Growing Companies with Big Potential

Weitz | INVESTMENT MANAGEMENT

Small/Mid-Cap Value Strategy Webinar Transcript

Portfolio Managers: Wally Weitz, CFA & Drew Weitz

April 23, 2015 • 3:30PM CDT

Jo Ann Quinif: Hello. Welcome and thank you for joining us today. As the Operator mentioned, our call today is going to focus on our Small and Mid-Cap Value Strategy, otherwise known as Hickory Funds. This is the second of a five-call series for the year. Our last call that focused on Large-Cap Value is available on our website and on August 20, Wally Weitz and Brad Hinton will host a webinar on our Multi-Cap Value Strategy.

Before I turn the call over to Wally and Drew today, I thought I would provide a brief update on our organization. Most of you know, in our almost 33 years, we have always focused on research and investing. It is simply who we are. This shows through our deliberate and measured manner in which we grow our business, our decision to remain independent and employee-owned and how we work as a team. We now have 38 employees and 35 of those are here in Omaha. We've had no departures from our Investment or Client Service Teams and as I mentioned on our last call, we're planning to expand our team this year. Specifically, we will be adding an Equity Analyst to our Research Team this quarter.

We manage almost $6 billion in assets, primarily in six main offerings: Large-Cap Value; Multi-Cap Value; Multi-Cap Alternative; a Short-Intermediate Fixed Income Strategy; and Small and Mid-Cap Value, which is approximately $445 million in assets. In addition, we have a Core Plus Bond Fund, a Balanced Fund, a Research Fund, which is managed by our Analysts. If for all of you dying for Nebraska (communities), we have a Nebraska Tax-Free Income Fund.

Information on all of our offerings is available on our website.

As you probably figured out by now, we have one philosophy of process when it comes to equity investing. So as you listen to our series of calls over the year, you will certainly hear our core principles that resonate across all of our Strategies. We don't try to overcomplicate it and we believe much of what we do is based on common sense. Having the right temperament and patience to identify undervalued stocks and buy them at the right time, we believe, is a unique skill and one where we can add great value.

With that in mind, I will introduce our host for today's call. Wally has been at our helm since he started the firm in 1983. He is our Chief Investment Officer and a Portfolio or Co-Portfolio Manager on most of our Equity Strategy. Drew Weitz came back home to Omaha in our firm in 2008 after spending several years at Ariel Investments. Everyone on our Research Team is an Analyst first and foremost. Drew manages a sleeve of the Research Fund and joined Wally as a Co-Portfolio Manager on our Mid Strategy in 2011.

Before I turn the call over to Wally, one last item. We will take questions following the prepared remarks today but throughout the webinar, you're welcome to e-mail questions to advisors@weitzinvestments.com or use the Q&A tab on the webinar and we will address all questions at the end.

With that, I'll turn it over to you, Wally.

Wally Weitz: Hey, good afternoon. I'm going to start out talking about our principles and Drew and I will tag team as we go through this. We think like business owners, buying a company that we expect to keep for years. We want to know if it has a durable competitive advantage. Will it generate predictable amounts of discretionary cash flow for

Weitz | INVESTMENT MANAGEMENT

the owners? Will Management do a good job of allocating capital and use prudent amount to leverage as Management focus on growing per share business value? We try to be intellectually honest with ourselves and use common sense. Are we kidding ourselves about the quality of the business? We trust Management to treat us like partners in the business. What could go wrong? What's our downside risk?

We're bottoms up Investors and we're driven by valuations. We want to understand the macro environment and the risk of surprise external events but we're buying businesses one at a time. Disciplined about the price we pay and we will wait patiently for our pitch. Concentrate our portfolios and our best ideas on adequate diversification that we don’t feel compelled to own stocks in all sectors. We try to be imaginative about how risk might be correlated in unexpected ways and we want to know our companies well enough that we're comfortable putting 35% to 50% of portfolio in our top 10 stocks. We think of risk as the possibility of permanent loss. Volatility is not the same thing as risk. Volatility can be quantified so it's handy for academic studies but we think volatility is good for price sensitive Investors. Permanent loss is bad and we do try to avoid that.

And finally, we eat our own cooking; come to be a cliché but it’s true for us. All employees are offered equity in the Company and virtually all have invested in it, an amount equal to 25% of everybody's comp up to the IRS limit; those into a profit sharing fund and has to be invested in our own funds.

We do allow personal accounts but for the vast majority of everybody's investable net worth that's invested in our funds. So personally, I own some Berkshire Hathaway stock but all the rest of my investable funds which is 95 plus percent is invested in our funds. So this doesn't guarantee that the funds will go up but does mean that we win or lose the same way and that you have our full attention.

Drew?

Drew Weitz: Thanks Wally and let me also add my thanks to everyone for joining us this afternoon. So Wally just laid out our core principles and these are the foundations for all the Strategies that we manage here at Weitz. On today's call, however, we are focusing only on our Small and Mid-Cap Strategy or SMID which we describe more fully on Slide 8.

