

Warren Buffett and the Interpretation of Financial Statements Determining if a Company Has a Durable Competitive Advantage

This project will require you to use some of the accounting knowledge you have learned – or will learn this term – to perform the kind of analysis Warren Buffett performs to identify companies that have what he calls a durable competitive advantage. (A competitive advantage exists when a company can create monopoly-like economics, allowing them either to charge more or to sell more of their products.) If the company's competitive advantage could be maintained over a long period of time (durable), then the value of the business would increase year after year. (Sounds easy, doesn't it?) His ability to identify these companies has enabled him to become one of the world's richest men. What is his method? It is not a secret, "...put in the effort to learn accounting – how to read and interpret financial statements ..."

To complete this project, you will do just that: read and interpret financial statements for a company you have selected, then perform financial analysis using information you will find in the income statement, balance sheet and cash flow statement so that ultimately you can answer the question: does the company have a durable competitive advantage?

Required: Warren Buffett & the Interpretation of Financial Statements, Mary Buffett and David Clark, Scribner, 2003

Here is how to proceed:

Step 1:

Purchase and read the book. As you are reading, create a list of the chapters that you think will be most useful for your analysis. As you will discover, Warren uses most all the chapters as indicators to discover whether the company in question has a durable competitive advantage. For the project, you are asked to use 10 indicators (10 chapters).

Step 2:

Once you have tentatively identified the indicators that will enable you to decide whether a company has a durable competitive advantage, you will need to select the company you will analyze. (Refer to chapter 3.) You **cannot** select any of the companies Warren has invested in – they are mentioned throughout the book. Before finalizing your choice, I recommend that you locate and look over the company's financial statements. To perform your analysis, you will need to review a minimum of 3 years of financial data. (5 years would be better – Warren uses 10 years of data. If you were investing money in the company, I would use more than 5 years myself!) Locating a company's financial statements will be a learning experience for some. I will provide some tips going forward. Here's a link to get you started - <https://www.investopedia.com/ask/answers/119.asp>

Step 3:

As soon as you have selected the company, respond to the questions in the forum (soon to be posted). You will identify the company you have chosen and state your preliminary opinion (likely to be just a hunch!) about the company's durable competitive advantage. **Once a student selects a company, and discloses that choice in the Forum, that company is taken and not available for another student to use for analysis.** Once you have replied to the post, you can't change your selection; therefore, don't wait, but don't rush your choice either. All students should view all replies to make sure their company is not taken by another! To receive full points, your reply must be uploaded by 10/9. Don't wait until the deadline to reply – once you have selected a company, stake your claim! **Before you take next steps, I will confirm that the company you have selected is suitable and available.**

Step 4:

In this step, you will be re-reading the book, focusing on the chapters that you think will be the most useful for your analysis. In a Blackboard assignment, you will upload a Word document (a template will be provided) in which you will answer a few questions about your work, including identifying 5 of the 10 chapters you will include in your analysis. (To complete the project, you will need to use a total of 10 chapters, with this stipulation: a minimum of 3 income statement items, 3 balance sheet items, and 1 cash flow statement item. You'll have to use more than the minimum to reach 10, but this stipulation is designed to make sure that you don't select all chapters from one financial statement.) This part of the assignment will be due on 10/22. Also, by this date, you will be asked to upload the financial statements for the company you have selected. Details about this step will be discussed going forward.

Step 5:

You will have approximately 6 weeks to perform your analysis, in which you will have used the tools identified in a total of 10 chapters, to make the case that the company does - or doesn't- have a durable competitive advantage. You will upload a Word document (a template will be provided) in which you will provide a brief rational for selecting the chapter as well as the results of your calculations.

The purpose of the analysis is to determine if the company has a durable competitive advantage, which you may not know until you have completed your analysis. If it turns out that you picked a company that doesn't have a durable competitive advantage, that is fine. You are not being graded on your ability to select a company that does, instead you are being graded on completing each step, on time, and using the tools to perform the analysis. This part of the assignment is due on 12/3.

Here is a quick summary of the project timeline and outcomes: