PETSMART™

The Berkshire Anne Hathaways

History

- 1986- Incorporated as PetFood Warehouse
- 1989- Name change to PETsMART
- 1992- First in-store adoption center
- 1994- First in-store pet training

History (cont.)

- 1996- expanded to Canada with 8 stores
- 2002- PETsHOTELs added to two stores
- 2005- change PETsMART to PetSmart
- 2012- Celebrated 25th Anniversary, 5 millionth pet adoption

Risk Factors

- General Business Risks
  - Downturn of economic conditions
  - Damaged relationships with suppliers
  - Change in consumer preferences
  - Increase in competition in pet product suppliers
- Technology Risk
  - Failure of information systems
  - Security breach in the private information of customers or associates

Risk Factors

- Expansion Risks
  - Failure to open new locations
  - Weak entrance into new markets
  - Foreign cultural/legal differences
  - Failure to integrate acquisitions
- Pet Food and Supply Risks (Industry Specific)
  - Availability of generic products
  - Food quality, food safety, and health concerns

Risk Factors

- Specific to PetSmart
  - Failure of online sales to keep up with e-commerce competitors
  - Limits of veterinarian services
  - Anti-takeover provisions
    - 10,000,000 shares of preferred stock without stockholder approval
    - No right of stockholders to call special meetings
    - No right of stockholders to act by written consent
    - No right to cumulative voting

Recent News

- David Lenhardt replaced Joseph O'Leary
- PetSmart Promise announced continuing through 2014
- Agreement to sell Martha Stewart Pet Foods is tied up in litigation
- Announced partnership with Kelly Osbourne
- Bank of America Merrill Lynch downgraded PETM to "underperform" from neutral

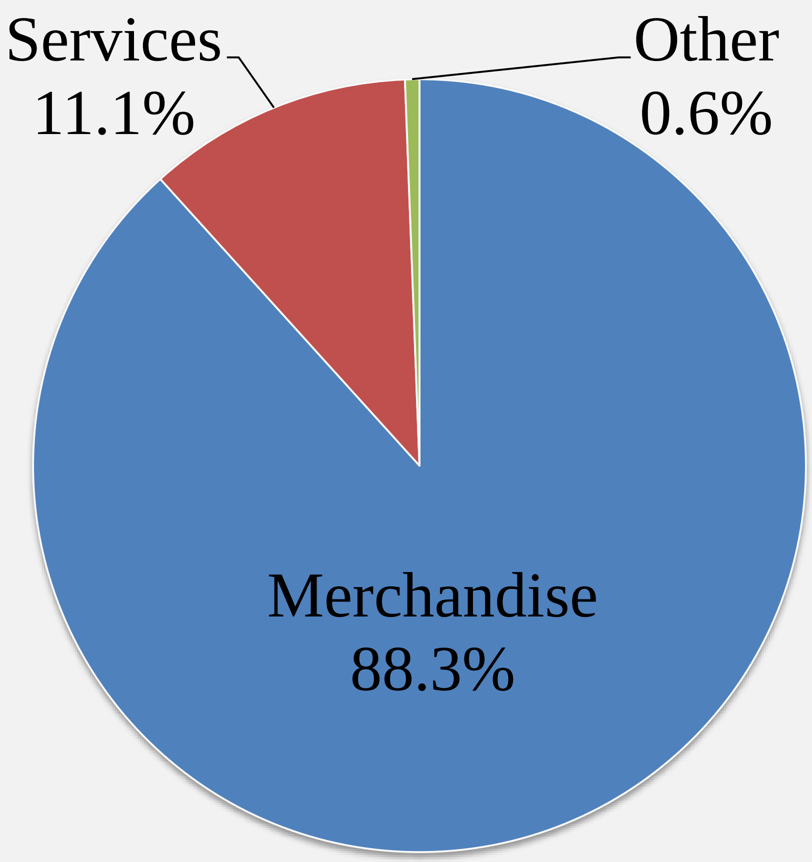
Strategy

- Connect with all pet parents in an authentic and personalized way
- Expand proprietary and exclusive products and services
- Attract and retain the most valuable customers

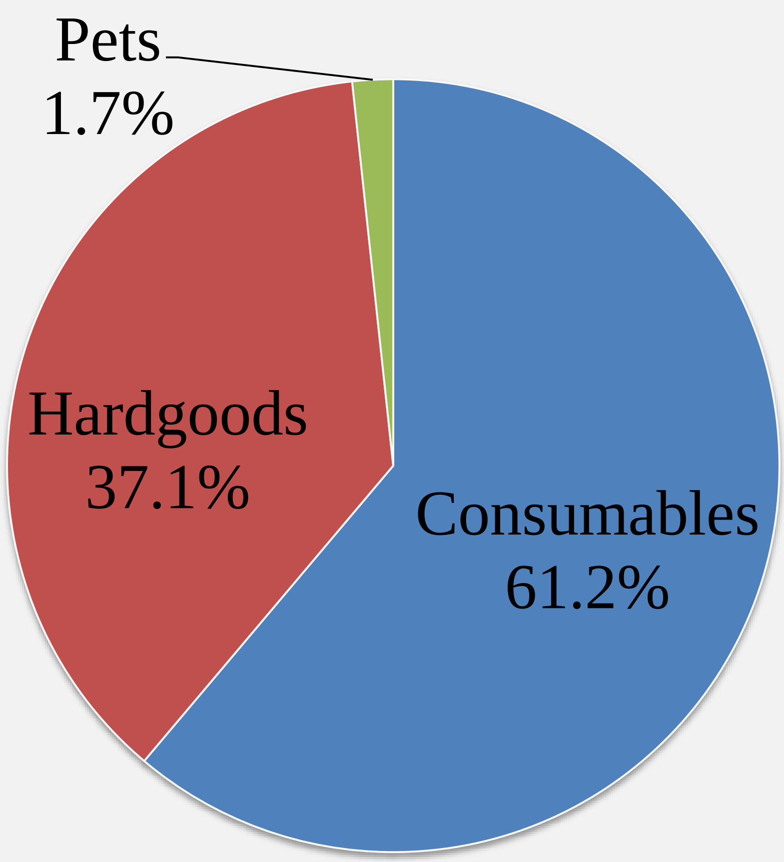
Business Model

- Merchandise
  - Consumables
  - Hardgoods
  - Pets
- Services
  - Professional room and board, day camps, and training

Revenue by Segment (2014)



Merchandise Revenue by Division (2014)



Veterinary Services

- 62% of PetSmart stores include Banfield veterinary services
- 21% investment in MMI Holdings, Inc.
  - Otherwise known as Banfield
- 2013 equity income from Banfield investment totaled $17.4 million
- Intangible value

Competitors

- PetCo
- Wal-Mart
- Amazon

Competitive Advantages

- Differentiated products
  - Exclusive brands such as *Simply Nourish* or *Top Paw*
- Availability of comprehensive veterinary care in majority of stores
  - Veterinary care also causes stickiness for PETM
- Convenient locations

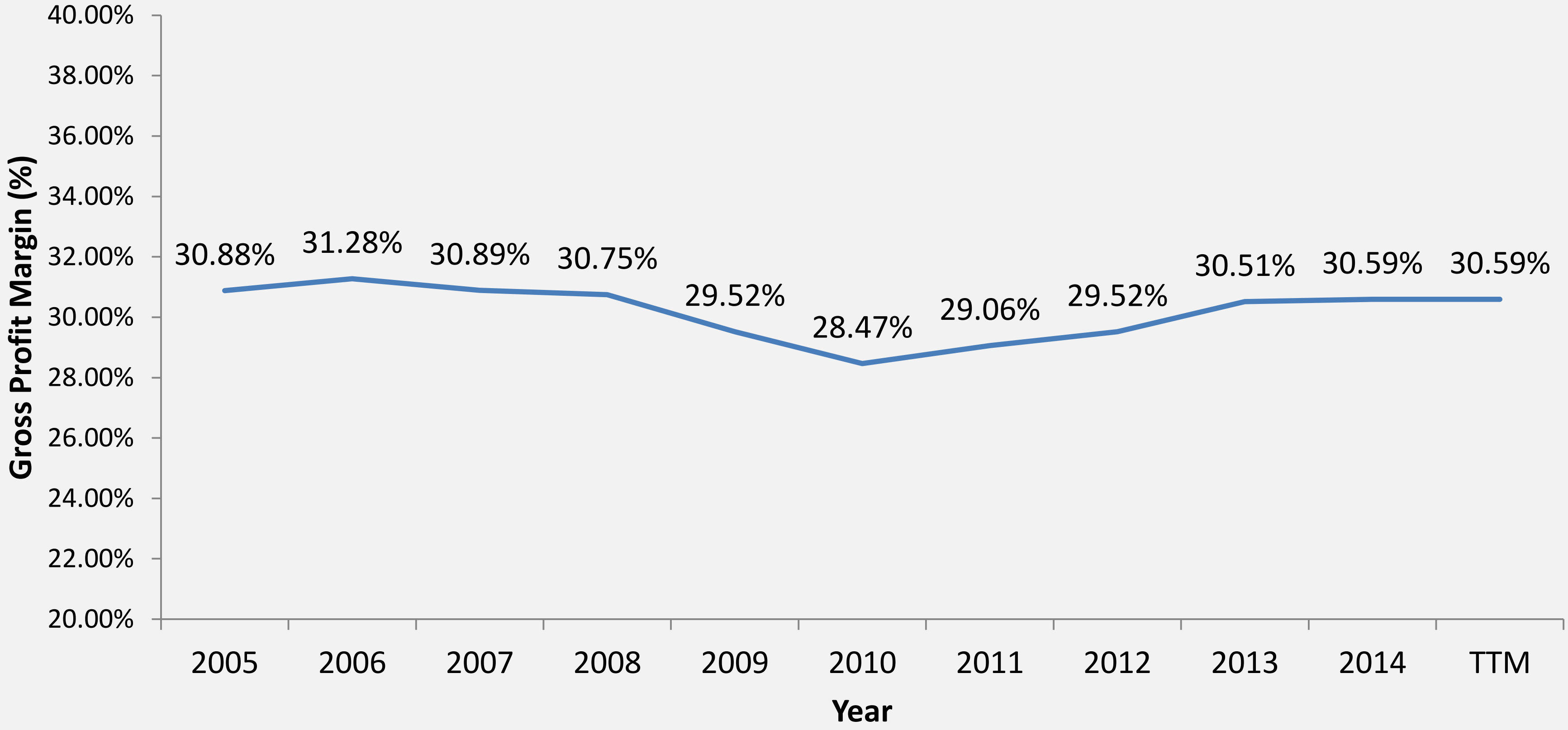
Protective Moat

- Brand recognition
- The ability to thrive in a strong economy and maintain customers in a weak economy
- Solution for pet parents
  - One-stop shop
  - Conveniently located
  - Sticky

Interpretation of Financial Statements

TTM	Value	Low Threshold	Pass?
Gross Profit Margin	30.59%	≥ 20%	Yes
% SGA	67.23%	≤ 80%	Yes
% R&D	0.00%	≤ 10%	Yes
% Depreciation	11.13%	≤ 10%	No
Interest % of OP	1.91%	≤ 15%	Yes
Net Profit Margin	6.07%	≥ 10%	No
Current Ratio	1.66	≥ 1	Yes
Obligation Ratio	8.61	< 5 years	No
Adj. Debt to Shareholder Equity	0.39	< 0.8	Yes
Return on Equity	38.35%	≥ 15%	Yes
Return on Capital	27.15%	≥ 15%	Yes
Dividend Payout Ratio	12.96%	≤ 60%	Yes
Preferred Stock	None	None	Yes
Capital Expenditures	35.00%	≤ 25%	No
Net Earning Trend	Up	Up	Yes
Retained Earnings Trend	Up	Up	Yes

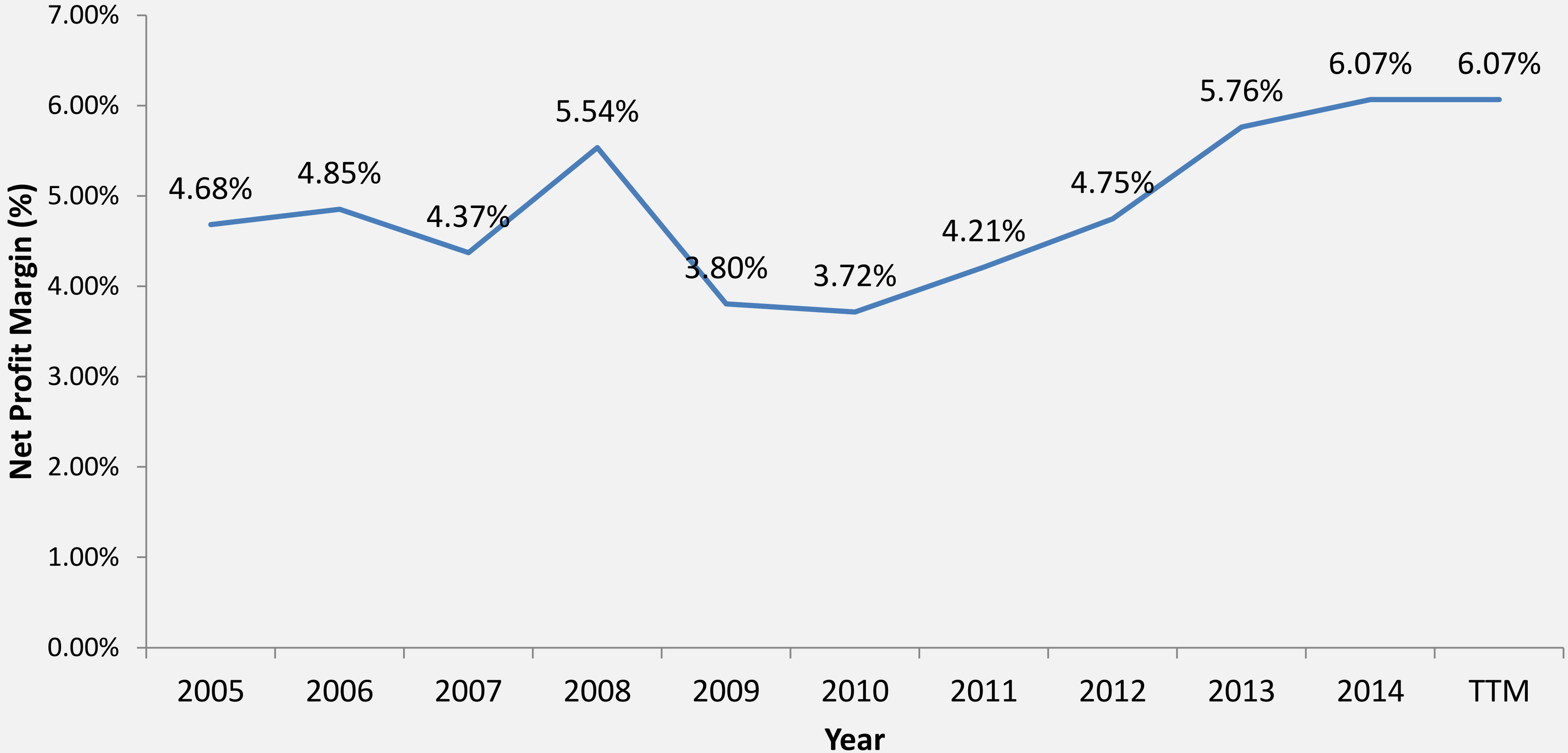
Gross Profit Margin



Gross Profit Margin as % = <u>Gross Profit($)</u>

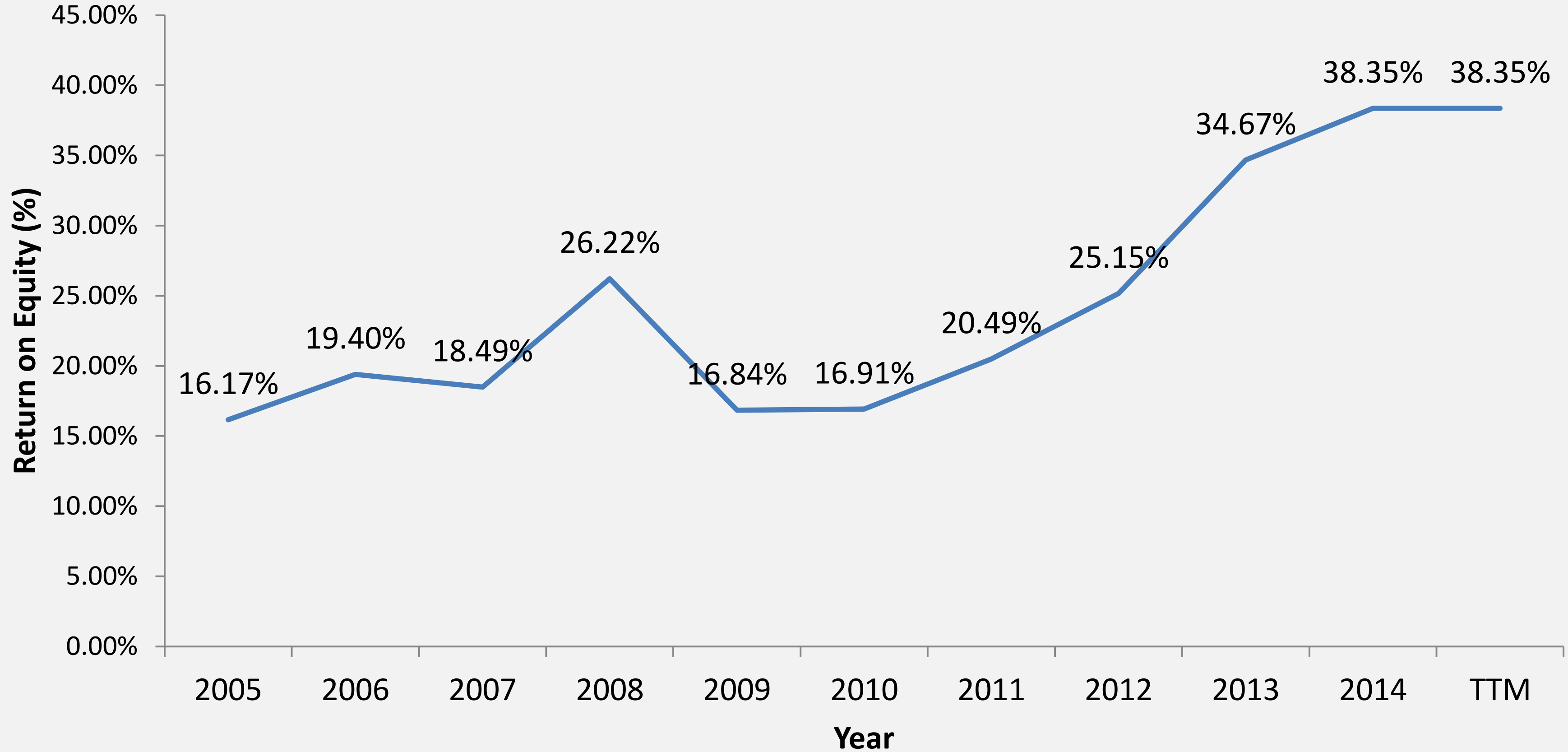
Revenue ($)

Net Profit Margin



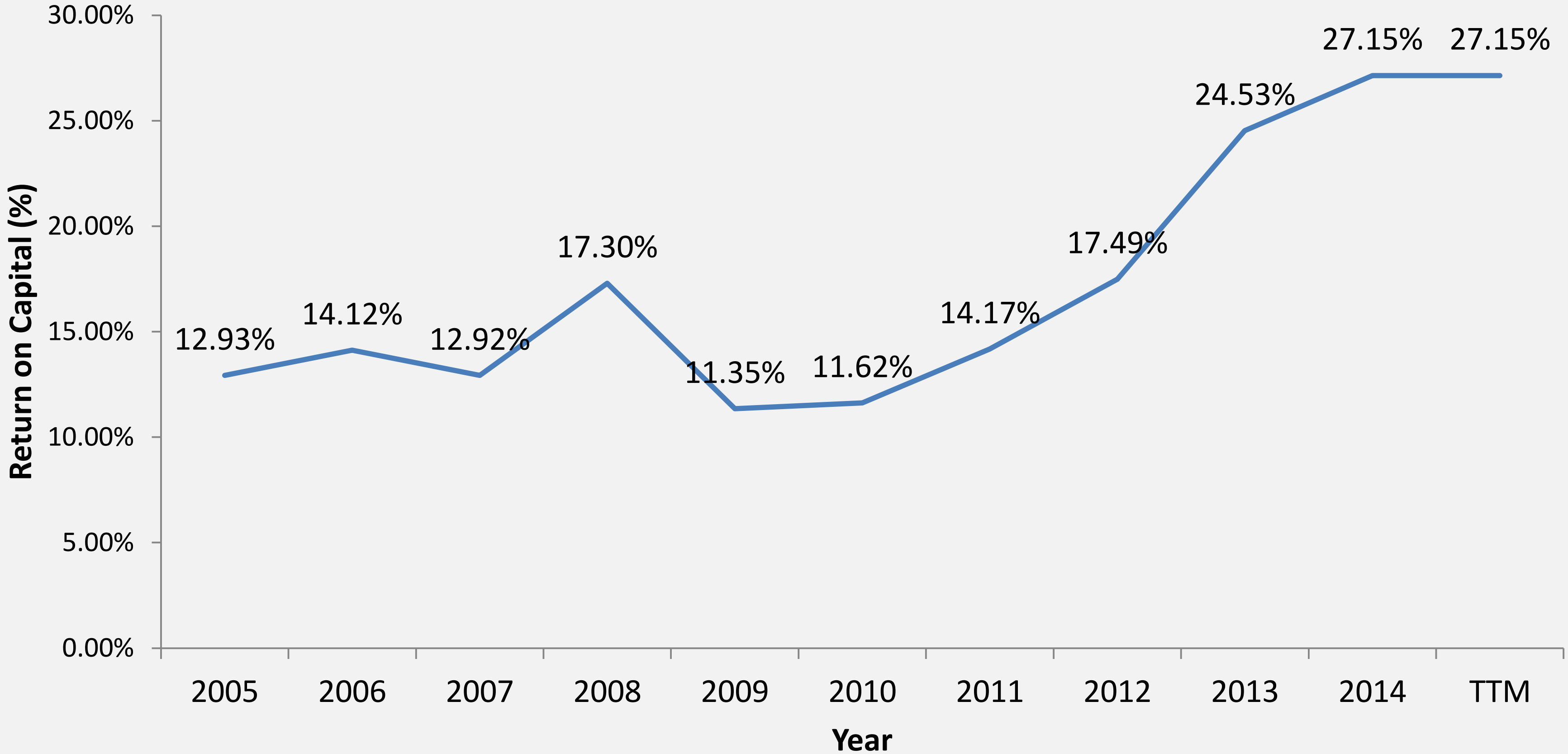
Net Profit Margin as % = Net Profit($) / Revenue ($)

Return on Equity



$$\text{Return on Equity as \% } = \frac{\text{Net Profit(\$)}}{\text{Total Equity (\$)}}$$

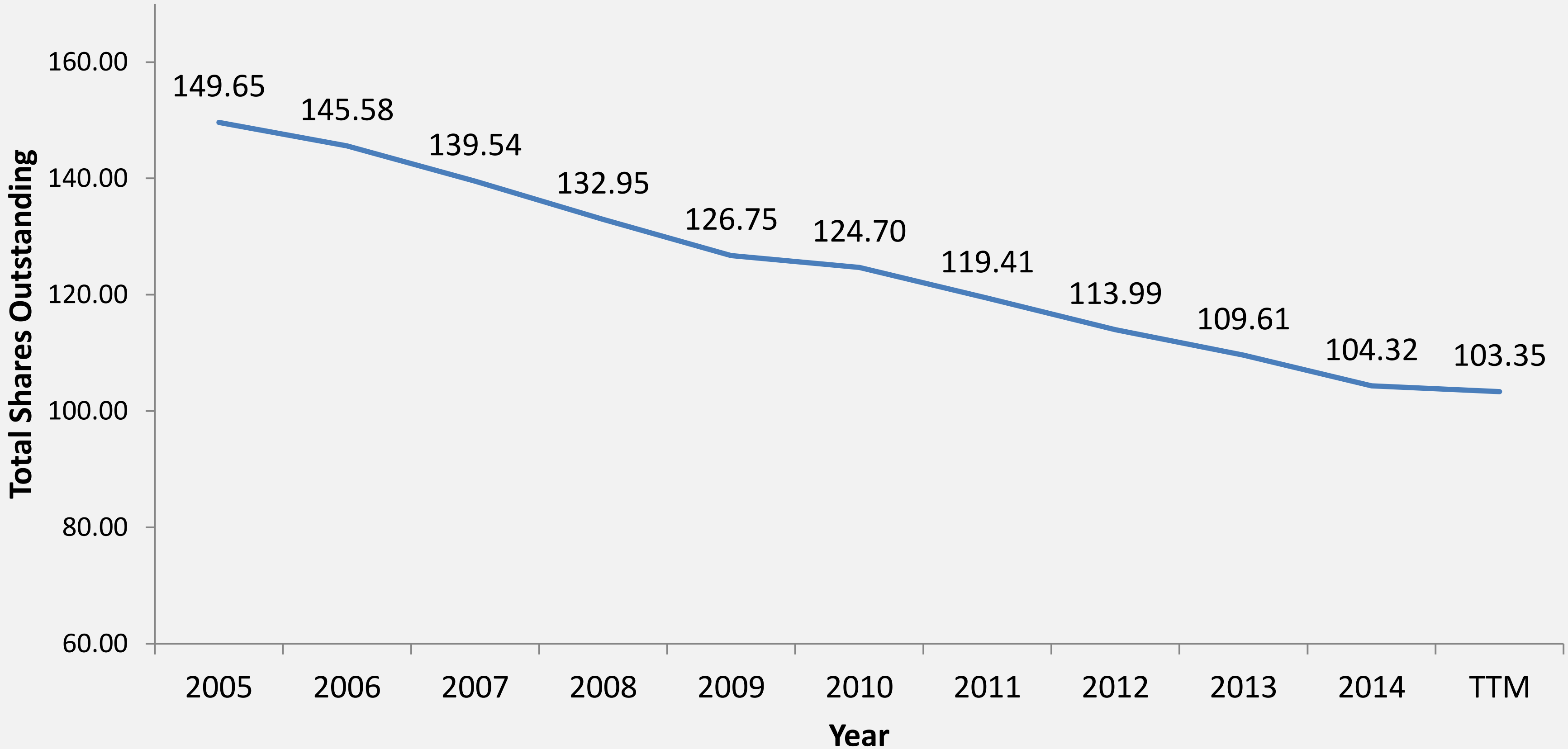
Return on Capital



Return on Capital as % = Net Profit($) / Total Equity + Long Term Debt ($)

$$\text{Return on Capital as \%} = \frac{\text{Net Profit(\$)}}{\text{Total Equity + Long Term Debt (\$)}}$$

Shares Outstanding



Millions of Shares

Earnings Per Share

Earnings Per Share=<u>Net Profit($)</u>
Total Shares Outstanding

Buffettology

Statistical Array Analysis	Increasing Trends
Sales per Share	Increasing
Cashflows per Share	Increasing
Earnings per Share	Increasing
Dividends Declared per Share	Increasing
Capital Spending per Share	Stable
Book Value per Share	Increasing
Revenues (Sales)	Increasing
Gross Profit Margin	Increasing
Operating Profit Margin	Increasing
Net Profit	Increasing
Net Profit Margin	Increasing
Retained Earnings	Increasing
Working Capital	Stable
Shareholder's Equity	Decreasing
Return on Total Capital	Increasing
Return on Shareholder's Equity	Increasing
Common Shares Outstanding	Decreasing
Long-Term Debt	Decreasing
LT Debt Payable in 5 years	No
All Dividends to Net Profit under 60%	Yes
Annual Growth Rate Analysis	Increasing

