



Club Meeting Meeting

Invest with™
your friends

This is an Educational Demonstration

- *No investment recommendation is intended.*
- 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 are for *illustrative purposes only* and are not to be considered endorsed or recommended for purchase or sale by Manifest Investing or bivio. The views expressed are those of the instructors, commentators, guests and participants. 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.

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Agenda Overview

- Club Business (15 min)
 - Welcome and introduction of any guests
 - Minutes
 - Treasurers Report
- Investing Discussion (45 min-1 hr)
 - Portfolio Review
 - Stock Discussion
- Educational Topic (15-20 min)
- Other (5-10 min)

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Why have a club meeting meeting? Because it is a fun project to select investments. It is another whole project to run a club which selects investments. We thought we might help you to take the burden of running the club off your shoulders so you can spend time on learning to invest.

Here's a sample of an agenda you could use for your club. Note that a reasonable time length for a meeting might be 1.5-2 hours. I'd break down the percentage of time spent in each area like this. A minimal amount of time on club "business" issues perhaps 15 minutes. Most of your time on your investing discussion perhaps 45 min-1 hr. 15-20 min on your educational topic and 5-10 minutes to wrap things up. It's very important not to spend too much of your meeting on club business. The fun is in discussing your investments. If you have some club management issue that needs to be discussed, I suggest you appoint a sub committee to meet and come up with recommendations you can put to the membership for a vote, even outside of the regular meeting time.


Club Business-Minutes

- Keep for each meeting
- Brief
 - Record important decisions
 - Votes
 - Stock purchases/sales
 - Club expenditures
 - Membership matters
 - New members
 - Withdrawals
 - Action Items
 - Store minutes in bivio files area

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Club Business-Treasurers Report

- Club financial status
- Member financial status

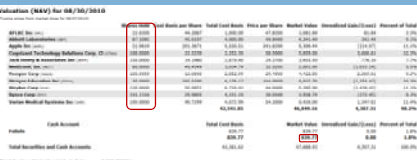



3 Reports




Your treasurers report should consist of the first three reports you will find on the Accounting>Reports page.

Treasurers Report Valuation Report

Purpose

Current Value of Club Assets

Amount of Cash available

Proves Club Accounts agree with financial institution statements

Shows value of clubs assets

Date of most recent financial account statement

Show comparison with statement



Proves account has been reconciled

Financial transactions in bivio are real

What date to prepare the report on? Official Club Valuation Date

Value

Treasurers Report Member Status Report

Shows contributions recorded since last meeting

Value of members accounts

Treasurers Report Transaction History Report

Transaction History

Date	Description	Debit	Credit
05/01/2024	Initial Cash		500.00
05/01/2024	Initial Cash		500.00
Investment Transactions, Sales, and Dividends			
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
Investment Transactions - Cash and Mutual Funds			
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
Investment Sales, Sales, and Dividends			
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	
05/01/2024	Investment	100.00	

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Transactions recorded since last meeting
Dividends and Interest received
Purchases/Sales Should agree with notes in minutes
Expenses should have been agreed to in minutes

End of Business Portion of Meeting

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That should wrap up the club operations business portion of your meeting. It's very important not to spend too much of your meeting discussing club operations. The fun is in discussing investing. If you have some club management issue that needs to be discussed, I suggest you appoint a sub committee to meet and come up with recommendations you can put to the membership for a vote, perhaps even outside of the regular meeting time.

Investing!

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Once you get your club operations business out of the way, you can get to the fun part of your meeting.

How are You Doing?

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How is your portfolio doing? You need to do a portfolio review.

Cherry Capital



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Tonights featured club is the Cherry Capitol Club from Traverse City Michigan.

Cherry Capital



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They have been very gracious to offer their portfolio to use for the portfolio demonstration . Just to give you a little flavor of the place they call home.

Cherry Capitol



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For those of you who always wondered what there was to see in Michigan.

Portfolio Review-Why?

- Looking at stocks in context
- A continuous monitoring and improvement process
- Dashboard Diagnostics

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It's important to start your investing discussion with a portfolio review because looking at your stocks in the context of overall portfolio return will help focus and guide your investing activities. When I asked the registration question "What would you like your club to be better at?", many of you gave responses such as Portfolio management and "deciding when to sell". We've been taught to go shopping and pick new stocks but we need to understand how to clean things up when our closets get overstuffed.

Maintaining a club portfolio is a continuous monitoring and improvement process.

I also think that focusing on your portfolio may help the problem some of you have with getting members more engaged in your club activities. While you are in a club, your meeting is not really about your club, it's about managing your portfolio. In fact, if your group really is focused on learning, perhaps you might like to think of yourselves as an investment partnership. That sounds a bit less social than an investment club. Members who are not engaged in this activity may just not want to be doing that. They may be participating more for the social aspects of the club. This is fine if that's how your club wants to operate. If it is causing frustration, maybe these are not people you really want to be in an investment partnership with. That said, people will likely have varying levels of expertise, make sure you give opportunities for everyone to participate even if it means accommodating "mistakes" as people learn. Again, it's up to your group to come to a comfortable way of operating that works for all the members.

I'm going to go through an overview of the Portfolio review process. If you would like more detail and to watch the process I suggest you attend one of the ManifestInvesting Dashboard Diagnostics sessions. Mark Robertson goes through the analysis and review of a club portfolio, just like you should go through your own analysis. During the upcoming months we'll also try and demonstrate the process with additional examples.

Portfolio Review

1. Look at how you're doing
2. Look at your projected return
3. Determine possible portfolio changes
4. Discuss other stocks
5. Implement changes

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- Look at how you're doing
- Look at how your portfolio is projected to perform
- Determine possible changes
- Study other stocks
- Implement Changes

1. How are You Doing? Performance Benchmark Report

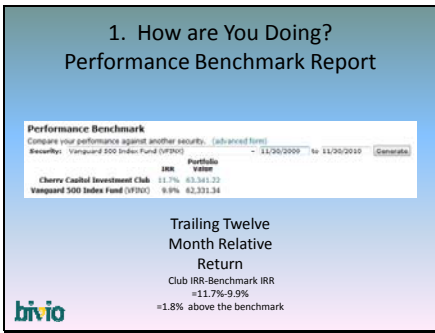


For some reason, (perhaps fear), we don't do this often enough. What you might think about is that having a goal you'd like to achieve will help make it clear what you must try and do to get to it. The first step toward fixing things is finding out where you stand.

Even if you are not doing well now, your overall goal is to learn to do well. Nobody does well when they are first learning something. In fact, many times the best learning comes from making mistakes.

Pat yourselves on the back that you are trying to learn. Investing is not something you will learn unless you really try and do it. So get up your courage and look at your portfolio performance numbers.

The place to go in bivio to see how you're doing is called the Performance Benchmark Report. You get to it from the reports page.



This report is called a performance benchmark report because it compares your rate of return to another investment . You select the investment you want to compare to and the time period over which you want to make the comparison

The comparison that is made is between IRR or Annualized Internal Rate Of Return for the two investments.

This gives you a birds eye view of how good you are at making investing decisions A higher number means your investments are growing faster than if you'd put the money into whatever you are comparing with.

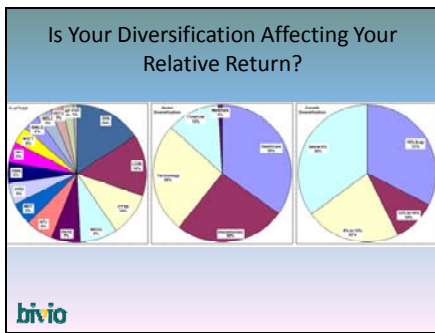
What's interesting is to track "relative Return"

this is the difference between the return you achieved by your club investment management efforts and the return you would have received if you had done a lot less work and just purchased shares of your benchmark investment.

I usually have clubs regularly keep on eye on their relative return for the past year. Especially the month to month trend in this value. But, looking at your relative return for longer time periods can give you an overall indication of how good of investors you are. The relative return for the Valley Ventures for the lifetime of their club (which started in 1997) is plus .9%. Anything above 0 is very impressive and not easy to achieve over such a long time frame. Remember, most professional money managers don't beat the indexes very reliably.

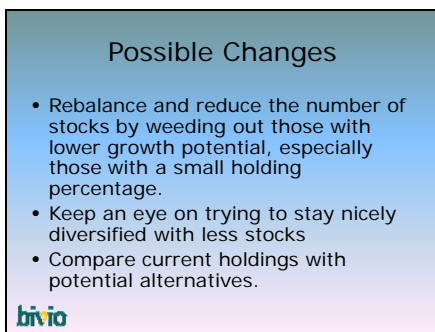


Here's a graph of the trend in their relative return since the beginning of 2008. At bivio, we are encouraging clubs to join our Quest for Positive Relative Returns. If you'd like to participate, we'll make a graph like this for your club and add a link to your club pages to see it. The graph shows your club's relative return for successive 12 month periods starting in 2008 (assuming you have enough data). The graph for this club is a bit different from what I am seeing in a lot of clubs. Many clubs had an easier time beating the market when it was down in 2008, but haven't had as much success as it has come back in 2009 and 2010. However, this club seems to be doing better than the market even when compared to an up market. That's very impressive.



This club has a pretty nicely diversified portfolio by holding size and by sector. It does have quite a few stocks. If holding sizes get too small, changes in value may not have much impact on portfolio performance. Of course, this is good if the value goes down. However, not so good, if the stock was a good choice and increases in value. It's also hard to really follow the business results of this many companies thoroughly. The club might find they could do just as well with more in depth watching of fewer companies.

The club has a nice balance of sales growth potential. This probably helped them when the market was falling and they have enough stocks with higher growth potential to help them beat the better market going on lately.



Once you've determined where your portfolio stands, you will have a better idea of your problem areas which will give you some direction to decide what stocks to study.

Do you need to increase the growth projections for your portfolio by replacing lower growth potential stocks with higher quality alternatives? What stocks might be dragging your projected return down? Possible sell candidates! What higher potential return stocks might you add to your portfolio? These are your stock study candidates.

Are you over/underweighted in any stocks or sectors? This will also lead you to possible sell candidates or help guide your search efforts for new stocks.

Is your portfolio meeting sales growth and quality targets?- You want to invest in high quality companies and have a portfolio where the cumulative projected sales growth is between 10 and 12 percent.

Compare current holdings-This isn't as important. You might already have enough good stocks to make a nice portfolio. You don't always have to be shopping. Better to keep a close eye on what you already own. If it's good, buy some more of it!

bivio Dozen

Public Dashboard: bivio dozen

This list of "Top 1%" stocks will be published monthly at www.bivio.com. Values are continuously benchmarked against the "benchmark" S&P 500 index.

