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Dustin Hunter, SunRift Capital Partners (www.sunriftcp.com)

 *(These notes are to the best of my recollection and trusty ink pen. Discrepancies are due to my error in understanding & transcribing.)*

**Pat Dorsey, Sanibel Captiva Trust – Using Economic Moats to Improve Investment Returns**

*Pat is an author, Vice Chairman, and Director of Research at Sanibel.*

Sanibel has about $600M under management

* Capitalism works - High profit operations attract competition
	+ Most businesses see returns decline over time
	+ A moat is a structural business characteristic
	+ Smart mangers are not moats, but they can create moats
* Moats
	+ Intangibles
	+ Switching Costs
	+ Network effects
	+ Cost Advantages

ROIC

ROIC

Time

Time

**Narrow Moat**

**Wide Moat**

* What are moats worth
	+ A lot if they can effectively reinvest returns to grow the business (Fastenal)
	+ Less if they cannot effectively reinvest (Microsoft)
* Management
	+ You've heard "Bet on the jockey, not the horse."
	+ Still need a good horse!
	+ The management can only be a factor in the context of a business with a moat
* Dig fanatically - what drives a business's moat
	+ Walmart - low price
	+ Amazon - Online shopping is *not* the same as offline shopping (there is a system of trust/no trust in the network) Pat mentioned that he was wrong about this early on.
	+ Louis Vuitton (LVMH) - Focus on scarcity and exclusivity
* Shoveling dirt into the moat... (investing outside the moat)
	+ Cintas - uniform business mature; tried fire safety and document management
	+ Pitney Bowes - moved into mail room outsourcing (really getting into staffing business)
	+ Cisco - trying consumer markets
	+ *A business needs to consider fitting their strategy to the moat (it's not a universal)*
* Digging the moat - Intangible Assets
	+ Brands - consistency & 'aspirational' experience
	+ Consumer
	+ Luxury
	+ Patents
	+ Regulatory
* Digging the moat - Switching costs
	+ Integrate with the business process (payback in renewals of services)
	+ Ongoing services highly profitable (elevators, jet engines)
	+ Stickiness is higher when you address 'pain points' (Stericycle - waste disposal in a doctor's office; 'just take care of it')
	+ High cost/benefit ratio (fasteners for construction availability, compressors for industrial processes availability) Important to , but small cost in the overall process
* Digging the moat - Network Effect
	+ This is one of the few 'first mover' advantages
	+ Scale quickly (eBay)
	+ Position between fragmented groups of suppliers and users (Fastenal)
* Digging the moat - Cost Advantages
	+ Process - temporary
	+ Scale - win through attrition of competitors (UPS&FEDEX vs. DHL)
	+ Niche - size brings competition (See's candies)
* Digging the moat - Technology
	+ Be willing to kill your business because landscape changes
	+ Have moral authority to do
	+ Do not ignore the inevitable (Nokia, Garmin)
* Digging the moat - Industrials
	+ Built/Destroyed via acquisitions
	+ Big Fish in small pond can lead to success & wealth (Graco, Enerpac, Scotts Miracle Grow, Middlebury kitchens)
* Digging the moat - Banks
	+ Commodity - low cost producer critical (US Bank, M&T, Wells Fargo)
* Digging the moat - Consumer Brands
	+ Longer product cycles reduce 'fashion risk'
		- 'Holy Grail' is exclusivity + ability to generate volume (Polo, Tiffany, Coach)
	+ NEVER create an incentive to switch (Schlitz beer 'bungle' with changing formula)
* Acid test to ask managers - "What are you doing to build the moat?"
* Q&A
	+ Clarification of miners?
		- Low cost raw material can be a moat
	+ Amazon - how could you have seen it ahead of time?
		- Tough - believes it's still cheap...