Qualitative Review

Review	
What type of business is this: commodity or sustained competitive advantage?	Sustained Competitive Advantage
Can you easily explain what the business does?	Yes
Is it heavily unionized?	No
Does it require heavy capital infusion?	Yes
Does it require lots of research and development?	No
Can inventory become obsolete?	Yes
Are there chronic "one time" write offs?	No
Is the company able to raise its prices to offset inflation?	No
Will the company be able to sell more in the future?	Yes
If I gave you $1 billion could you develop a competitor? If the answer is "no" your business has a sustained competitive advantage.	Yes

DuPont Analysis

Company	**Total Asset Turnover** (Revenue/Total Assets)	**Net Profit Margin** (Net Income/Revenue)	**Financial Leverage Multiplier** (Total Assets/Total Equity)	Return on Equity
PetSmart	2.74	0.061	2.31	38.61%
Amazon	2.15	0.004	3.52	3.03%
Wal-Mart	2.33	0.034	2.69	21.27%

Industry Comparison

Company	PetSmart	Amazon	Wal-Mart
Market Cap (Millions of $)	$6,735	$136,476	$257,559
Return on Equity	38.35%	2.81%	21.01%
Return on Assets	16.63%	0.68%	7.83%
Net Margin	6.07%	0.37%	3.36%
Operating Margin	10.02%	1.00%	5.64%
Debt to Equity	47%	53%	74%
Dividend Yield	1.10%	N/A	2.39%
Price/Earnings	17	508.8	16.1
Price/FCF	15.1	92.96	25.36
EV/EBITDA	7.43	33.92	8.45

Discounted Cash Flow- 10 year Earnings Growth

Earnings Per Share : $ 4.02

Growth Rate In the Next: 10 Years : 14.8 %

Business Predictability

Terminal Growth Rate: 4 %

Years of Terminal Growth: 10

Discount Rate: 12 %

DCF | Reverse DCF NEW

Tangible Book Value: $ 10.09 Add to Fair Value

Growth Value: $ 46.16

Terminal Value: $ 35.01

= Fair Value: $ 91.27

Margin Of Safety: 26%

Financial Data of PetSmart Inc

Annual Rates (per share)	10 yrs	5 yrs
Revenue Growth (%)	12.70	12.00
EBITDA Growth (%)	14.00	17.20
EBIT Growth (%)	15.30	23.60
Earning Growth (%)	14.80	27.40
Free Cash Flow Growth (%)	31.80	9.90

DCF- Break Even

Earnings Per Share : $ 4.02

Growth Rate In the Next: 10 Years 11.93 %

Business Predictability

Terminal Growth Rate: 4 %

Years of Terminal Growth: 10

Discount Rate: 12 %

DCF Reverse DCF NEW

Tangible Book Value: $ 10.09 Add to Fair Value

Growth Value: $ 40.06

Terminal Value: $ 27.18

= **Fair Value: $ 67.24**

Margin Of Safety: 0%

Financial Data of PetSmart Inc

Annual Rates (per share)	10 yrs	5 yrs
Revenue Growth (%)	12.70	12.00
EBITDA Growth (%)	14.00	17.20
EBIT Growth (%)	15.30	23.60
Earning Growth (%)	14.80	27.40
Free Cash Flow Growth (%)	31.80	9.90

DCF- Break Even 2

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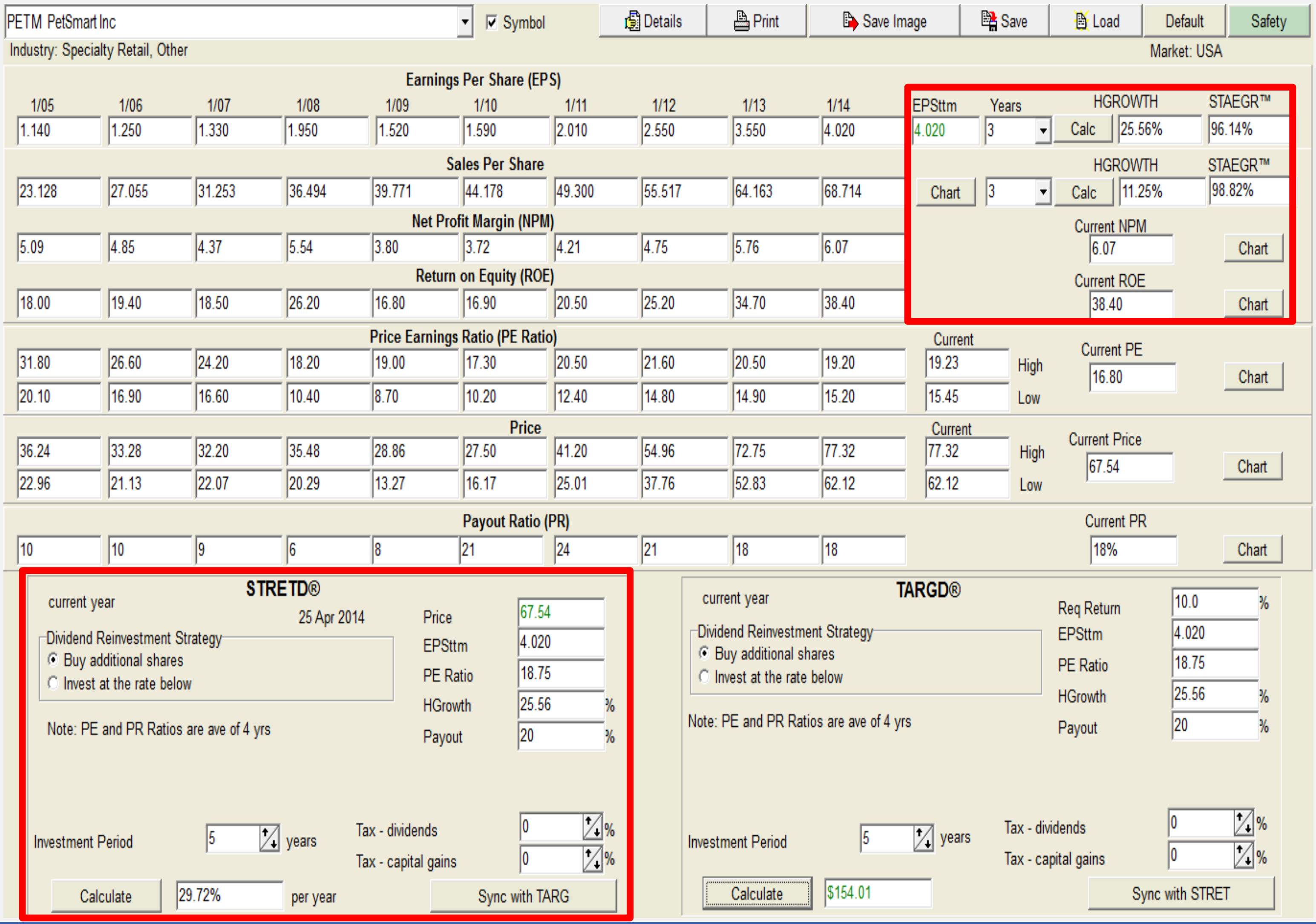
Conscious Investor- 3-year Default


PETM PetSmart Inc ☑ Symbol | Details | Print | Save Image | Save | Load | Default | Safety

Industry: Specialty Retail, Other — Market: USA

Earnings Per Share (EPS)

1/05	1/06	1/07	1/08	1/09	1/10	1/11	1/12	1/13	1/14
1.140	1.250	1.330	1.950	1.520	1.590	2.010	2.550	3.550	4.020

EPSttm	Years		HGROWTH	STAEGR™
4.020	3	Calc	25.56%	96.14%

Sales Per Share

23.128	27.055	31.253	36.494	39.771	44.178	49.300	55.517	64.163	68.714

	Years		HGROWTH	STAEGR™
Chart	3	Calc	11.25%	98.82%

Net Profit Margin (NPM)

5.09	4.85	4.37	5.54	3.80	3.72	4.21	4.75	5.76	6.07

Current NPM 6.07 Chart

Return on Equity (ROE)

18.00	19.40	18.50	26.20	16.80	16.90	20.50	25.20	34.70	38.40

Current ROE 38.40 Chart

Price Earnings Ratio (PE Ratio)

										Current	
31.80	26.60	24.20	18.20	19.00	17.30	20.50	21.60	20.50	19.20	19.23	High
20.10	16.90	16.60	10.40	8.70	10.20	12.40	14.80	14.90	15.20	15.45	Low

Current PE 16.80 Chart

Price

										Current	
36.24	33.28	32.20	35.48	28.86	27.50	41.20	54.96	72.75	77.32	77.32	High
22.96	21.13	22.07	20.29	13.27	16.17	25.01	37.76	52.83	62.12	62.12	Low

Current Price 67.54 Chart

Payout Ratio (PR)

10	10	9	6	8	21	24	21	18	18

Current PR 18% Chart

STRETD®

current year 25 Apr 2014

Dividend Reinvestment Strategy
- ◉ Buy additional shares
- ○ Invest at the rate below

Note: PE and PR Ratios are ave of 4 yrs

Price	67.54
EPSttm	4.020
PE Ratio	18.75
HGrowth	25.56 %
Payout	20 %

Investment Period 5 years — Tax - dividends 0 % — Tax - capital gains 0 %

Calculate 29.72% per year — Sync with TARG

TARGD®

current year

Dividend Reinvestment Strategy
- ◉ Buy additional shares
- ○ Invest at the rate below