Company	Market Cap	Price	YTD Total Return	12 Month	5 Year	10 Year	Div Yield	PE Ratio	EPS	EPS Growth
Microsoft	\$784.1	\$427.1	14.1%	20.0%	0.9%	97%	88	84	22.2%	
Amazon	\$678.1	\$203.7	13.8%	19.0%	1.2%	82%	89	85	22.1%	
Facebook	\$484.1	\$133.9	13.5%	18.0%	1.7%	83%	78	73	21.4%	
Google	\$445.1	\$217.3	14.4%	21.0%	0.8%	84%	34	41	14.1%	
Apple	\$308.1	\$205.5	13.1%	19.0%	0.8%	89%	67	74	14.2%	
Oracle	\$281.1	\$41.0	13.0%	18.0%	0.0%	88%	86	82	14.1%	
LinkedIn	\$278.1	\$45.9	13.0%	18.0%	0.0%	81%	80	80	14.1%	
Microsoft	\$267.1	\$28.8	13.0%	14.0%	1.8%	89%	81	81	14.0%	
Facebook	\$218.1	\$90.1	13.0%	14.0%	1.8%	89%	88	78	14.0%	
Google	\$182.1	\$77.4	13.0%	14.0%	1.8%	100%	89	86	14.0%	
Amazon	\$112.1	\$11.4	13.0%	14.0%	1.8%	89%	78	84	14.0%	
Total & Average	\$1,198	100.0%	14.0%	18.0%	1.0%	78%	78	86	14.0%	

If you need a starting point to get some ideas of stocks to study, you might look at the ManifestInvesting bivio dozen. This list is published monthly and it is the stocks with the highest quality and growth projections from the Manifest universe. You'll find a link to the current list in the Expected Returns column on our Homepage.

Here's an example of this months list. You can see how their PAR compares to VFINX. You can also see they represent a variety of industries. I would not just purchase any of these stocks blindly but, depending on what your portfolio needs, you may find some of them might be interesting for you use as a starting point for further studies.

- Recap**
Portfolio Review Process
1. Look at how you're doing
 - Performance Benchmark Report
 2. Look at how your portfolio is projected to perform
 - ManifestInvesting Dashboard
 3. Identify areas for improvement
 4. Identify and study candidates for replacement
 5. Implement changes

Educational Topic

Profitability
Net Margin

Tonight's club educational topic is about one of the business fundamentals you should keep an eye on when you own stock in a company,

Its profitability or net margin

Following a Stock


Business results

As we discussed last month, once we own a stock, we want to track it's

business results from quarter to quarter. If we see big changes or management starts to warn us of difficulties ahead, we need to decide whether we want to stay an owner of the company.

Net Margin

$$\frac{\text{Net Income}}{\text{Sales}}$$



So what is net margin?. I'm sure you've all heard about something called profit margin.


Profit margin is the percentage of a company's sales the company gets to keep after subtracting the expenses of running the business.

on financial reports, profit is called Net income.

Profit margin is called Net margin.

Chiquita Brands Intl. Inc.
 Condensed Statement of Income
 (in thousands, except per share data)

	2014	2013
Revenues	\$1,214,213	\$1,214,213
Recessed operating costs (exclusive of Depreciation and amortization (shown separately below)):		
Food, beverage and packaging	444,000	414,471
Labor	111,234	86,619
Overseas	32,206	28,877
Other operating costs	71,677	64,238
General and administrative expenses	18,732	24,751
Depreciation and amortization	1,148	1,414
Pre-opening costs	1,943	2,757
Loss on disposal of assets	2,512	7,242
Total operating expenses	683,450	630,759
Income from operations	530,763	583,454
Interest and other income	185	183
Interest and other expense	(127)	(110)
Income before income taxes	530,821	583,527
Provision for income taxes	(28,271)	(27,430)
Net income	\$ 48,550	\$ 50,097
Earnings per share:		
Basic	\$ 0.52	\$ 0.52
Diluted	\$ 0.52	\$ 0.52
Weighted average common shares outstanding:		
Basic	93,222	93,672
Diluted	93,428	93,848




On an income statement all the different types of expenses are listed between the sales at the top of the report and the

Net income at the bottom.

To track and project the net margin, we follow news about the types and amounts of a expenses a company has.

In a well managed company, management will have good control of their expenses and the net margin will stay fairly constant or, in the best case increase.

Net Margin
 Predict Future Earnings



The reason we want to keep an eye on net margin, is because it is one of the judgments we use to

predict future earnings.

Earnings
 Stock Price




And, as we all know, earning are important because ultimately, they drive a

Stock's price.

	A	B	C
3			
4	Quarterly Sales-4th Quarter 2008	30583	
5	1. Enter your Projection for the Percentage Growth in Quarterly Sales	20%	
6	2. Sales Growth Projection (Percentage)	20%	
7			
8	3. Enter your Projection for the Net Margin for the First Quarter	20.00%	
9	4. Net Margin Projection (Percentage)	20.00%	
10			
11	Your Prediction of Earnings	\$ 4,444.95	
12	(Press F8 to calculate after you enter the four judgments above)		
13			
14	5. Enter your Projection for Average Number of Shares Outstanding at the End of the First Quarter	100	
15	6. Projection of Number of Diluted Shares Outstanding	100	
16			
17	Your Prediction of Earnings Per Share	\$ 4.79	
18	(Press F8 to calculate after you enter the three judgments above)		
19			
20	7. P/E Projection	15	(P/E for Nov 2008)
21	(Press F8 to calculate)		
22	Your Prediction of the Stock Price	\$ 357.75	

