%	28.3%	25.7%	27.7%	DOWN
% Eamed on Equity	14.2%	16.0%	13.1%	10.2%	22.4%	25.9%	20.6%	16.9%	19.6%	19.3%	20.5%	DOWN
% Debt To Capital	5.2%	4.7%	4.8%	5.1%	4.1%	13.8%	20.8%	18.8%	19.7%	27.1%	20.0%	UP

35

B 36

If You Want to Learn More?

Securities are for educational purposes only

36

B 37

Van Eck Morningstar Wide Moat Index - MOAT

Stock ideas

Top 10 Holdings

Holding Name	Ticker	% of Net Assets
SALESFORCE.COM INC	CRM US	3.04
EQUIFAX INC	EFX US	2.94
MASCO CORP	MAS US	2.93
WELLS FARGO & CO	WFC US	2.88
WALT DISNEY CO/THE	DIS US	2.84
ECOLAB INC	ECL US	2.76
INTERCONTINENTAL EXCHANGE INC	ICE US	2.75
ALLEGION PLC	ALLE US	2.75
VEEVA SYSTEMS INC	VEEV US	2.65
US BANCORP	USB US	2.58
Top 10 Total		28.13

These are not recommendations to buy or to sell any security. Securities and holdings may vary.

Securities are for educational purposes only

37

B 38


Summary

- Strong Moats = Strong business models = “Quality” stocks = Sustainable Competitive Advantage.
- The concept of wide/narrow moat stocks fending off competitors to earn excess profits is important.
- Find Morningstar information at online libraries that subscribe and Charles Schwab.
- Moat analysis is a good additional work to help support owning a stock.
- Could this additional information help your SSG?

38

B BETTERINVESTING™
Empowering Investors Since 1951

Questions or Comments?



Craigbraemer1@gmail.com

www.betterinvesting.org

39

39

B 40

Share The Wealth!

Have you benefited from **BetterInvesting**?

 Introduce our unique investment education to others!

Share the Wealth of BetterInvesting
with
your family and friends!
Make a difference in their lives!!!



“Friends Don’t Let Friends Retire Broke”

BetterInvesting.org/InvestBetter

40