Note: PE and PR Ratios are ave of 4 yrs

Req Return	10.0 %
EPSttm	4.020
PE Ratio	18.75
HGrowth	25.56 %
Payout	20 %

Investment Period 5 years — Tax - dividends 0 % — Tax - capital gains 0 %

Calculate $154.01 — Sync with STRET

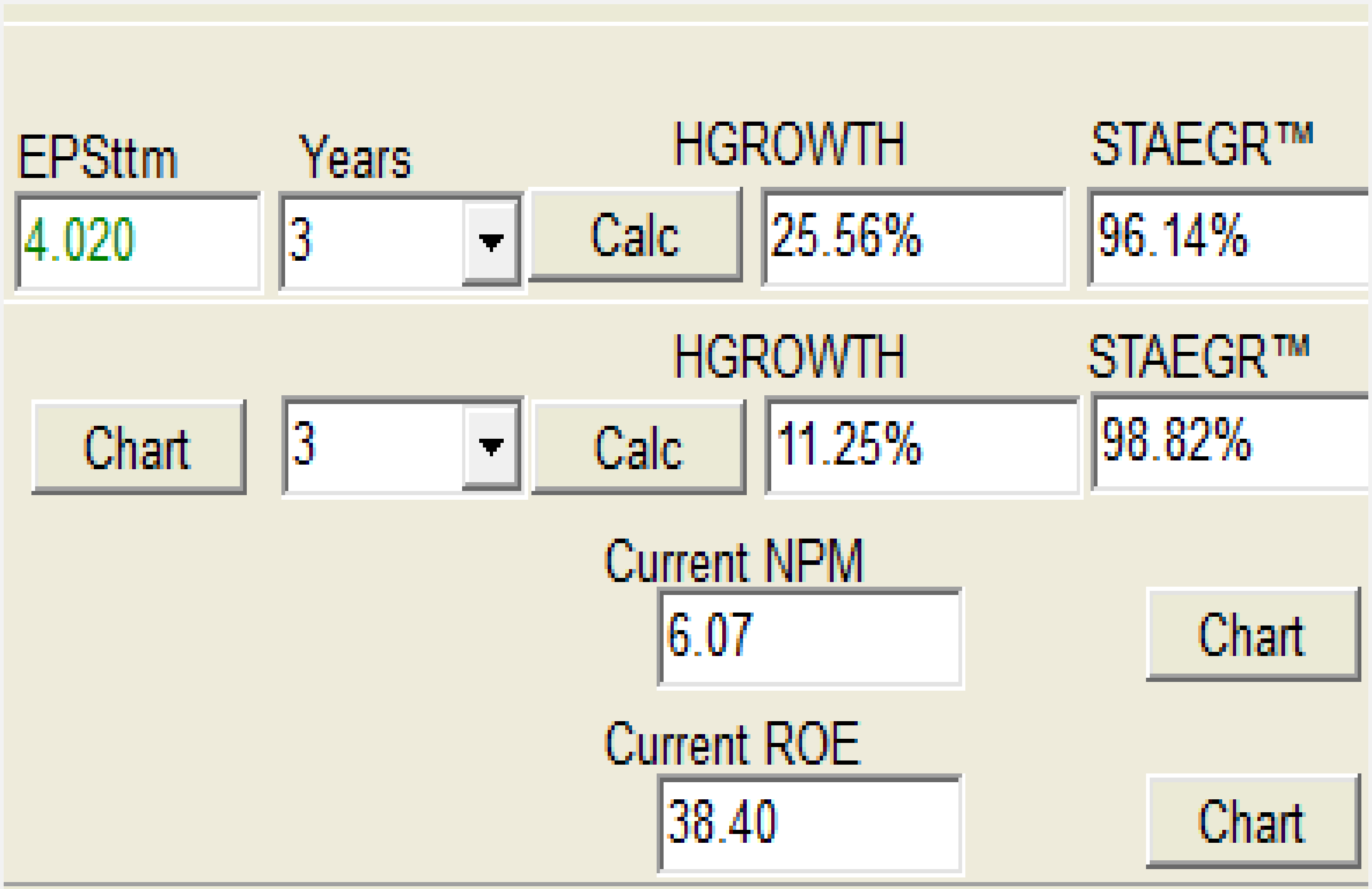

EPSttm
4.020
Years
3
Calc
HGROWTH
25.56%
STAEGR™
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Chart
3
Calc
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11.25%
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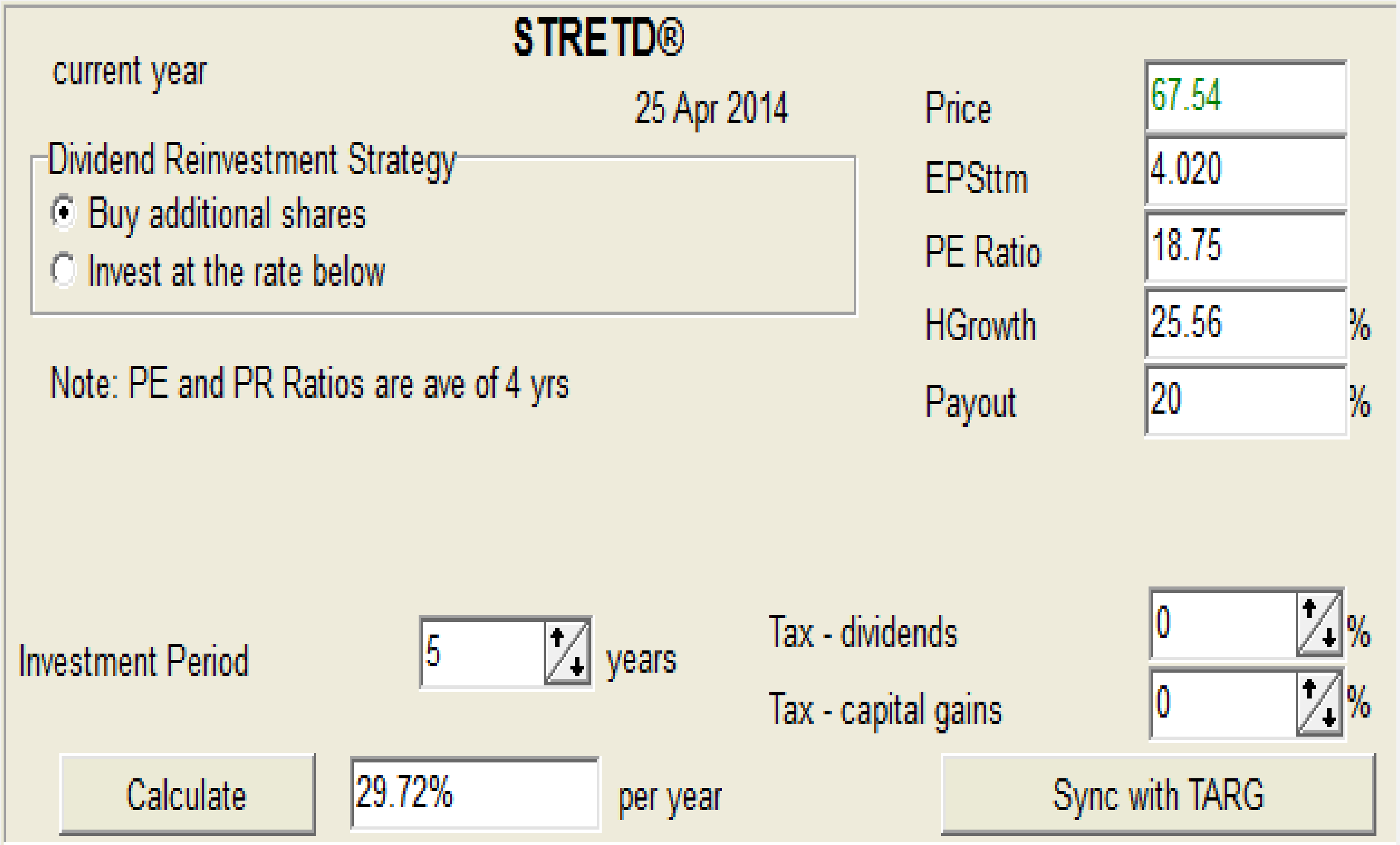
98.82%
Current NPM
6.07
Chart
Current ROE
38.40
Chart


STRETD®
current year
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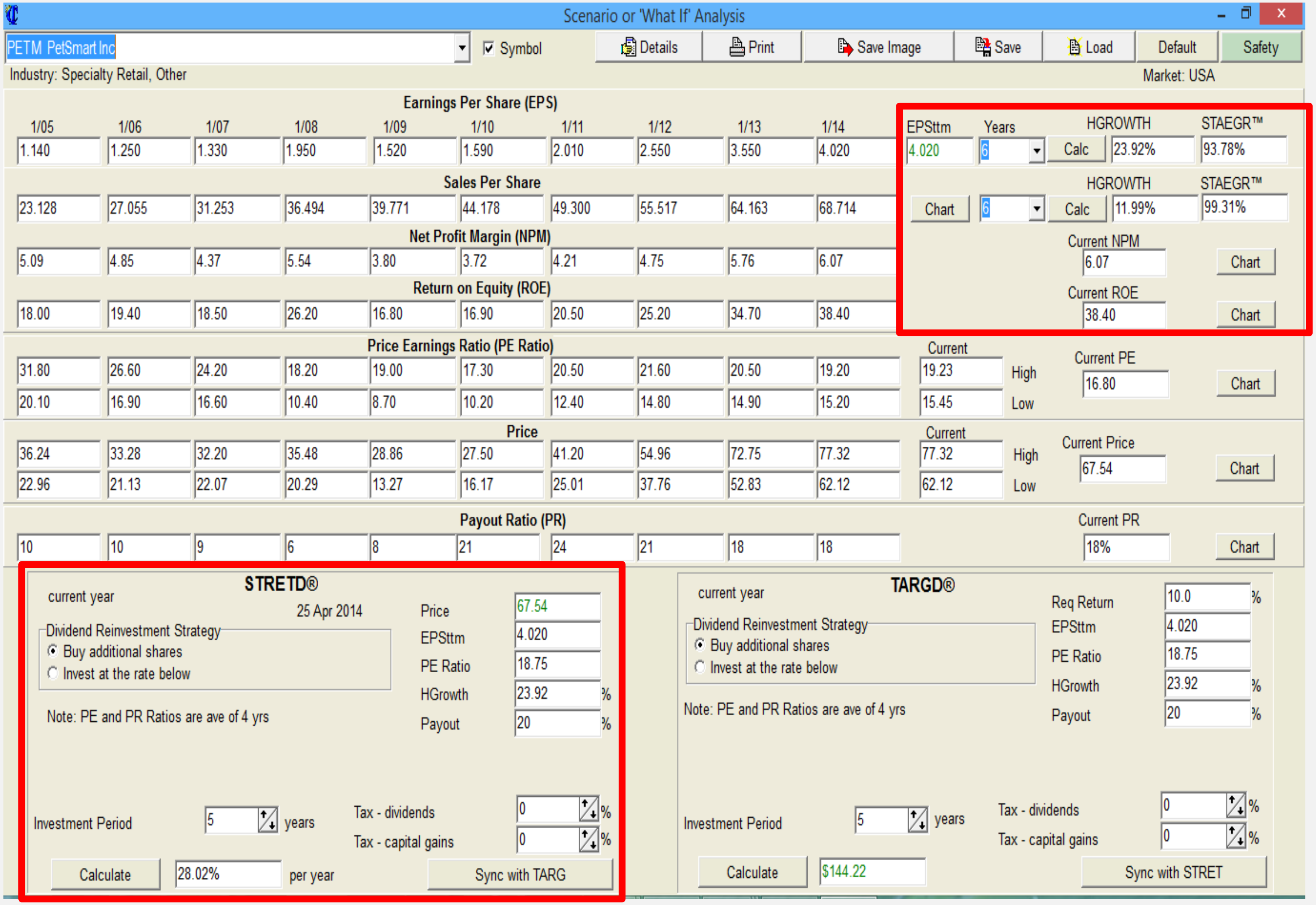
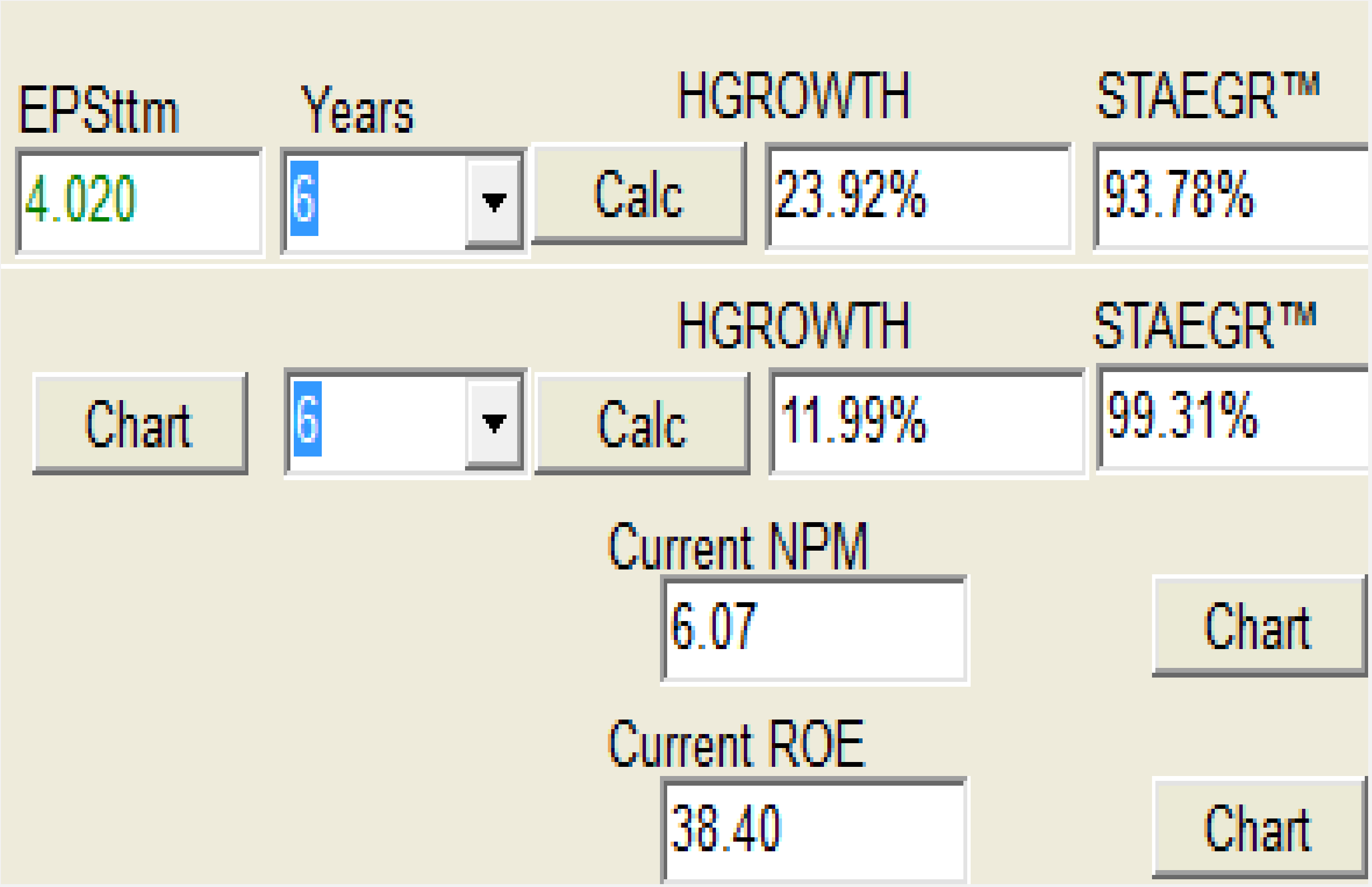
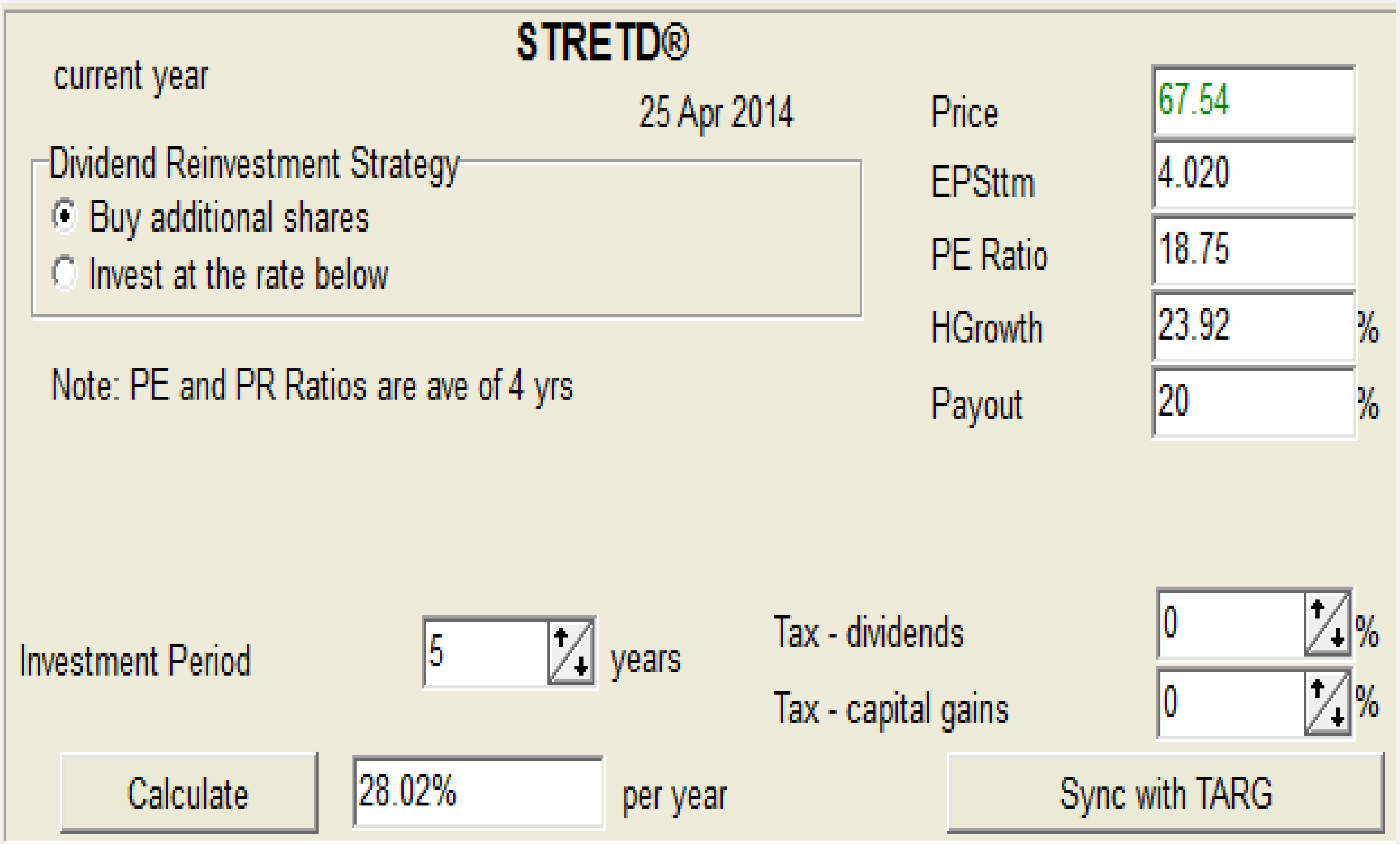
EPSttm 4.020
PE Ratio 18.75
HGrowth 25.56 %
Payout 20 %
Investment Period 5 years
Tax - dividends 0 %
Tax - capital gains 0 %
Calculate
29.72% per year
Sync with TARG