We use a spreadsheet like this to make our calculations. You can input your judgments about

future sales growth

Future net margin

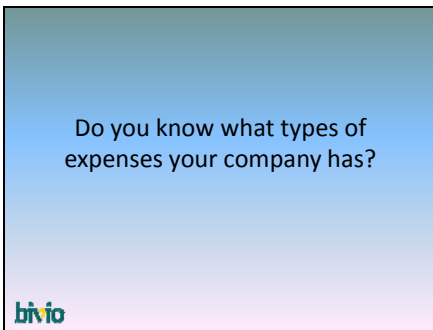
And Future P/E to project

Future earnings and ultimately

Future stock price.

We discussed how to make the judgment for future sales growth last month. The net margin is the second judgment and the one we're talking about tonight. What's great about using a spreadsheet is that as you're making decisions about how the different judgment items, you can easily do "what if" studies to get an idea of the impact certain events might have on the stock price of a company. The spread sheet can also be easily adjusted to make projections over different time horizons.

When you purchased a stock, you actually made a judgment about what type of net margin you expected the company would maintain. Once you own it, you want to track whether management is meeting your expectations. If they are, your stock price should increase as you expected. If they are not, you might want to revise your judgment to decide whether you want to keep the stock or not.



The first thing to think about when making a judgment about net margin is this.

Do you know what types of expenses your company incurs to run it's business?

Sounds like a simple question but if you really start to pay attention to this, you will realize that you are much more comfortable assessing certain companies than others. This is why you often hear to buy what you know. If you don't understand how a company makes money, how will you be able to understand if it is doing well now and might do well in the future?

Types of Expenses

- Cost of Goods Sold
- Operating Expenses
- Other Income and Expenses
- Income Tax Expense

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What types of expenses might a company have? Most of the time, they will fall into 4 main categories.

Cost of goods sold for a manufacturing or retail company

Operating Expenses

Other Income and Expenses

Income Tax Expense

Types of Expenses

- Cost of Goods Sold
 - Raw Materials
 - Direct Manufacturing Labor
 - Direct Manufacturing costs
 - Purchase of inventory

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Here are some examples of the different types of expenses.

Cost of Goods sold-In a manufacturing or retail company, these are all the costs directly associated with the production or purchase of items the company sells. It includes things like:

Raw Materials

Direct Manufacturing labor

Direct Manufacturing costs

Costs of goods purchased for sale

Types of Expenses

- Operating Expenses
 - Management
 - Administrative Costs
 - Sales and Marketing Costs
 - Research and Development Costs
- Other Income and Expenses
 - Interest Expense
 - Gains and Losses on disposal of assets
 - Goodwill impairment (write down) expense
- Income Tax Expense

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Operating Expenses

These are regular costs of running the business, often referred to as Overhead. They include costs such as

Management Expenses

Administrative Expenses

Sales Expenses

Research and Development

Other Income and Expenses

These are costs which may occur infrequently but are not unusual. If a company has long term debt, the interest payments will be shown in this category

as will gains or losses as assets are sold.

If a company has goodwill on it's balance sheet that becomes less valuable, it will have to deduct or writedown the loss in value as an expense. This will be shown in this category.

Income Tax Expense

All companies need to pay taxes. The income tax expense reported is an estimate. It is important to understand whether increases or decreases in net income are coming about because of changes in the estimated tax rate.

Apple Inc. (AAPL) Income Statement

Fiscal year ends in September. USD in millions except per share data. 2010-09 2009-09

Revenue (Sales)	65225	42955
Cost of revenue (Cost of Goods Sold)	39541	25683
Gross profit (Sales - Cost of Goods Sold)	25684	17272
Operating expenses		
Research and development	1782	1333
Sales, general and administrative	5517	4149
Total operating expenses	7299	5482
Operating income (Gross Profit - Operating Expenses)	18385	11790
Other income and expense	155	326
Income before taxes (Operating Income +/- Other Income & Expenses)	18540	12116
Provision for income taxes	4527	3811
Net income	14013	8305
Earnings per share		
Basic	13.41	9.32
Diluted	13.15	9.08
Weighted average shares outstanding		
Basic	909	893
Diluted	925	907

The different types of expenses are grouped on the income statement. An income statement is designed like a set of steps. By grouping the expenses into different types of categories, you can take a birds eye view of a company business results and get a quick feel for whether it will be harder for them to make a profit going forward than it was in the past.

The first section is where you will find the cost of goods sold expenses.

This leads to a line called gross profit. Gross profit is sales minus just the cost of what is actually being sold.

In the second section are all the other operating expenses.

Income after they are subtracted is called Operating income

After that is a section where the Other Income and Expenses are recorded.

It leads to a line of income called Income before taxes or pretax income.

Then the estimate of the tax expense

Leading finally to net income.

