

BFC Financial (OTC:BFCF)

February 18, 2014

BFC Financial is a convoluted, confusing, and completely misunderstood company trading at marked discount to fair value. While I am excited at the prospects for the company, there were many investors burnt by Chairman Alan Levan during the financial crisis. I am hardly a cheerleader for management, but the likelihood of lightning striking twice is considerably lower now and the company is safer than at any point in its history.

Most investors, especially those burned in the past, are quick to disregard changing fundamentals if the story is complex. While BFC Financial (BFCF) is complex now, the cash flows are strong and the company will gradually become simpler and slimmed down. From a 10,000 ft perspective it is easiest to think of the company as a collection of three assets: BFC Financial, BBX Capital, and Bluegreen Holdings. It is tough to discern an exact value for the consolidated company, but I believe that Bluegreen Holdings by itself is worth \$6/share and possibly more.

There are numerous catalysts along the way that should raise share prices and while \$6/share is my low estimate for fair value, the actual value could be significantly higher depending on the timing and actions of a court case.

Background

BFC Financial started as a holding company in the 1970's. The company was and still is run by Alan Levan and John Abdo. Levan has a rather interesting past, and as one [publication](#) put it "Levan's no cream puff." Along with BFCF, Levan is the Chairman of BankAtlantic Bancorp since 1994, and has previously had directorship/Chairman positions on Benihana, Bluegreen Corporation, and Woodbridge Holdings Corp.

This report will focus on the three segments most important to the company, BankAtlantic, Bluegreen Holdings, and BFC Capital. Levan is taking these three segments and consolidating them under the BFCF umbrella. In the segments below I will attempt to give a brief background for each pertinent section and try to derive a fair value.

BankAtlantic Bancorp

It is no secret that Florida was one of the worst states to make it through the financial crisis. Funding that excess was no other than BankAtlantic, a company with a spotty history, but a regional powerhouse. To make a long story short, BankAtlantic's loan book was incredibly toxic despite what Alan Levan said on an October 2007 [conference](#) call. After languishing for a couple of years, BankAtlantic's primary subsidiary was [sold](#) to BB&T in 2012.

BankAtlantic is now BBX Capital (BBX) and, for all practical purposes, is a hedge fund focused on distressed Florida real estate assets. BB&T and BBX formed two entities, BBX Capital Asset Management (CAM) and Florida Asset Resolution Group (FAR) that would act as a "bad bank." BBX contributed \$50

million of cash and \$346 million of assets (Aggregated value as held on BankAtlantic's balance sheet in 2012) to FAR in July of 2012. BB&T received a 95% interest in FAR, exchanged for the assumption of BankAtlantic's \$285 million of outstanding Trust Preferred Securities (TruPS). The assets allocated to FAR will be worked through until BB&T receives \$285 million plus a priority return of LIBOR +2%. As of 9/30/2013 this liability was only \$110.6 million, a decrease of ~\$175 million in 14 months. [\(10Q\)](#)

When the FAR deal was [announced](#) as final in March of 2012, the assets being placed into the subsidiary had a unpaid principal balance of approximately \$500 million. BB&T estimated that the recoverable principal value from FAR LLC was around \$350 million. Based on BB&T's math, BBX holds an interest in FAR worth \$65 million, plus some interest. If the economy recovers, it is likely that this interest is worth more and vice versa.

The other segment, CAM, was similar to FAR, except BB&T holds no interest. CAM contained \$125 million of assets and \$82 million of cash in July of 2012. These assets are slowly being worked through an on June 7, 2013 BBX reached an [agreement](#) with Daniel Catalfumo (a former developer who BBX sued to get back land that was personally guaranteed by Catalfumo) that resulted in the recovery of \$25 million of cash and property valued at \$14 million. Not bad for one asset in a pool of assets valued at \$125 million. There are [several](#) other [properties](#) that are working through the Florida court system right now which could add material upside if properly developed. I would encourage other investors to look through individual state filings and property tax records for evidence of the significant land holdings.

Finally, BBX Capital [owns](#) a few companies such as Hoffman's Chocolates, Williams & Bennett (more chocolate), and Renin Corp.

An estimate of fair value for BBX Capital is tough to determine, but here goes.

1. FAR: \$65 million
2. CAM: \$125 million of assets and \$82 million of cash for a total value of \$207 million
3. Other businesses: unknown. For now I will assign these businesses zero value.

Total value of BBX Capital is \$272 million at a base case. How that value accretes is anyone's guess, so choosing a discount rate and a time to discount appears to be a fool's errand.

Bluegreen Holdings – Timeshare Group

Bluegreen is a developer and owner of timeshares. Bluegreen became part of BFC Financial early in 2013. Currently the group operates 30 Club Resorts and 30 Club Associate Resorts. The estimated life-of-project sales was \$3.4 billion as of 12/31/2012. The timeshare business, while wrought with shady [characters](#), is a very lucrative business. Besides building and owning property, a timeshare owner also collects fees, offers financing, and can foreclose on delinquent owners to resell the property. Please see the appendix for a list of all sites owned by Bluegreen along with remaining economic life.

Since the financial crisis, Bluegreen has focused on fee based income versus the typical development cycle of owning and financing the property. The company should experience less working capital issues and should not run into as many financing issues normally associated with developers in downturns. If

they are quality developers they can offer their services for development and management and weaker companies take the risk. The table below shows the shift in revenue since 2008.

Table 1. Revenue for BFCF Timeshare Group and Predecessor

In Millions	2008	2009	2010	2011	2012	9M 2013
Sales of VOI	\$421.15	\$199.59	\$123.71	\$164.14	\$208.16	\$193.65
Fee-based sales commission	\$ -	\$20.06	\$52.97	\$73.67	\$87.80	\$74.39
Other Fee revenue	\$58.64	\$57.01	\$67.04	\$70.99	\$74.63	\$60.90
Interest Income	\$57.83	\$69.34	\$106.46	\$94.65	\$86.28	\$69.38
Other Income net					\$0.81	\$2.07
Total Revenue	\$537.62	\$346.00	\$350.17	\$403.45	\$457.67	\$400.39

The goal to a fee-focused business is clearly working, as fee's represented 10.9% of revenues in 2008 and in 2012 fees were 35.5% of total revenues. It stands to reason that the shift in income should help the company gain a higher multiple, relative to property developers who take on a larger portion of financing risk. In particular, "Other Fee Revenue" is very profitable and stable. Bluegreen's 2012 10K shows a 49.8% profit margin from "Other Fee Revenue in 2012. This helped drive FCF, as shown in the table below.

Table 2: FCF Generation From Timeshare Entity

In Millions	2008	2009	2010	2011	2012
Consolidated Cont Op Income			\$10.50	\$36.00	\$54.34
Discontinued Op Income			-\$46.37	-\$45.56	-\$3.49
<i>Less Non-Controlling Interest</i>			-\$8.09	-\$7.69	-\$11.14
Net Income to Bluegreen	\$6.58	\$3.90	-\$43.97	-\$17.25	\$39.71
<i>Add Back: Non Cash Impairment</i>	<i>\$13.71</i>	<i>\$13.16</i>	<i>\$56.19</i>		
<i>Add Back: Non-Cash Loss on Assets</i>				<i>\$59.14</i>	
<i>Add Back: Stock Comp</i>	<i>\$4.38</i>	<i>\$4.41</i>	<i>\$2.57</i>	<i>\$2.61</i>	<i>\$2.35</i>
<i>Add Back: D&A</i>	<i>\$15.08</i>	<i>\$15.58</i>	<i>\$14.91</i>	<i>\$13.17</i>	<i>\$12.26</i>
<i>Add Back: Provision for Credit Losses</i>	<i>\$76.08</i>	<i>\$31.64</i>	<i>\$94.55</i>	<i>\$29.55</i>	<i>\$28.62</i>
CapEx	-\$22.88	-\$7.52	-\$3.70	-\$4.01	-\$6.21
FCF (Cont Operations)	\$92.94	\$61.16	\$166.93	\$144.14	\$102.49
Consolidated FCF	\$92.94	\$61.16	\$120.56	\$24.06	\$76.72

Since 2008, Bluegreen has generated an average of \$113.5 million in FCF from continuing operations and an average of \$75.0 million in FCF for the consolidated entity. As the company generates more

income from fees there will be less of an impact from credit events as a significant portion of fees are stable and recurring. If the merger of BBX and BFCF is completed, all of this FCF will go directly to BFCF.

Complimenting the attractive cash flows, Bluegreen now has a world-class partner, Choice Hotels. In January of 2013, Bluegreen and Choice [announced](#) their new alliance. Bluegreen Vacations is the official vacation ownership provider for Choice Hotels. I believe Choice's selection of Bluegreen is very positive for BFCF shareholders, the proof can be seen in statements made by Choice executives.

"Our alliance with Bluegreen enables us to further expand Ascend into a great resort destination. It marks a unique relationship with a timeshare company and an opportunity for us to monetize our distribution capabilities in a new market with new customers. It also represents a blueprint for pursuing similar opportunities that can further monetize our distribution capabilities in the future. We are very pleased with the initial results from this alliance on both the timeshare lead generation front and with room booking trends through our central channels for these resorts."