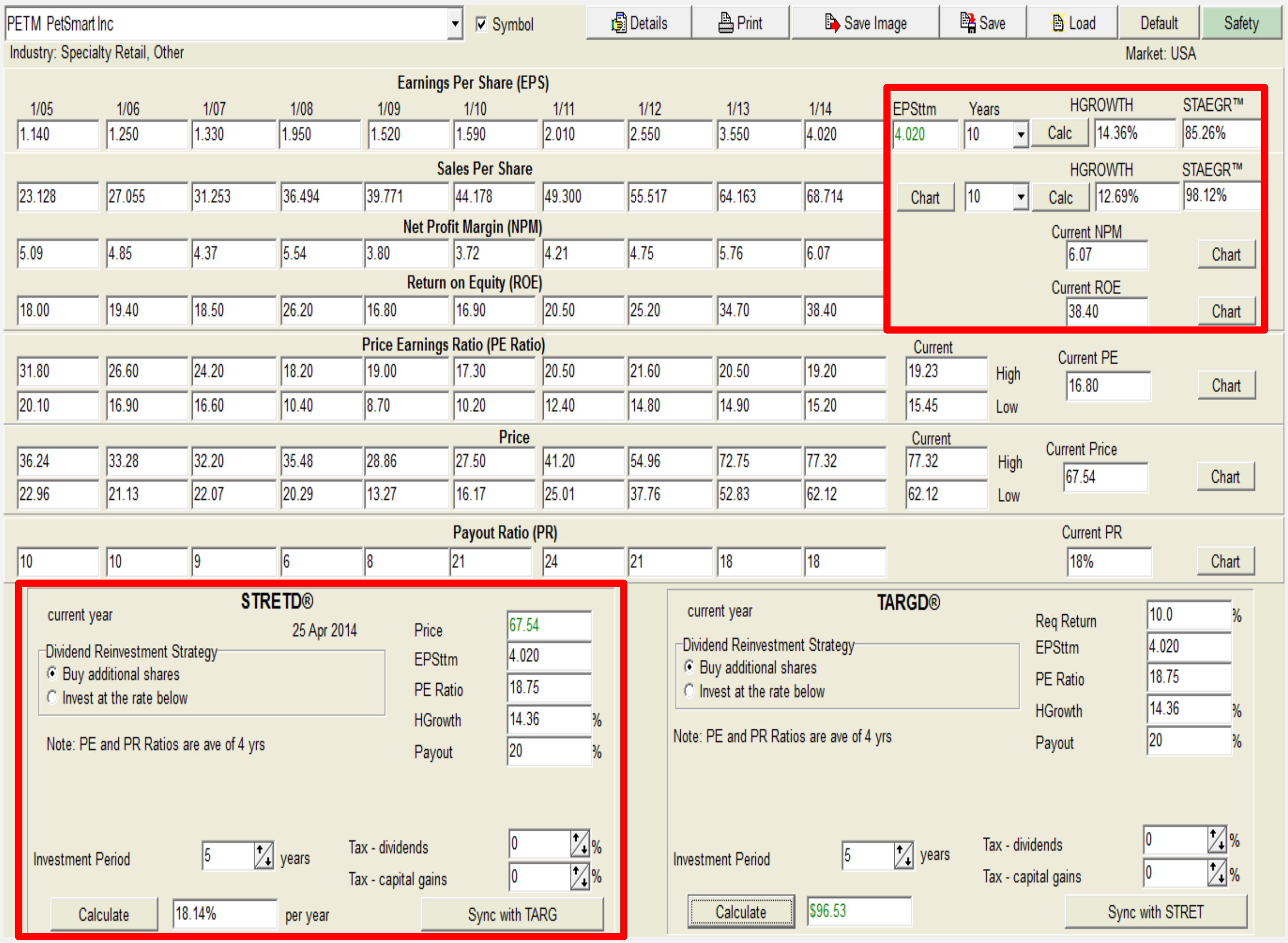
CI- 6-Year Default

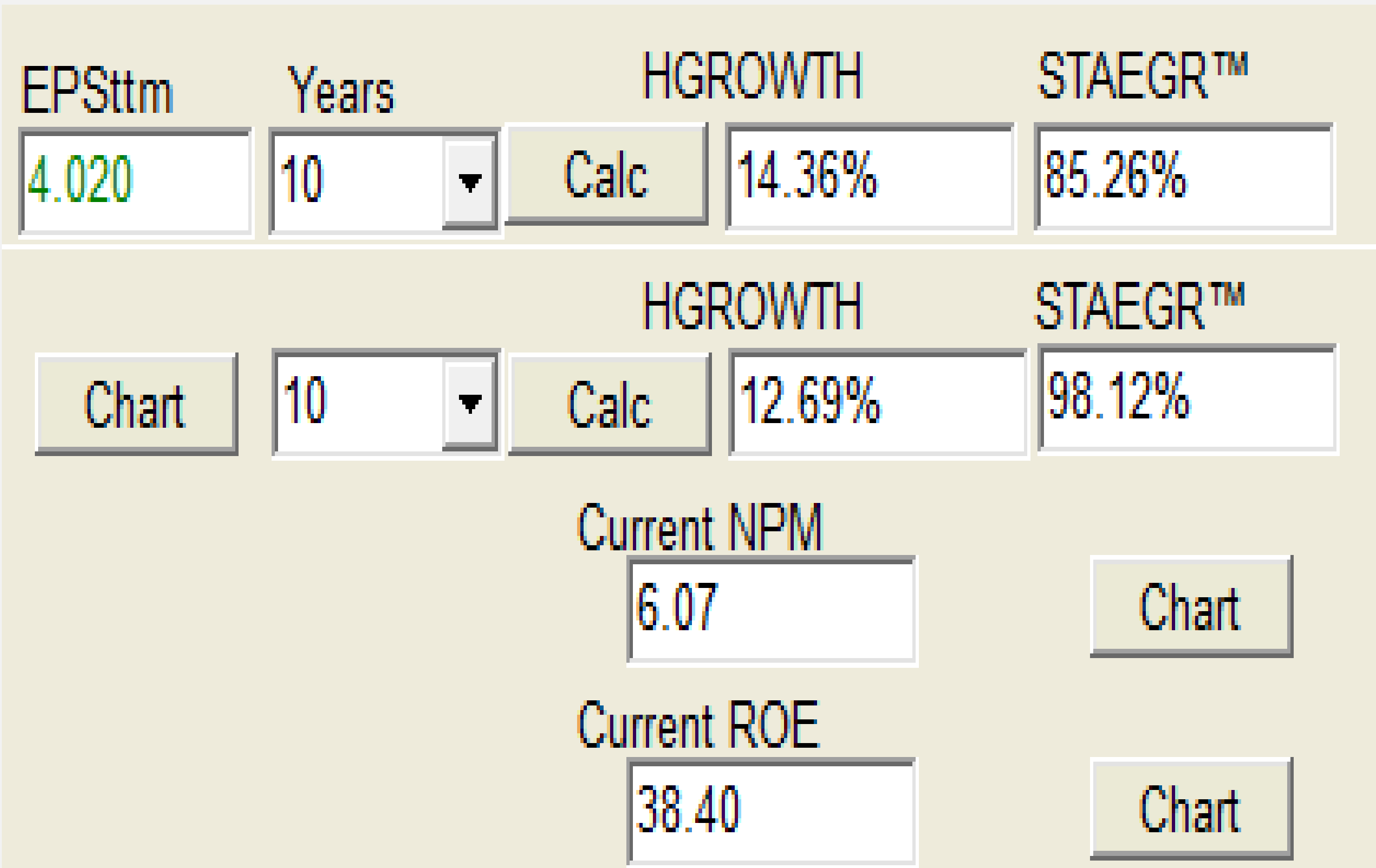


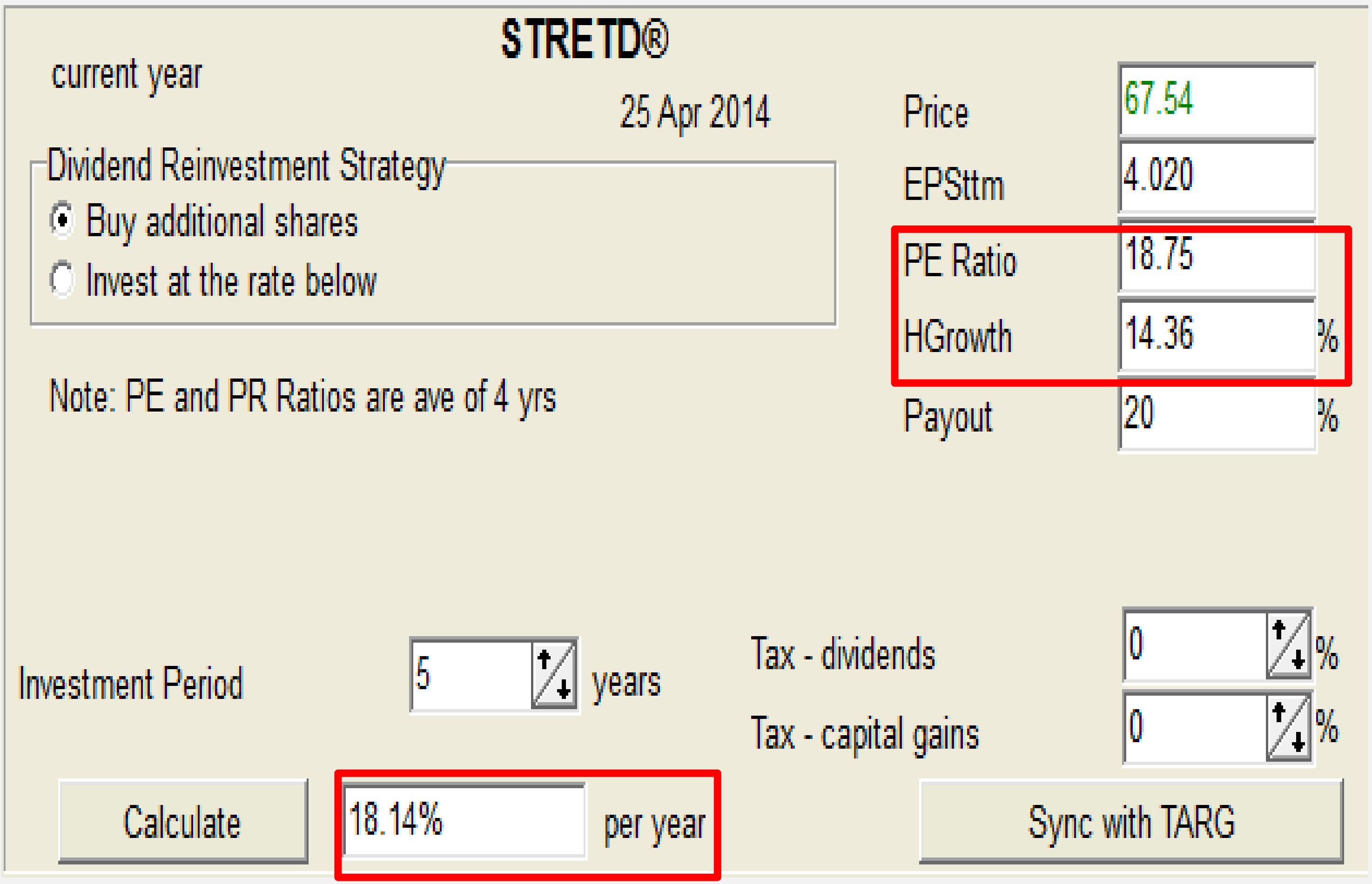

EPSttm
4.020
Years
6
Calc
HGROWTH
23.92%
STAEGR™
93.78%
Chart
6
Calc
HGROWTH
11.99%
STAEGR™
99.31%
Current NPM
6.07
Chart
Current ROE
38.40
Chart


STRETD®
current year
25 Apr 2014
Dividend Reinvestment Strategy
Buy additional shares
Invest at the rate below
Note: PE and PR Ratios are ave of 4 yrs
Price
67.54
EPSttm
4.020
PE Ratio
18.75
HGrowth
23.92 %
Payout
20 %
Investment Period
5 years
Tax - dividends
0 %
Tax - capital gains
0 %
Calculate
28.02% per year
Sync with TARG

CI- 10-Year Default




EPSttm
Years
HGROWTH
STAEGR™
4.020
10
Calc
14.36%
85.26%
HGROWTH
STAEGR™
Chart
10
Calc
12.69%
98.12%
Current NPM
6.07
Chart
Current ROE
38.40
Chart