	2018	2019	2020	2021	2022
Revenue (Sales)	\$215.6	\$233.8	\$262.2	\$276.0	\$295.4
Cost of Revenue (Cost of Goods Sold)	\$120.0	\$127.7	\$135.7	\$145.6	\$150.0
Gross Profit (Sales - Cost of Goods Sold)	\$95.6	\$106.1	\$126.5	\$130.4	\$145.4
Gross Profit Margin (Gross Profit/Sales)	44.4%	45.4%	48.2%	47.4%	49.2%
Operating Expenses	\$10.2	\$11.0	\$12.0	\$12.0	\$12.0
Research and development	\$6.5	\$6.9	\$7.5	\$7.5	\$7.5
Sales, general and administrative	\$3.7	\$4.1	\$4.5	\$4.5	\$4.5
Total operating expenses	\$10.2	\$11.0	\$12.0	\$12.0	\$12.0
Operating Income (Gross Profit - Operating Expenses)	\$85.4	\$95.1	\$114.5	\$118.4	\$133.4
Other income and expense	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Income before taxes (Operating Income + Other Income & Expense)	\$85.4	\$95.1	\$114.5	\$118.4	\$133.4
Provision for income taxes	\$12.7	\$13.1	\$13.0	\$13.0	\$13.0
Net Income	\$72.7	\$82.0	\$101.5	\$105.4	\$120.4

Note that this is what's called a condensed income statement. You won't find a list of all the detailed expenses here but it does offer you the numbers you need to determine what categories of expenses you should focus your attention on. I pulled up this spreadsheet of information for apple right from morningstar.com. What's useful is to look at what percentage each category is in relation to the total amount of sales.

For example, one number you will often hear discussed is gross profit margin. Gross profit margin is gross profit divided by sales. Changes in this come about due to changes in expenses directly related to the product the company sells. If raw material or labor expenses are going up, it may be hard for a company to maintain historic gross profit margin levels. This, of course will mean downward pressure on earnings. You can see for Apple that gross profit margin has increased for the past 2 years.

You need to watch how these percentages are changing as new earnings reports come out. If there has been a significant change or if management discusses future product costs which might impact it, you might want adjust your future net margin judgments.

	2018	2019	2020	2021	2022
Revenue (Sales)	\$215.6	\$233.8	\$262.2	\$276.0	\$295.4
Cost of Revenue (Cost of Goods Sold)	\$120.0	\$127.7	\$135.7	\$145.6	\$150.0
Gross Profit (Sales - Cost of Goods Sold)	\$95.6	\$106.1	\$126.5	\$130.4	\$145.4
Gross Profit Margin (Gross Profit/Sales)	44.4%	45.4%	48.2%	47.4%	49.2%
Operating Expenses	\$10.2	\$11.0	\$12.0	\$12.0	\$12.0
Research and development	\$6.5	\$6.9	\$7.5	\$7.5	\$7.5
Sales, general and administrative	\$3.7	\$4.1	\$4.5	\$4.5	\$4.5
Total operating expenses	\$10.2	\$11.0	\$12.0	\$12.0	\$12.0
Operating Income (Gross Profit - Operating Expenses)	\$85.4	\$95.1	\$114.5	\$118.4	\$133.4
Other income and expense	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Income before taxes (Operating Income + Other Income & Expense)	\$85.4	\$95.1	\$114.5	\$118.4	\$133.4
Provision for income taxes	\$12.7	\$13.1	\$13.0	\$13.0	\$13.0
Net Income	\$72.7	\$82.0	\$101.5	\$105.4	\$120.4

Another comparison that is often made is for pretax profit margin. This is the ratio of Income before taxes to total sales. Some feel that expenses up to this point are those that management has the most control over and therefore if this margin stays pretty steady, it is an indication management is performing up to expectations. As you can see, Apple has increased or maintained it's pre tax profit margin for the last four years.

	2010	2009	2008	2007
Revenue (Sales)	\$4923	\$4206	\$3745	\$3008
Cost of Revenue (Cost of Goods Sold)	\$2835	\$2118	\$1957	\$1514
Gross Profit Margin (Gross Profit/Sales)	42.4%	43.3%	43.2%	34.2%
Operating Expenses	\$1762	\$1557	\$1387	\$952
Operating Income (Operating Profit/Income)	\$3126	\$2649	\$2358	\$2056
Income Before Taxes (Operating Income of Other Income & Expenses)	\$3080	\$2599	\$2304	\$2008
Income Tax Rate (Provision for Income Tax/Income Before Taxes)	19.8%	18.1%	18.8%	18.4%
Net Income	\$802	\$950	\$924	\$808
Net Margin (Net Income/Sales)	16.3%	22.6%	24.7%	26.8%

A ratio I personally like to keep an eye on is

the income tax rate. This is just the provision for taxes divided by the income before taxes. I don't like to see net earnings increase just because for some reason the company has managed to achieve a better tax rate during this period. I even sometimes recalculate earnings as they would have been if the tax rate hadn't changed.

As you can see, some of the increase in Apples earnings for 2010 were due to a decrease in their income tax rate.

	2011	2010	2009	2008
Revenue (Sales)	\$6528	\$4206	\$3745	\$3008
Cost of Revenue (Cost of Goods Sold)	\$3540	\$2118	\$1957	\$1514
Gross Profit Margin (Gross Profit/Sales)	45.8%	43.3%	43.2%	34.2%
Operating Expenses	\$2162	\$1557	\$1387	\$952
Operating Income (Operating Profit/Income)	\$4366	\$2649	\$2358	\$2056
Income Before Taxes (Operating Income of Other Income & Expenses)	\$4320	\$2599	\$2304	\$2008
Income Tax Rate (Provision for Income Tax/Income Before Taxes)	16.9%	18.1%	18.8%	18.4%
Net Income	\$1102	\$950	\$924	\$808
Net Margin (Net Income/Sales)	16.9%	22.6%	24.7%	26.8%

Finally, of course, we get to the calculation of the fundamental judgment we are discussing tonight, the net margin.