-Stephen Joyce Q1 2013 Earnings Call April 29, 2013.

While no exact value can be given to the partnership, the alliance adds to attractiveness to the Bluegreen name. It also could reduce costs incurred by Bluegreen for marketing and commissions of timeshare properties.

To value the Bluegreen, I will only use historical financial results. I believe this is realistic because the past five years saw the financial crisis and gradual recovery. Getting an exact value is difficult so I will use absolute and relative valuations to get an idea of potential ranges.

-Absolute Valuation

This range is pretty straight forward. From 2008-2012 Bluegreen generated an average of \$75 million of FCF from the consolidated company. Given the pipeline of projects (Appendix 1) and recurring fee revenue, it seems reasonable to believe that the company can generate close to this much FCF in the future, with relative stability.

Therefore I believe the equity should be valued between 8X-11X FCF. This is admittedly a crude range, but gives a fair value of \$600-\$825 million.

-Relative Valuation

There are two competitors that are public and only one is pure play on timeshares, Marriott Vacations Worldwide Corp(VAC). Marriott obviously has a world class brand to their products so I would expect BFCF to trade at a discount. Regardless, in the [Q3 2013 earnings release](#) the company expected to generate \$170-\$185 million of adjusted free cash flow for the full year 2013 period. With a current market cap of \$1.78 billion, VAC is trading 10X the mid-range estimate for FCF(\$1780M/\$177.5M).

Previous M&A activity can be used as a proxy too. Western Reserve published a timeshare market update in [April of 2012](#). The lowest multiple paid for a timeshare company was 7.1X EV/EBITDA in April 2001, the highest was 11.3X EV/EBITDA in Feb 2011. The table below shows possible M&A scenarios and

are based on EBITDA flows from 2010-2012. The debt figure is taken from the Q3 2013 10Q for BFCF and includes Receivable debt and mortgage debt payable.

Table 4. M&A Multiples Based on Historical EBITDA Acquisition Multiples from Western Reserve

In Millions	EBITDA	EV/EBITDA	EV	Debt	Equity
Low	\$93.99	7.0	\$657.93	\$539.75	\$118.18
Mid	\$132.23	9.0	\$1,190.07	\$539.75	\$650.32
High	\$124.53	11.0	\$1,369.83	\$539.75	\$830.08

From the above valuation ranges we can say that the timeshare business in BFCF is worth somewhere between \$118 million to \$830 million. I believe \$118 million is far too conservative and a more realistic valuation range is between \$400-700 million. This is a rough range based on interviews with industry experts. Overall, Bluegreen was well-regarded in the industry and other companies like working with them. An attentive reader will notice the wide range doesn't really matter.

Bear Valuation: \$400 million (an 18% FCF yield based on historical FCF)

Base Valuation: \$550 million

Bull Valuation: \$700 million

BFC Financial

BFC Financial has \$182.24 million of cash (as of 9/30/2013), \$6.93 million of that was held by variable interest entities. Ignoring the restricted cash, this leaves \$175.3 million of cash for BFCF. This cash can be used for acquisitions or other value creating activities.

Grand Total

BFC Financial: \$175.3 million of excess cash. Bear case, this can't be deployed, base case it can be deployed.

BBX Capital: \$272 million as a base case. Bear case, a 50% haircut, is \$136 million plus significant NOLs.

Bluegreen: \$550 million base valuation and a \$400 million bear valuation.

Potential Fair Value: \$536 million to \$997 million

If the merger completes there will be 117.87 million shares of BFCF common stock outstanding. At a current price of \$2.81, this implies a market capitalization of \$331.2 million.

Potential Fair Value Per Share: \$4.54 to \$8.45

Why is This Available and What Are The Risks?

I believe the opportunity is available for three reasons. First, and foremost, management has screwed over everyone except for themselves. In my opinion management can handle this from an operational perspective but they can't figure out how to reward shareholders, despite being large shareholders themselves.

However, I believe that ignoring this investment simply because of management's past would be myopic. After all, it is where we are going that counts, not where we have been. I believe that by consolidating all entities into BFC Financial, Alan Levan sets up the company to be the sole vehicle for wealth creation, outside of his salary. Besides taking all of his companies under one umbrella, Alan Levan made a stock option [agreement](#) with his son in December of 2013. This agreement allows for Alan's son, Jarett Levan, to purchase all of Alan's Class B shares upon the elder Levan's death. I believe it is in Levan's best interest to not screw up BFCF. However, a cynic would respond that it is in the best interest of Jarett to keep the stock price low.

The second reason the stock is undervalued is the ongoing SEC [lawsuit](#) against Alan Levan. The SEC believes Levan misled investors. After reading the court docket and the quotes, I believe they are correct. If a jury finds Levan guilty he will be banned from holding a directorship or management position at a public company.

This is a moot point though. As explained in the previous point, Alan has already set up the company to be run by his son Jarett. I must ask then: even if the SEC wins, so what? The company will be controlled by the same group that already runs it. Overall, I believe that this case is not that important, however, I continue to monitor it to make sure I am not missing something obvious. Usually excellent operational details arise out of court transcripts so I intend to follow the case with vigor.

The downside to the acquisition not going through is straightforward; BFCF will continue to enjoy the ratable share of profits from all entities. As the real estate works through the python that is BBX Capital, the resulting cash flows will still benefit BFCF. The same goes for Bluegreen and all timeshare holdings. Even if the merger fails to go through, downside seems protected from cash flows, assets, and cash on the balance sheet.

The third reason the opportunity exists is the complexity. Hopefully I have explained the business and broken down the various components in clear enough detail to get over this hurdle.

All these risks (along with the obvious real estate, timeshare securitization, and now premium chocolate market risk) should be factored into the stock. However, at what discount is everything baked in? With a current price of \$2.70/share, Mr. Market believes that a 40% discount for management is necessary versus my low price target of \$4.54/share. This seems absurd and quite excessive. In my humble opinion, a lower discount should be applied.

Conclusion

BFC Financial is messy, hated, and ignored – a perfect investment for Dichotomy Capital. Countless investors have been burned by Alan Levan and Co. but emerging from the ashes is a company with serious cash flows and significant catalysts. The crown jewel, Bluegreen Holdings, is worth more than the entire market cap of the combined company. Bluegreen has successfully transitioned significant portions of their timeshare business away from the financing dependent securitization market and into a recurring fee model. They are well respected in the industry and have a robust pipeline of projects ahead.

BBX Capital is the remnants of BankAtlantic, and by my calculations, plenty of value remains. How to properly value those assets is anyone's guess, but there is clearly some value embedded in there, time will tell how much.

As the company gets through the SEC trial and consolidates the business I expect true asset value and free cash flows to emerge. While there is risk in management, it seems absurd to apply such a high discount to fair value. Investors today can purchase shares of BFCF at a significant discount to fair value and enjoy the ride of simplification and consolidation.

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Appendix Item 1. Sites owned by Bluegreen

	Homes	Est Remaining	
Club Resorts	Not Sold	Life Of Project(\$MM)	\$/Home(MM)
Big Bear Lake California	50	\$264.00	\$5.29
Daytona Beach Shores, Florida	16	\$10.00	\$0.63
Marathon Florida	3	\$5.30	\$1.52
Orlando Florida: Fountains	313	\$454.50	\$1.45
Orlando FL Sunshine	14	\$15.60	\$1.16
Ormond Beach, Fl	10	\$8.30	\$0.84
St. Augustine, FL	18	\$17.50	\$0.96
Surfside FL	19	\$13.90	\$0.73
New Orleans, LA	18	\$15.90	\$0.89
Boyne Falls, MI	23	\$15.00	\$0.66
Branson Missouri	132	\$81.30	\$0.62
Hollister MI	183	\$415.00	\$2.27
Ridgedale MI	65	\$30.00	\$0.46
Ridgedale MI The Cliffs	161	\$364.00	\$2.27
Las Vegas NV	153	\$156.00	\$1.02
Atlantic City NJ	26	\$22.00	\$0.85
Hershey, PA	20	\$19.50	\$0.99
Charleston, SC	8	\$7.40	\$0.91
Myrtle Beach, SC	7	\$5.50	\$0.78
Harbor Lights Myrtle Beach	99	\$70.00	\$0.71
SeaGlass Myrtle Beach SC	24	\$70.00	\$2.86
Shore Crest North Myrtle Beach	19	\$19.00	\$0.99
Gatlinburg, TN	242	\$218.00	\$0.90
Pigeon Forge TN	93	\$85.00	\$0.91
Gordonsville VA	13	\$10.50	\$0.80
Wilderness Traveler Gordonsville	83	\$93.00	\$1.12
Williamsburg VA	439	\$607.00	\$1.38
Wisconsin Dells WI	104	\$147.50	\$1.42
Xmas Mt Village Wisconsin Dells	25	\$19.00	\$0.77
Oranjestad Aruba	9	\$5.80	\$0.65
Total	2,388	\$3,265.50	\$1.37