STRETD®
current year
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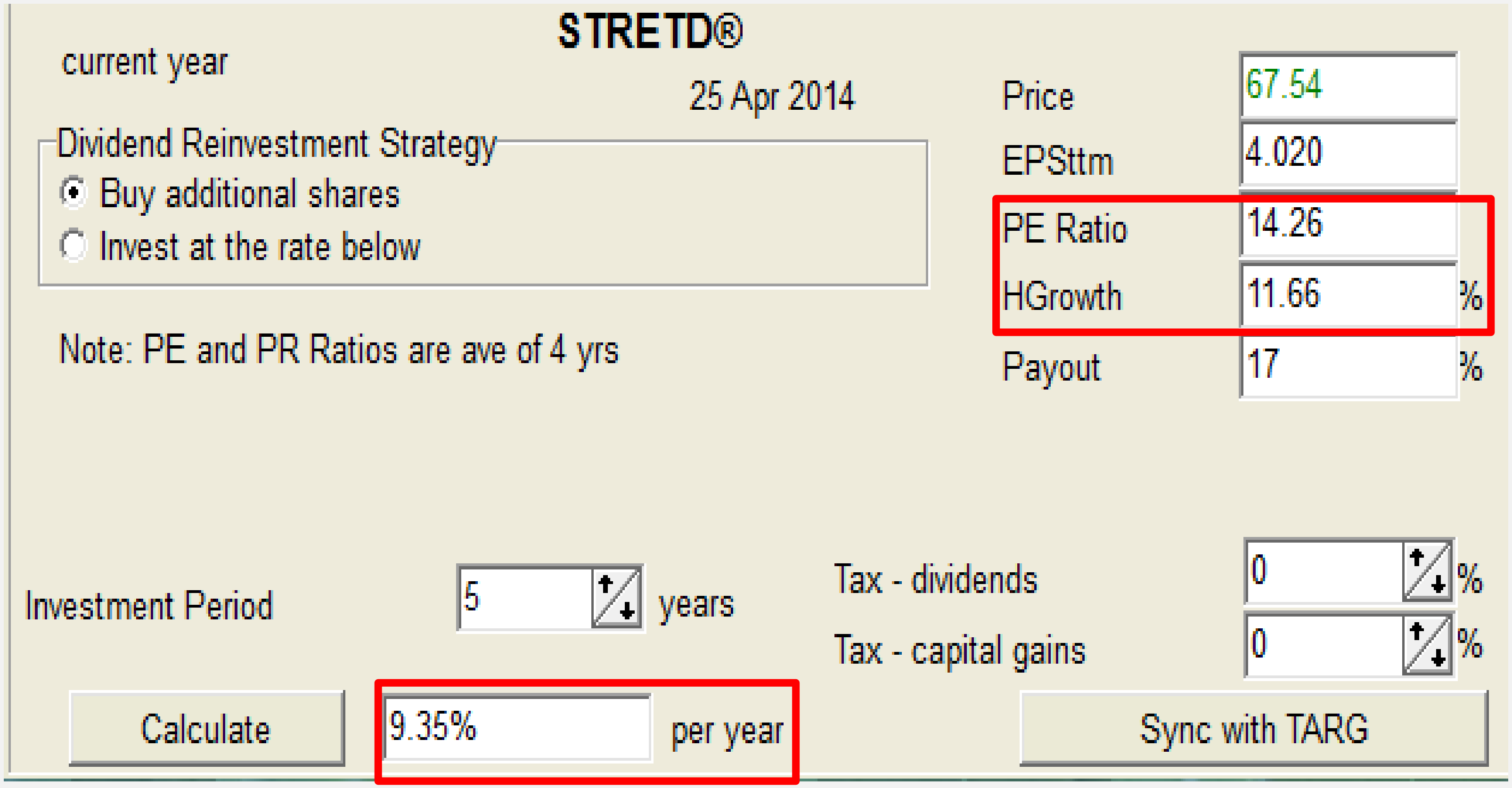
Price
67.54
EPSttm
4.020
PE Ratio
18.75
HGrowth
14.36
%
Payout
20
%
Investment Period
5
years
Tax - dividends
0
%
Tax - capital gains
0
%
Calculate
18.14%
per year
Sync with TARG

CI- Safety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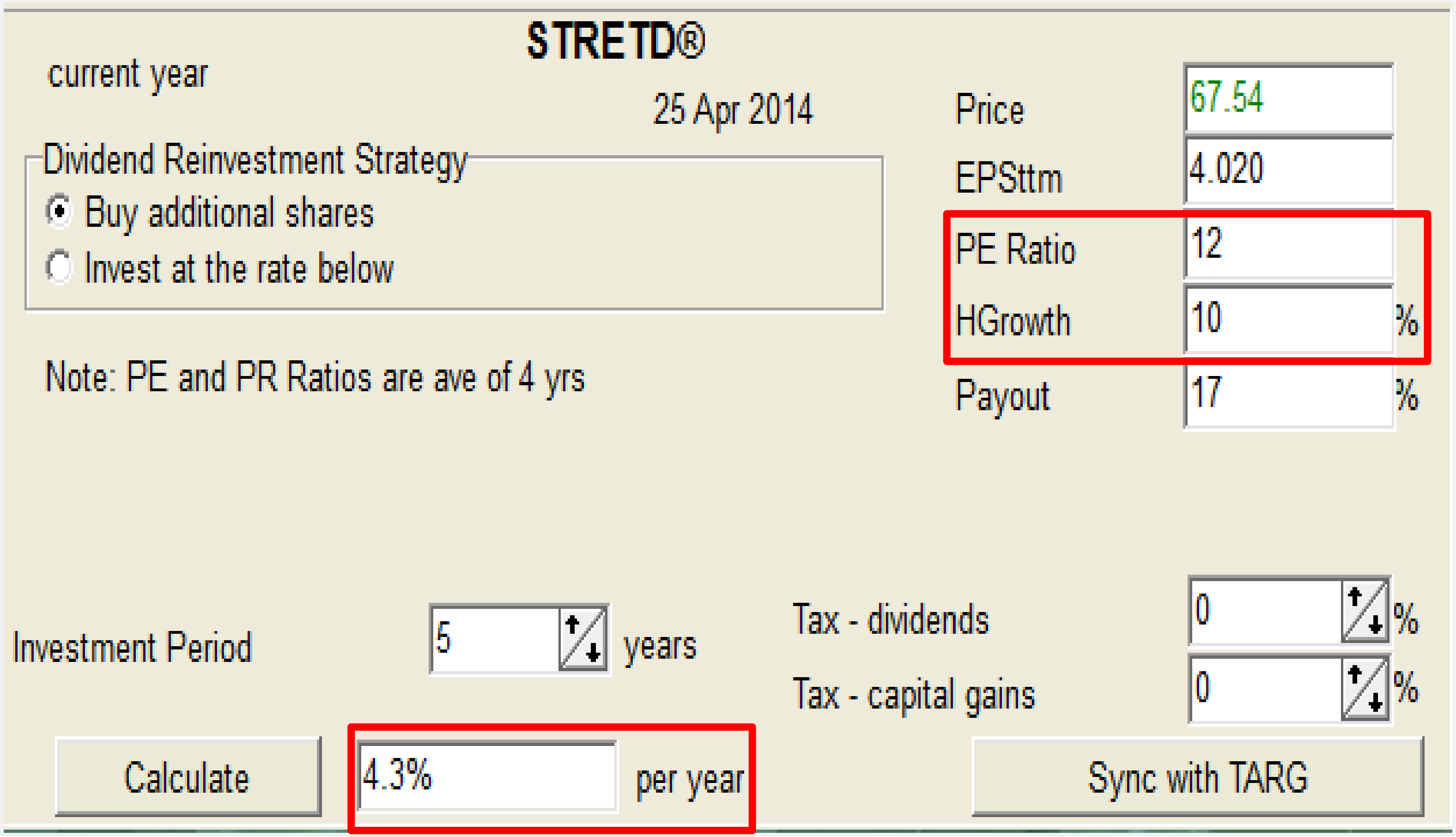
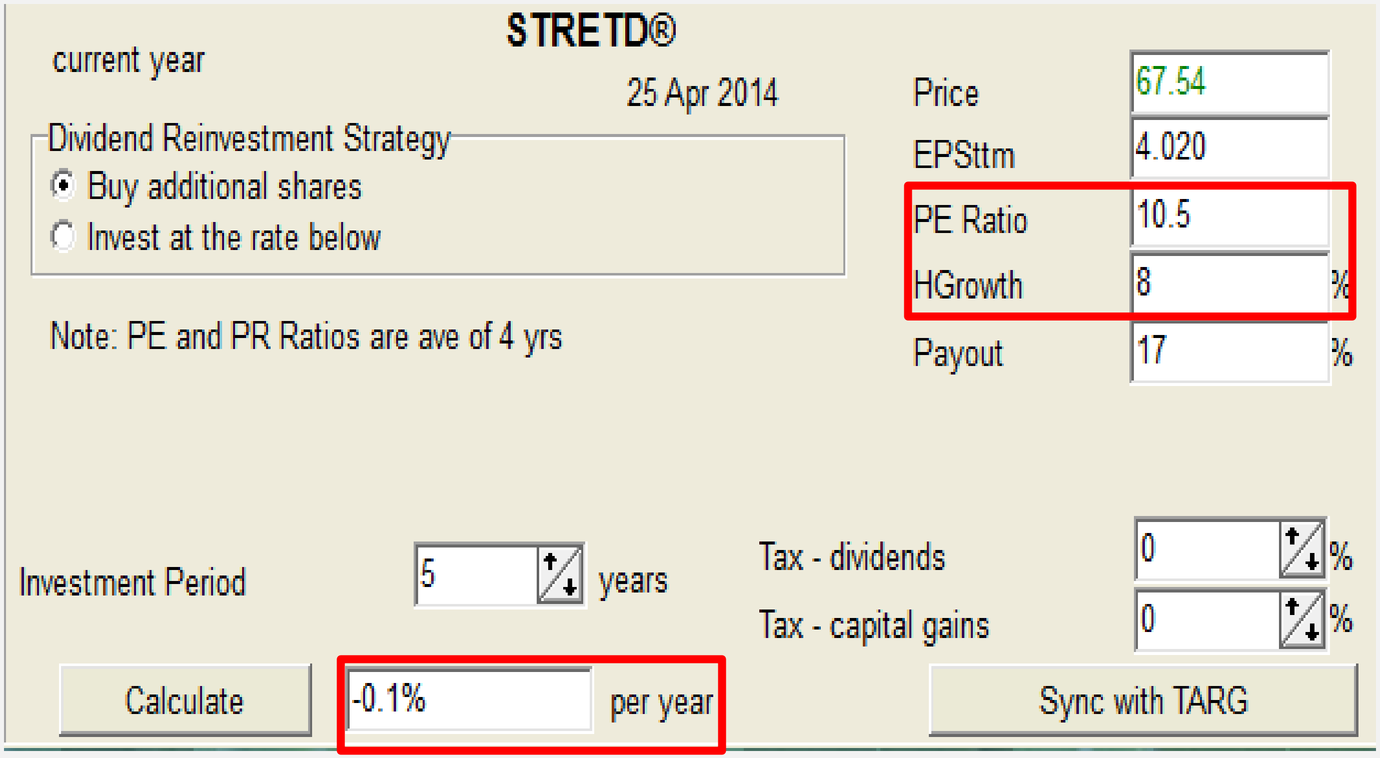
Price
67.54
EPSttm
4.020
PE Ratio
14.26
HGrowth
11.66
%
Payout
17
%
Investment Period
5
years
Tax - dividends
0
%
Tax - capital gains
0
%
Calculate
9.35%
per year
Sync with TARG

CI- Kill It


STRETD®
current year
25 Apr 2014
Dividend Reinvestment Strategy
Buy additional shares
Invest at the rate below
Note: PE and PR Ratios are ave of 4 yrs
Price
67.54
EPSttm
4.020
PE Ratio
12
HGrowth
10
%
Payout
17
%
Investment Period
5
years
Tax - dividends
0
%
Tax - capital gains
0
%
Calculate
4.3%
per year
Sync with TARG

CI- Kill It Again



Debt Analysis

- $100 million revolving credit agreement expires on March 23, 2017.
- $100 million Stand alone letter credit agreement expires on March 23, 2017.
- Total Debt $518.5 mill.
    - Long-term debt $451.6 million
    - Due in next 5 Yrs $313.0 million

Intra-Portfolio Valuations

Price/Sales

Ticker	P... Sales
AIG-WT	-
BBY	0.2
CTB	0.5
WMT	0.6
CHRW	0.7
WAG	0.9
PETM	1.0
AIG	1.1
BBBY	1.2
AAP	1.4
WRLD	1.6
BRK.B	1.6
PEP	2.0
IBM	2.1
NSRGY	2.3
BDX	2.7
LO	2.9
MDT	3.5
KO	4.0
MSFT	4.1
ORCL	4.9

Price/Free Cash Flow

Ticker	Price / Cash Fl...
AIG-WT	-
WRLD	3.9
CTB	6.0
BBY	8.1
BRK.B	10.8
WMT	11.3
BBBY	11.4
PETM	11.6
BDX	11.9
IBM	12.2
MSFT	12.2
MDT	12.3
ORCL	12.4
AIG	13.2
NSRGY	14.4
PEP	14.7
AAP	16.3
LO	17.1
WAG	17.3
KO	17.6
CHRW	25.5