Net margin is just the bottom line (net income) divided by the top line (sales). Each quarter I make this calculation and compare it to the judgment I used when I bought Apple stock. In my case, I used a 20% net margin to base my purchase decision on.

Apple did better than that during the most recent year.

Where Do you Find Information?

Management Discussion and Analysis sections in quarterly financial reports

<http://www.sec.gov/edgar/searchedgar/companysearch.html>

The next step is to understand why the changes you're seeing have happened. You should go to the financial reports and the earnings conference call to see how management is explaining them. As we discussed last time, all the financial reports are available at the SEC (securities and exchange commission) website.

Here is the link:

You type in the ticker of the company you are looking for

Where Do you Find Information?

Company Name	Industry	Market Cap	Other Metrics
Apple Inc.	Technology	150.00B	...
Microsoft Corp.	Technology	120.00B	...
Amazon.com Inc.	Retail	100.00B	...
Facebook Inc.	Technology	80.00B	...
Alphabet Inc.	Technology	70.00B	...

Then select the report you want to look at from this list. In this case, we are going to look at the latest annual report or 10-K

This is the top of the report. It looks scary at first but contains lots of great information.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
FORM 10-K
ANNUAL REPORT PURSUANT TO THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended September 30, 2012
APPLE INC.
Exact name of the registrant as it appears on its certificate of incorporation
Apple Inc.
100 Apple Park Blvd.
Cupertino, California 95014
Exact name of the registrant as it appears on its certificate of incorporation
Apple Inc.
100 Apple Park Blvd.
Cupertino, California 95014

What Causes Expenses to Change?

- Increase/decrease in price of raw materials
- Increase/decrease in labor costs
- Interest expense due to addition of debt
- Capital expense due to expansion
- Gains and losses due to sale of assets
- Increased selling and marketing expenses
- Increased bad debt expense if customers become more unable to meet commitments
- Increased warranty costs due to a bad design

First of all, it helps to know what you are looking for. What causes expenses to change? It will be different things for different types of businesses including things like:

Increase/Decrease in price of raw materials

Increase/Decrease in labor costs

Interest expense due to addition of debt

Capital expense due to expansion

Gains and losses due to sale of assets

Increased selling and marketing expenses

Increased bad debt expense if customers become more unable to meet commitments

Increased warranty costs due to a bad design

Gross Margin

The gross margin percentage in 2010 was 39.4% compared to 40.1% in 2009. This decline in gross margin is primarily attributable to new products that have higher cost structures, including iPad, partially offset by a more favorable sales mix of iPhone, which has a higher gross margin than the Company average.

The Company expects its gross margin percentage to decrease in future periods compared to levels achieved during 2010 and anticipates gross margin levels of about 36% in the first quarter of 2011. This expected decline is largely due to a higher mix of new and innovative products that have higher cost structures and deliver greater value to customers, and expected and potential future component cost and other cost increases.

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There is lots of good stuff to be found in financial reports. In the latest Apple report, there are specific reasons given for changes in each of the expense areas we pointed out. For example, here is the discussion of their gross margin.

First, they explain the reason their gross margin declined a bit between 2009 and 2010 is that the margin is not as high on Ipads. Their margin was, however helped by the fact that they sold so many Iphones which are more profitable.

Then a comment for what might be coming going forward. A warning that their gross margins will probably be decreasing. Apple was more aggressive in pricing the Ipad. Even if it is successful, it may not be as profitable as the Iphone.

There is more in this section but the bottom line appears to be that Apple expects gross margins to trend downward. This will mean net margin will probably also decrease from recent levels.

Operating Expenses

	2010	2009	2008
Research and Development	\$1,800	\$1,350	\$1,000
Selling, general and administrative	\$1,200	\$1,100	\$1,000
Percentage of net sales	8.3%	8.7%	11.0%

Research and Development Expense ("R&D")
R&D expense increased 34% or \$449 million to \$1.8 billion in 2010 compared to 2009. This increase was due primarily to an increase in headcount and related expenses in the current year to support expanded R&D activities.

Although total R&D expense increased 34% during 2010, it declined as a percentage of net sales given the 52% year-over-year increase in net sales in 2010.

The Company continues to believe that focused investments in R&D are critical to its future growth and competitive position in the marketplace and are directly related to timely development of new and enhanced products that are central to the Company's core business strategy. As such, the Company expects to make further investments in R&D to remain competitive.

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How about the next category of expenses, operating expenses? Often in the notes, you can find more detail about the values that made up each line item in the condensed income statement. Here R&D and Selling, General and Administrative expenses as a percent of sales are shown.

First Apple discusses a significant increase in R&D spending. For a company like Apple this is a good thing. It is also good that despite spending more dollars on R&D, on a

percent of sales basis there was a bit of a decrease due to the high year to year increase in sales.

Management also confirms that they believe R&D expenditures are important. This might be important in terms of margins, because if sales growth slows down a bit, the same level of R&D spending might mean that margins will decline a bit.

Operating Expenses

	2010	2009	2008
Research and development	\$ 3,762	\$ 3,233	\$ 2,853
Selling, general and administrative	\$ 1,717	\$ 1,540	\$ 1,392
Percentage of net sales	6%	6%	5%

SG&A expense increased \$1.4 billion or 33% to \$5.5 billion in 2010 compared to 2009. This increase was due primarily to the Company's

- continued expansion of its Retail segment,
- higher spending on marketing and advertising programs,
- increased stock-based compensation expenses
- variable costs associated with the overall growth of the Company's net sales.

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They discuss a fairly large increase in sales/administrative and general expense

Coming from:

- continued expansion of its Retail segment,
- higher spending on marketing and advertising programs,
- increased stock-based compensation expenses and
- variable costs associated with the overall growth of the Company's net sales.

has come about from continued retail expansion

Other Income and Expense

	2010	2009	2008
Interest income	\$ 175	\$ 157	\$ 175
Other non-recurring gain	\$ 220	\$ 117	\$ 107
Total other income and expense	\$ 395	\$ 274	\$ 282

The overall decrease in other income and expense is attributable to the significant declines in interest rates on a year-over-year basis, partially offset by the Company's higher cash, cash equivalents and marketable securities balances.

Additionally the Company incurred higher premium expenses on its foreign exchange option contracts, which further reduced the total other income and expense.

During 2010, 2009 and 2008, the Company had no debt outstanding and accordingly did not incur any related interest expense.

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The next category of expenses that Apple discusses is the "other income and expense" category. If you recall, this is where expenses are recorded that are not unusual to a company's business but do not necessarily occur on a regular basis. Items in this category can either increase or decrease net income.

Again, we find a little table which provides some details for the numbers shown in the condensed report.

Just like the rest of us, Apple was not able to earn as high of an interest rate on their cash as they have in the past. However, that was somewhat offset by the fact that they have more of it.

They did have some higher expenses for premiums on foreign exchange option contracts. These are probably used by them to hedge the effects of their foreign currency exposure.

If a company has long term debt, the interest payments they have to make on it will be an expense in this category. Apple makes sure to point out that they do not have any debt.

Income Taxes

•The lower effective tax rate in 2010 as compared to 2009 is due primarily to an increase in foreign earnings on which U.S. income taxes have not been provided as such earnings are intended to be indefinitely reinvested outside the U.S.

•The Internal Revenue Service (the "IRS") has completed its field audit of the Company's federal income tax returns for the years 2004 through 2006 and proposed certain adjustments. The Company has contested certain of these adjustments through the IRS Appeals Office.

•The IRS is currently examining the years 2007 through 2009.

•All IRS audit issues for years prior to 2004 have been resolved. During the third quarter of 2010, the Company reached a tax settlement with the IRS for the years 2002 through 2003.

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As we noted earlier, some of the increase in Apples net income in 2010 was due to an income tax rate that was lower than it had been in the past. If company's have earnings overseas and they do not bring those earnings back to the US, they do not have to pay US taxes on them. They may have to pay foreign taxes on them but it appears in this case, it is less than the US taxes.

Many companies discuss IRS audit activity in their financial reports and it's important to watch what's going on with them. Many times a settlement can mean an extra expense in the future. Apple does not give any specific amounts for the settlement they mention which usually means they do not feel it will have a material impact on their financial results. If it would, they would have to give more detail on the amount they expect to have to pay. A large settlement expense could make it harder for a company to meet it's expenses with it's current cash flow which would mean they might have to take on debt to cover their day to day operations.

Where Do you Find Information?

Earnings conference calls



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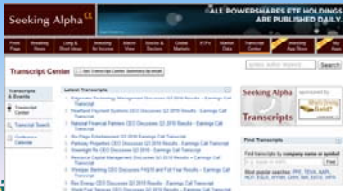
A second excellent source of information about current and future expenses are the

quarterly earnings conference calls.

You can listen to these live when they happen or listen to recordings posted on company websites.

Earnings Conference Calls

- Seeking Alpha
- <http://seekingalpha.com/tag/transcripts>



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Seeking Alpha also seems to be regularly transcribing them.

You can search for transcripts here.

Click

Apple 4th Qtr 2010 Conf. Call

- Total company gross margin was 36.9%, better than expected. About two-thirds of this favorability was driven by lower commodity and other costs, and the remainder was mostly attributable to a better-than-planned mix of iPhone sales.
- Operating expenses were \$2.07 billion and included \$185 million in stock-based compensation expense.
- OI&E was \$14 million
- The tax rate for the quarter was 21%, about five points below our guidance, largely a result of two factors. First, we had a higher mix of foreign earnings than we planned. Second, we had some discrete one-time tax benefits in the quarter as well. Our tax rate for fiscal 2010 was about 24.5%.

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Here's an excerpt from the fourth quarter Apple call. As you'll see, they discuss the expense categories we've gone over tonight.

First they talk about their gross margin and how it was better than expected due to lower materials costs and a better than anticipated percentage of sales coming from iPhones which bring in higher margins.

Then they talk about the operating expense category and how much of that was related to stock based compensation. Perhaps to fend off concerns that management is being overpaid.

Ah. Some jargon. Since you've attended tonight's webinar, you know that OI&E stands for Other Income and Expenses. Remember, that's the category where they include interest they've earned and they would have included interest they paid on debt if they had any. For now, for Apple, the OI&E category is adding to their net income.

Finally, they make note of why their income tax rate was lower than usual. A mention of "one time" benefits, is a clue that what was seen this year might not continue into the future. When you decide whether their net margin will be the same going forward as it has been, you will probably want to decide whether you think this favorable tax rate will continue or it might move back toward historical rates. It looks like the answer to that question depends on how much of Apple sales come from overseas in the future.

