Some things and ideas: December 2018

Some random thoughts on articles that caught my attention in the last month; this month may be a bit lighter than most given the holidays! Note that I try to write notes on articles immediately after reading them, so there can be a little overlap in themes if an article grabs my attention early in the month and is similar to an article that I like later in the month.

Drama at Rent-a-Center (RCII)

- On December 18th, Rent-A-Center shareholders woke up to rather surprising news. The company's agreement to be purchased for $15/share by Vintage Capital had reached its end date, and Vintage had not provided Rent-A-Center with an extension notice. Rent-A-Center's board decided to terminate the agreement and collect their reverse breakup fee (a hefty $126.5m, or >$2/share!).
- Generally, it's bad news for shareholders when a deal breaks, and it's particularly bad news when a cash deal breaks and the overall stock market has fallen >10% since the merger announcement (as was the case here); however, Rent-a-Center made clear that Vintage's failure to extend the merger had given Rent-A-Center the option to break the merger, and they had decided to do so "in light of the current financial and operational performance of the company".
- It was clear that something interesting was going on here. The intrigue only picked up when Vintage put out a press release later that day. The release noted that Vintage believed the merger agreement remained in effect and "that Rent-A-Center's actions constitute a further material breach of the merger agreement" (emphasis

mine).

- So what was going on here? Had Rent-A-Center decided their standalone value was higher than the merger proceeds and tried to walk away from the deal? It seems strange that could be the case; if so, wouldn't Vintage have simply extended the merger agreement? Or had Rent-A-Center been in breach of the merger agreement (as alluded by the “further” in Vintage’s statement) and tried to use the end date to cover up their breach?
    - We got some clarity the next day, when Vintage filed a copy of the letter they sent to Rent-A-Center. The letter is quite long, but it appears to dance around one simple fact: the merger agreement called for Vintage to deliver an extension notice to Rent-A-Center in writing, and Vintage appears to have simply forgot to do so. Incredible!
    - Vintage soon filed a lawsuit against RCII to compel them to extend the merger; again, the lawsuit makes a valiant effort but it fails to address the simple fact that they forgot to extend the agreement.
- As I write this, RCII is trading significantly higher than the merger agreement (around $16/share versus the $15/share merger price) and Vintage has been buying RCII shares pretty aggressively in the open market at prices >$15/share.
    - My guess is there's plenty of drama left to play out at RCII. Vintage is a major shareholder, so they could push for a board more amenable to settling the lawsuit / selling. The company could push Vintage to bump their offer in light of how the business is performing and that Vintage is probably on the hook for the termination fee. And there's probably plenty of other drama on the fringes of this (if you're a Vintage LP, you can't be thrilled that the company let an undervalued

merger target get away because they forgot to sign an extension!).

- As far as special situations goes, this is a crazy interesting one. It seems like you've got pretty significant downside protection between the huge termination fee and that RCII could always just settle the lawsuit and agree to get taken out for ~$15/share and pretty interesting upside from a possible bump in Vintage's bid (which would make tons of sense given how high the break-up fee is; even if they think RCII's fair value is just $15/share (which they appear to think is higher given the open market purchases) they could pay ~$17/share and come out ahead by avoiding the break up fee) or a simple got it alone / return cash to shareholders as results improve strategy from RCII. So why am I not involved? Three reasons: 1) I haven't done enough fundamental work on the company 2) RCII's merger proxy reveals they were pretty well shopped and the highest non-Vintage bid was ~$13/share; yes, results have improved a bit since then but today's price is way higher than what a lot of informed / sophisticated investors were willing to pay when RCII was shopping itself and 3) I I've never loved the business model / the large subprime consumer exposure / the potential for regulatory crackdown in some form.

Returns from “pulling an Adobe”

- I’ve mentioned “pulling an Adobe” (switching from selling software to selling subscriptions) on the blog several times (most recently in my post on Yelpv; disclosure: long)
- Here’s a Barron’s article that discussed “pulling an Adobe” and shows the gains from some companies that have

made the switch.

    - Obviously this isn't a scientific study / there's probably a good bit of selection bias here, but the returns presented in the article are fantastic. I suspect most companies that can make the switch have made it at this point, but I wouldn't be surprised if there are still several potential "winners" (from an investment point of view) that haven't made the switch to subscriptions yet and present investors who recognize the opportunity to make an investment ahead of the market realizing the upside / make a substantial return.
    - The Peloton example is interesting as well. Perhaps the opportunity for investors going forward isn't in finding companies that have yet to switch to subscriptions; instead, perhaps the opportunity is to apply a subscription business model to things that investors / consumers have never thought about having as a subscription service before (MealPal, for example, has tried to turn eating out into a subscription service; AMC and MoviePass (mentioned in the article) are trying to turn movie going into a subscription, and Uber and Lyft have both tried out subscription services)

Sports media update: A core tenant of the monthly update: continued highlights of the increasing value of sports rights (mainly because of my love of MSG (disclosure: Long)).

- Most tweeted about athletes of 2018
    - One of the reasons I like MSG so much is I think the NBA is the perfect sport for the digital age, and I think this list shows that off a bit. 7 of the top 10 tweeted about athletes are basketball players and 4 of the top 10 teams are basketball

teams.

- The NHL’s most valuable teams
- James Dolan Unplugged (interview w/ ESPN)
- New Fox Strategy Echoes Old Fox: Lots of Sports
- MLB eyes giving teams streaming rights
    - MLB Commish Confirms interest in RSNs
- The Great NFL Heist: How Fox Paid for and Changed Football Forever
    - I really liked this one; here are some key quotes I pulled out.
- David Stern built the modern NBA; now he wants to change how we consume sports
- Big Media, Selicon Valley Battle for Multibillion-Dollar Sports TV Rights (old, but I don’t think I’d seen it before and includes some really nice graphs and charts)
- NFL Advertising Revenue Falls Sharply Despite Higher TV Ratings
- Disney’s Hail-mary Sports Deal
- ESPN Wants to make SportsCenter great again
- Seattle gets NHL expansion team to debut in 2021-2022 season
- Startup Plans to Crunch Data to Invest In Pro Athletes

Other things I like

- Interview with Matt Rose (retiring Chair of Berkshire’s railroad, BNSF)
- Interview with Jeremy Grantham
- 16 ways to measure network effects
- Why Tips Won
- All I Want For Christmas Is You Comes Sooner Every Year
- Eddie Lampert Shattered Sears, Sullied His Reputation, and Lost Billions of Dollars. Or did he?
- AT&T Plans 3-Tiered WarnerMedia Streaming Service to Take on Netflix
- S. Mulls Changing Rules for Big Screen
- Charter (disclosure: long) files to test C-Band

- Some highlights from CHTR at UBS conference
- Liberty Media angling to snag post-bankruptcy iHeartMedia
- How this 7-year-old made $22m playing with toys
- Netflix renews Friends Rerun Deal
- When AI is the Product: The Rise of AI-Based Consumer Apps
- The Sneaky Fight to Give Cable Lines Free Speech Rights