Enterprise Value/EBITDA

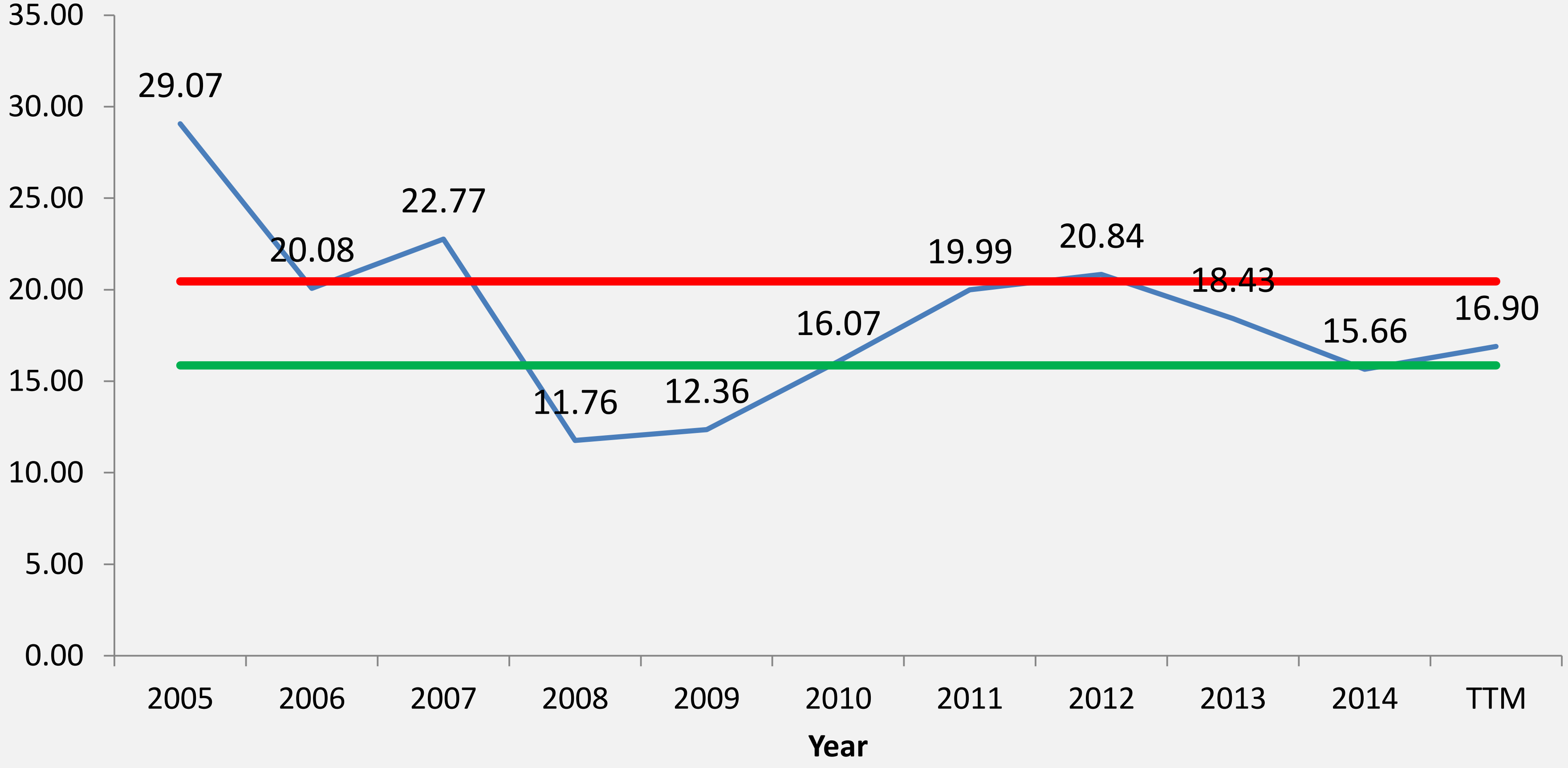
Ticker	EV / EBITDA
AIG-WT	-
BBY	4.7
CTB	5.2
BBBY	7.0
MSFT	8.3
WRLD	8.4
PETM	8.9
AIG	9.2
ORCL	9.4
WMT	9.7
IBM	10.2
LO	10.5
MDT	11.1
AAP	11.3
BRK.B	11.3
CHRW	13.0
WAG	13.1
PEP	13.8
NSRGY	14.9
BDX	15.0
KO	17.2

52-week Price Range

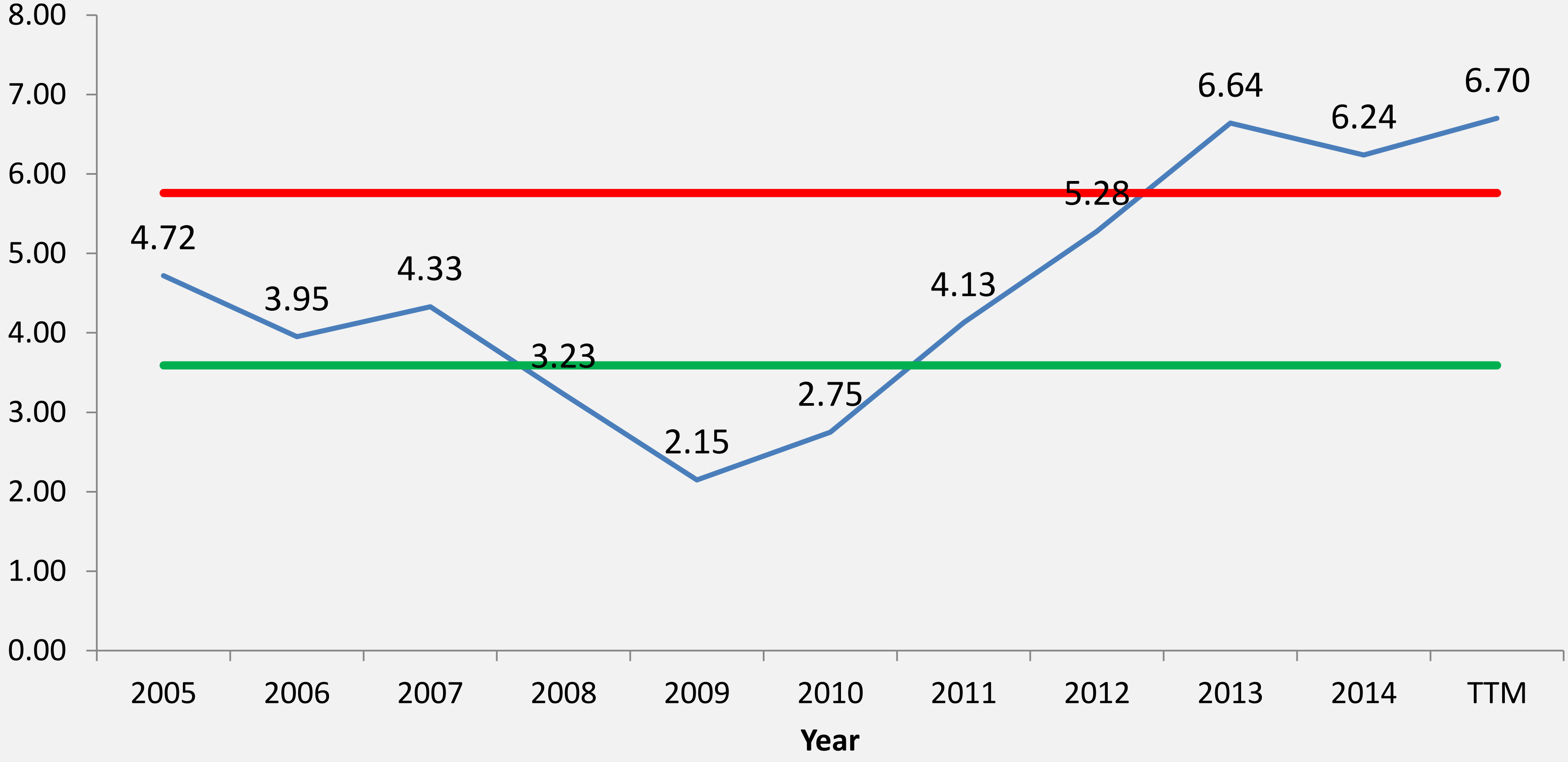
Ticker	52-wk Range	
BBBY	$62.12	$80.82
BBY	$22.15	$44.66
WRLD	$71.58	$107.98
CTB	$20.55	$34.80
PETM	$62.12	$77.32
CHRW	$50.21	$62.46
IBM	$172.19	$211.98
KO	$36.83	$43.43
MDT	$46.17	$62.90
BDX	$93.31	$118.77
AAP	$78.91	$129.99
WMT	$71.51	$81.37
ORCL	$29.86	$42.00
NSRGY	$63.38	$78.05
LO	$41.56	$56.85
AIG	$40.37	$53.33
WAG	$43.31	$69.84
MSFT	$30.84	$41.66
PEP	$77.01	$87.06
BRK.B	$105.63	$127.96
AIG-WT	$16.75	$21.78