Projections-1st Qtr. 2011

- We expect revenue to be about \$23 billion compared to \$15.7 billion in the December quarter last year.
- We expect gross margins to be about 36% reflecting approximately \$52 million related to stock-based compensation expense.
- We expect OpEx to be about \$2.325 billion including about \$250 million related to stock-based compensation.
- We expect OI&E to be about \$65 million.
- We expect the tax rate to be about 25.5%.
- We're targeting EPS of about \$4.80

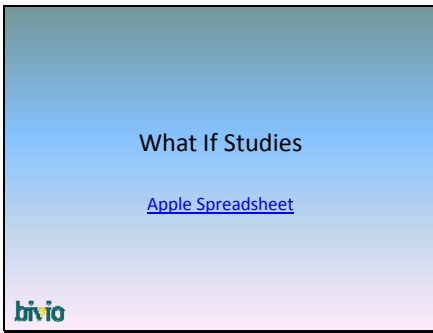
bivio

They go on to give projections for the next quarter. Which is very useful because we can go back to our spreadsheet and put together an expected income statement for the next quarter using this information.

Fiscal year ends in September. USD in millions except per share data.		Projected 2011- First Qtr
Revenue (Sales)		23000
Cost of revenue (Cost of goods sold)		14720
Gross profit (Sales - Cost of Goods Sold)		8280
Operating expenses		
Research and development		
Sales, General and administrative		
Total operating expenses		2325
Operating Income (Gross Profit - Operating Expenses)		5955
Other income and expense		60
Income before taxes (Operating Income +/- Other Income & Expenses)		6020
Provision for income taxes		1534.50
Net Income		4484.50
NET MARGIN		19.5%

Allowing us to calculate what Apple is giving guidance might be the Net Margin for the first quarter.

- We expect revenue to be about \$23 billion compared to \$15.7 billion in the December quarter last year.
- We expect gross margins to be about 36% reflecting approximately \$52 million related to stock-based compensation expense.
- We expect OpEx to be about \$2.325 billion including about \$250 million related to stock-based compensation.
- We expect OI&E to be about \$65 million.
- We expect the tax rate to be about 25.5%.
- We're targeting EPS of about \$4.80



It's a number we can plug into our projected earnings spreadsheet and see what it leads us to in terms of possible stock price.

Apple guided that they expected earnings to grow 46.5 % (from \$15.7- \$23 billion) from the Same quarter a year ago.

From the expected income statement we prepared from their guidance, they are projecting a 19.5% net margin

This leads to earnings for the quarter of \$4428.04

If the number of shares outstanding remains where it was at the end of the most recent quarter, this leads us to an Earnings per share amount of \$4.66.

At an projected average P/E of 21, a price of \$338.96 does not seem unreasonable for their stock.

Apple is actually guiding an earnings per share amount of \$4.80. Given their other projections, they could achieve this be decreasing the number of shares of stock they have outstanding to 922.5

If that happened, perhaps their stock price might rise as high as \$341.88.

Perhaps you don't think their sales will increase as much as they are projecting. Perhaps you think they will not be able to keep the margins they are projecting. The beauty of having a computer and a spreadsheet is that it allows you to perform "what if" studies to give you some sense of the range of prices you might anticipate.



Remember, following a stock doesn't mean just following it's price.

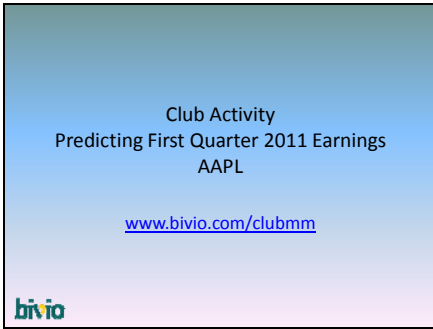
It means following how it's business is doing.

Keep up to date on news from the company about sales and expenses in the future. Make sure the company is growing as you expected when you purchased it.



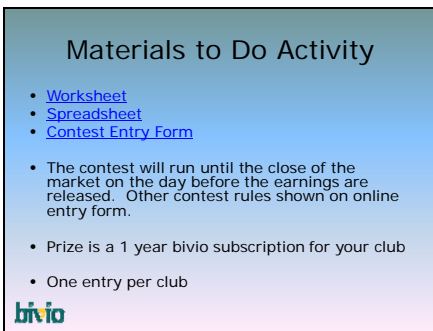
The more you pay attention to this, the better you'll get at "seeing things coming"

and moving in and out of investments at appropriate times.



As I announced last month, I have developed an activity I hope you will attempt and I hope might help the problem some of you have with getting your club members engaged with the process of investing. We're going to have a contest. The prize for our contest will be 1 year free bivio subscription for your club.

Play with the spreadsheet I just showed you and see what you come up with as your first quarter earnings projection.



Last month we talked about how to project sales growth. I gave you a worksheet you can use to help you decide your sales growth judgment. It,

The Spreadsheet to make calculations

And the Contest Entry Form

Are all posted on the Club MM website. A copy of this presentation is also posted there.



Add link to sec and earnings transcripts to Clubmm page

Other Upcoming Events

Dashboard Diagnostics-December 16
Challenge Club-December 21
Audit Party Weekend-January 29&30
Register at www.bivio.com/club_cafe



Finally, thank you again to all who have become our friends on Facebook. It's time for the drawing.

www.facebook.com/bivio