Van Den Berg Metrics

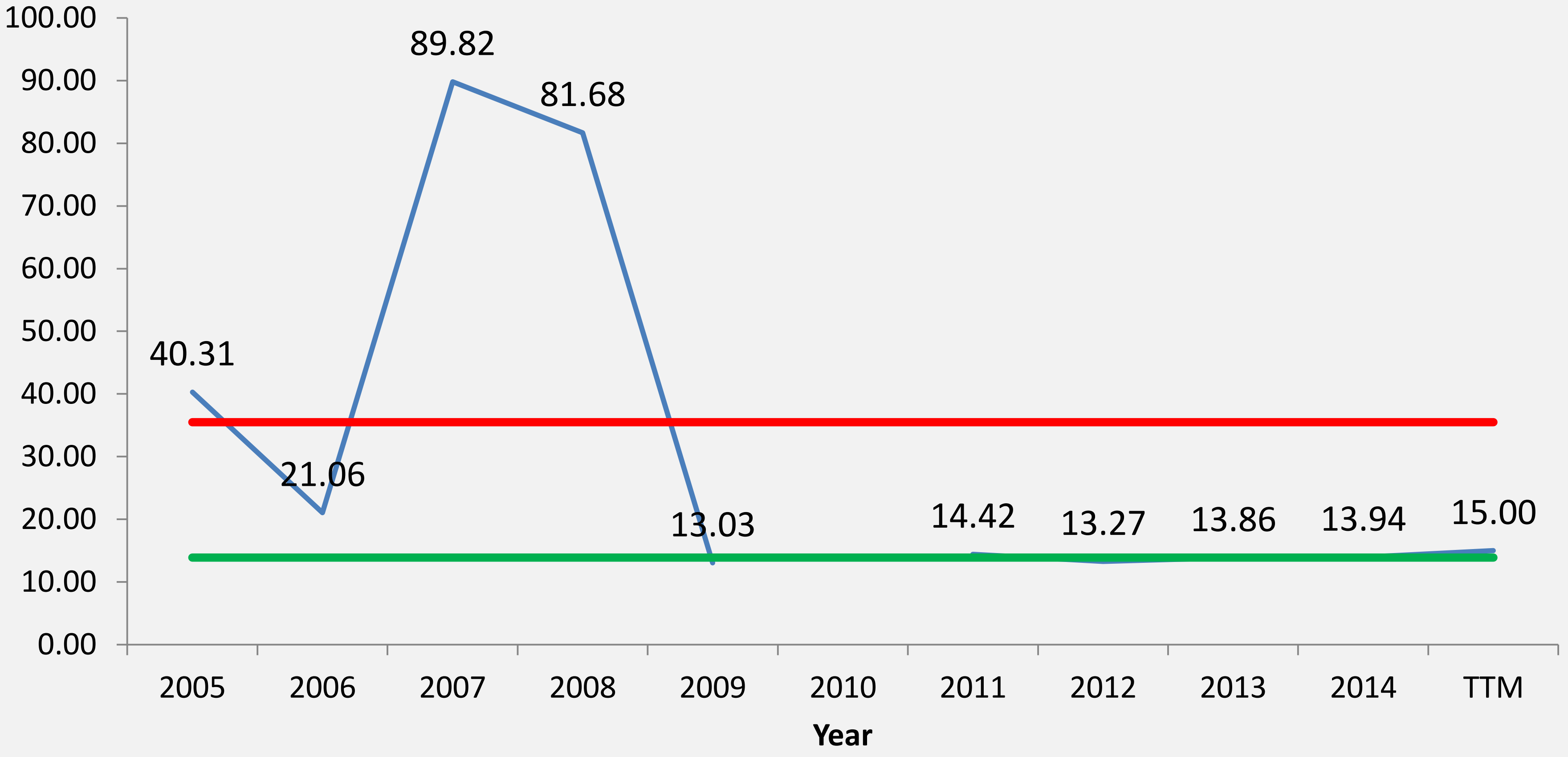
Price/Earnings



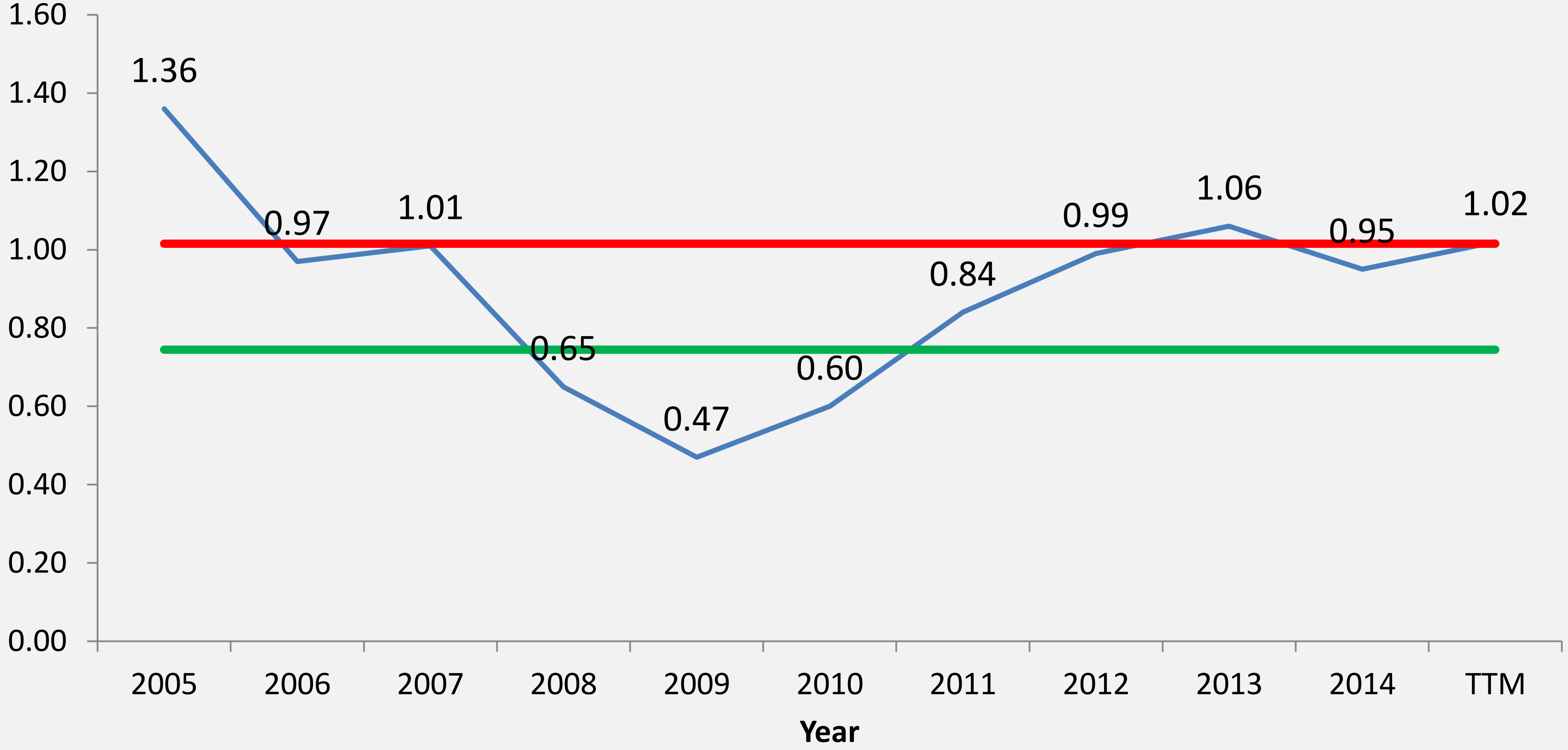
Price/Tangible Book



Price/Free Cash Flow

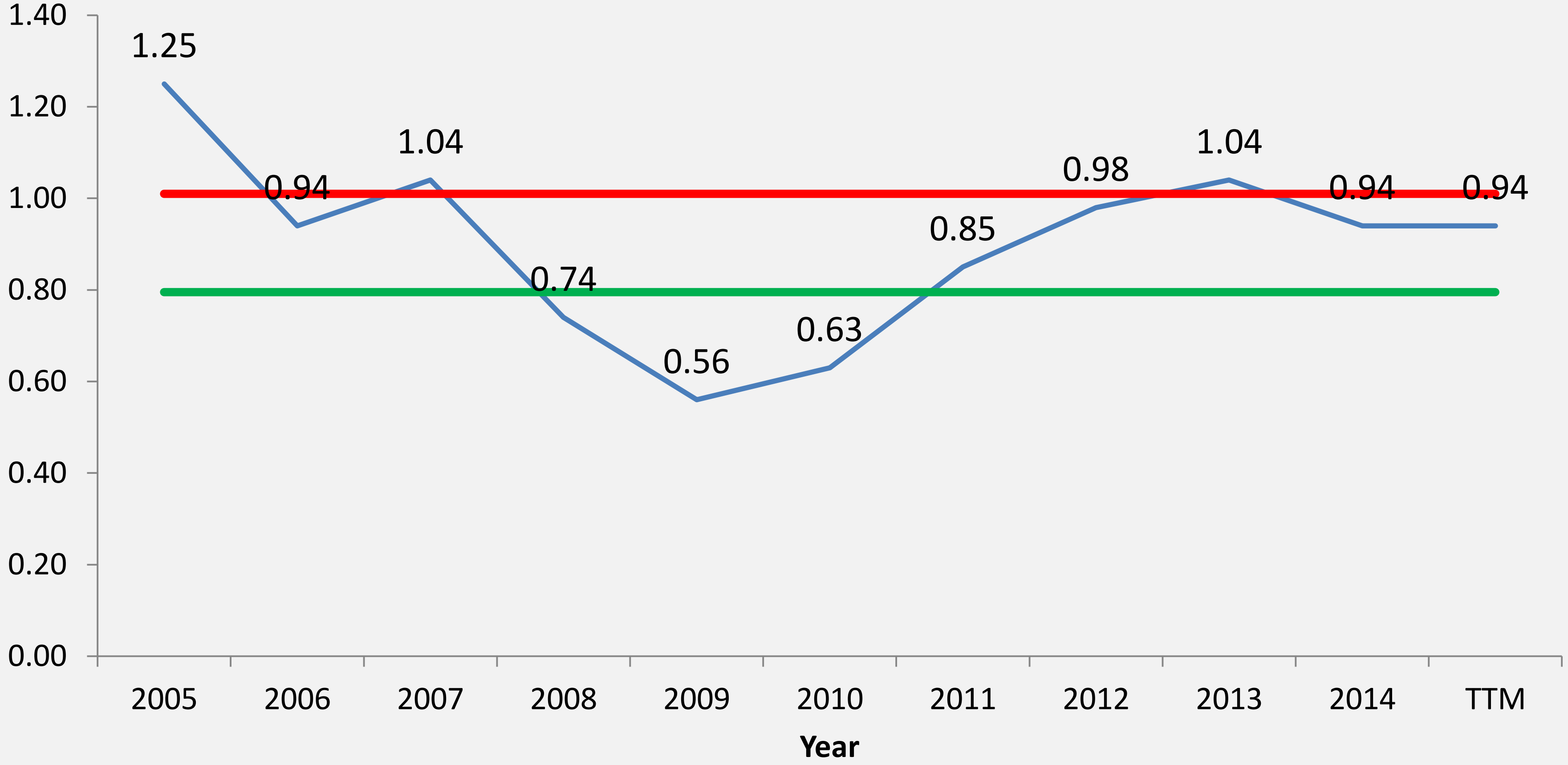


Price/Sales



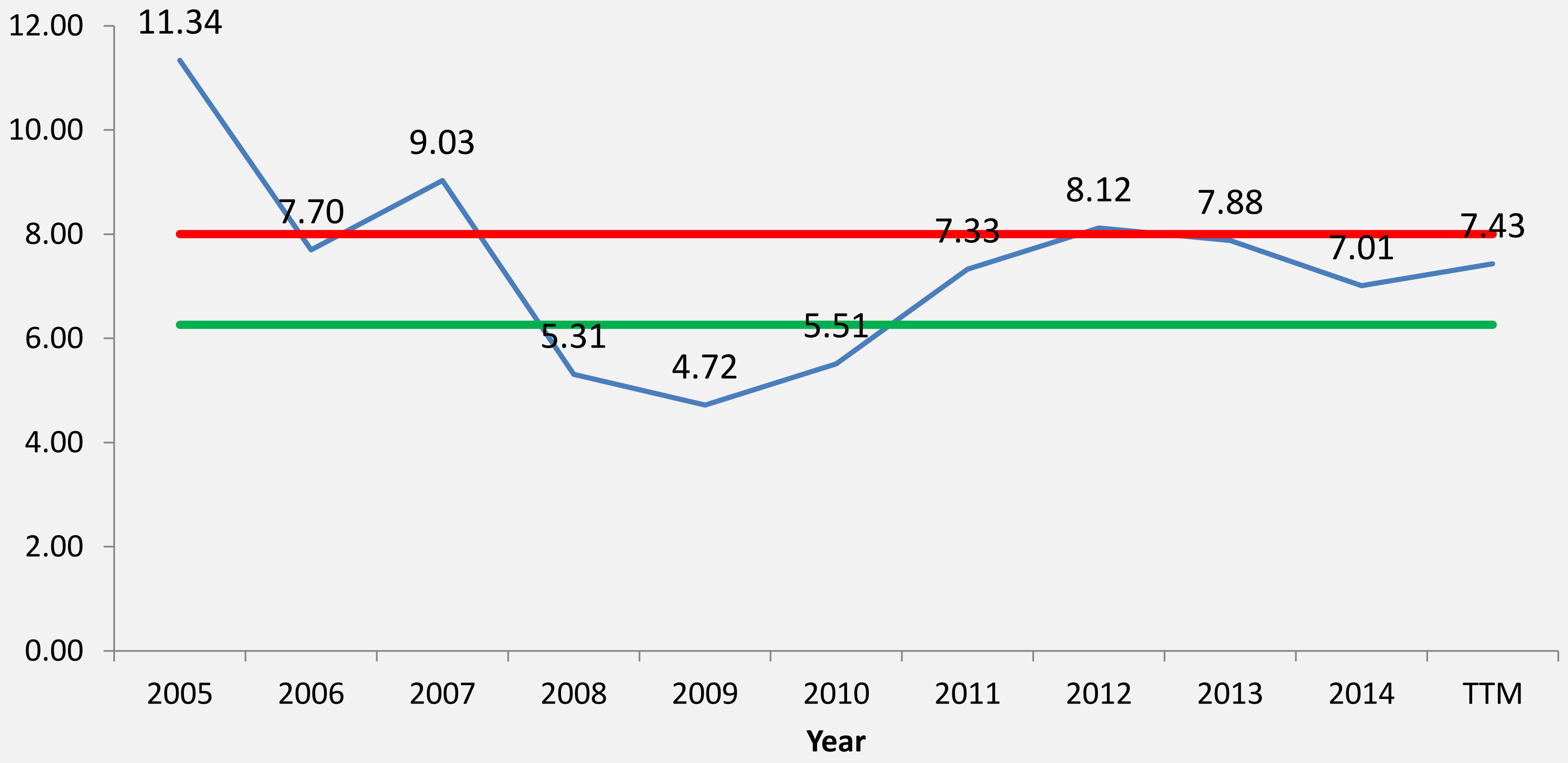
1.60
1.40
1.20
1.00
0.80
0.60
0.40
0.20
0.00
1.36
0.97
1.01
0.65
0.47
0.60
0.84
0.99
1.06
0.95
1.02
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
TTM
Year

EV/Revenue



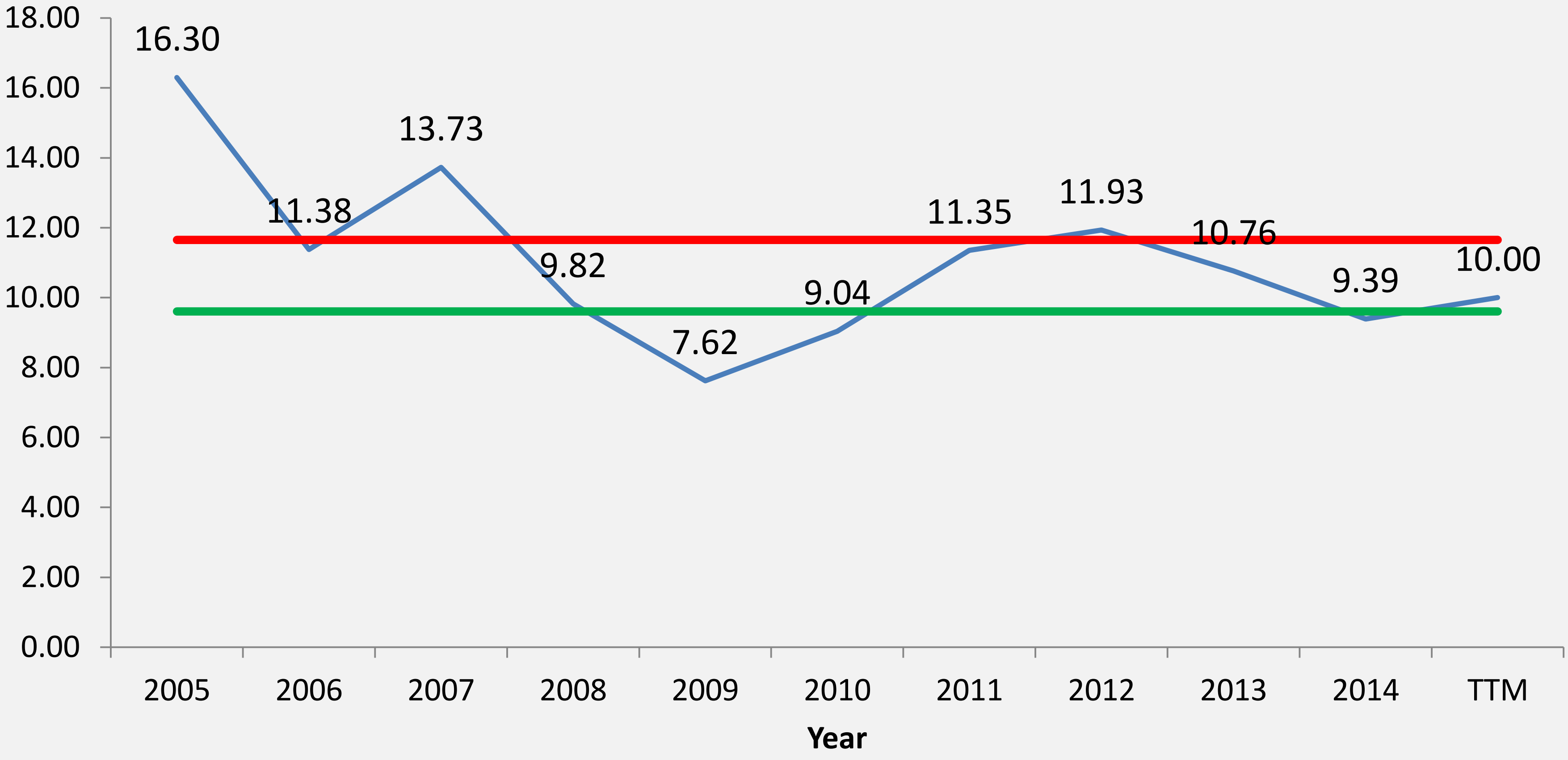
1.40
1.20
1.00
0.80
0.60
0.40
0.20
0.00
1.25
0.94
1.04
0.74
0.56
0.63
0.85
0.98
1.04
0.94
0.94
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
TTM
Year

EV/EBITDA



12.00
10.00
8.00
6.00
4.00
2.00
0.00
11.34
7.70
9.03
5.31
4.72
5.51
7.33
8.12
7.88
7.01
7.43
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
TTM
Year

EV/EBIT



18.00
16.00
14.00
12.00
10.00
8.00
6.00
4.00
2.00
0.00
16.30
11.38
13.73
9.82
7.62
9.04
11.35
11.93
10.76
9.39
10.00
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
TTM
Year

Conclusion

- The leader in the pet industry
- Sticky business
- Differentiated products and services
- Excellent financials
- Great company at a fair price

Decision

- Write put option contract at a strike price of $67.50 with expiration date of June 21, 2014
  - Premium of $2.15