SMID can mean different things to different Investors. At Weitz, we define this universe as companies with market caps between $250 million and $10 billion at the time of purchase. Although we believe $10 billion is an appropriate upper bound when considering putting additional capital to work in a SMID Strategy, we don’t treat it as a hard ceiling that forces us to exit a position. As a reminder, our sell discipline is typically defined as exiting positions that exceed our sense of business values. Additionally, we’re willing to sell an investment we think is cheap if we find a more compelling opportunity to invest in. And lastly, if we discover an error in our thinking or our business value estimate becomes impaired, we will sell a position and learn from the experience and move on.

Our mandate then is to uncover investment opportunities wherever we can find them within this market cap range. Once in the portfolios, we opportunistically add to positions as they become cheaper and pare back on holdings as they become more expensive. Within this range, you can imagine finding smaller company opportunities is advantageous as they have a longer runway for growth and maximize our flexibility to opportunistically trade around positions

before hitting that $10 billion threshold. And since 2011, 1/2 of all our new portfolio companies have been below $2 billion in size at the time we purchased them.

In all our strategies, we run concentrated portfolios as Wally mentioned earlier. For SMID, this has tended to mean between 30 to 40 portfolio companies at any time, with roughly 35% to 45% of total assets invested in our ten largest positions. Portfolio construction is purely done from the bottom up, weighing each individual investment opportunity against what's already in the portfolio, as well as potential new investments from our lift of fully researched investment ideas which we call our on-deck list.

Also, as Wally previously mentioned, we're benchmark agnostic, filling portfolios from the bottom up without pre-determined industry, sector or market cap weightings. That being said, we do spend time thinking about degrees to which our holdings may have common exposures or shared risk factors and attempt to manage these accordingly.

The Fund's cash position is a result of overall valuations and the number of opportunities we have to deploy capital at sufficient discounts to our estimates of business value. Later in this afternoon's call, we'll speak in more detail about the Fund's residual cash position and how it's fluctuated over time. For now however, I'll turn it back over to Wally for a review of our performance.

Wally Weitz: Okay, as we turn to the slide on portfolio performance, we're actually going to show the same slide three times focusing on different segments of it. We're showing the Hickory Fund numbers and the Russell 2500 numbers on the top half of the table and cash levels on the bottom. So, on the first sector, 2010 to 2012, we had bought aggressively as the market fell in '08/'09 and we enjoyed a strong bounce coming off the bottom. So, our performance was better than the Russell 2500 by a wide margin and we sold into the rally as the price-to-value ratios of our stocks rose.

In 2014, on the next Slide, we had strong absolute gains but trailed the 2500. Cash peaked out in 2013 and as individual stock performance diverged a little and we had some market corrections, we added to existing positions and bought some new ones.

Then on the next Slide, the boxes at the right show results for the three and five-year periods ending March 31, and for the full period since mid 2008 when Hickory was officially designated a Small/Mid-Cap Fund. What that shows is good absolute returns though the 2500 was hard to keep up with. Smaller companies seemed more expensive to us so cash grew during the recovery and held back our performance. We look for a high probability of positive returns, not just good relative returns and our conservatism cost us some upside. Drew is going to elaborate on our tactics and discuss our use of cash next.

Drew Weitz: So before we dive into the recent portfolio activity and uses of cash, I think it's helpful as Wally just did, to take a step back and look through the last several quarters through the lens of overall evaluations. We sometimes confuse our family and friends because we appear most frustrated when markets are racing ever higher and most excited when stocks appear to wobble. Naturally, they ask, what are you rooting for anyway? And the answer is volatility.

And the Slide starting on Page 15 attempts to demonstrate why. This first chart depicts two data series, the multicolored mountain chart measured

by the left axis is just the growth of $10,000 invested in the Russell 2500 starting on December 31, 2012. We've broken the calendar years into separate colors for convenience. The purple line measured against the right axis is the weighted average ratio of our portfolio company stock prices compared to our base case estimates of their business value. This aggregated price-to-value ratio, or P-to-V, is therefore a representation of how cheap or expensive our portfolios are at any given time.

We are naturally most excited when we perceive stocks to be cheap and there is a competition for investment capital. However, as we progress through 2013, represented by the blue portion of the mountain chart, you can see that the market moved higher in a fairly orderly pattern. The Russell would ultimately finish that year up an impressive 36.8%. That's the best calendar year performance since the depths of the crisis in 2009, coming fully five years into the current bull market. That's actually the best calendar year performance for the 2500 since 2003. Our equity investments kept up with the market but in such a broadly strong environment, we found few cheap stocks to replace more expensive holdings. Naturally, the portfolio price-to-value ratio crept higher throughout 2013.

Calendar 2014, here shown as the red portion of the mountain chart, was a different experience. The Russell 2500 ended the year with a perfectly satisfactory 7% return but its trajectory in doing so was anything but straight up. The volatility experienced that year, as represented by the various peaks and valleys on the chart, was more dramatic than in 2013, particularly early in the fourth quarter.

A lower P-to-V indicates a cheaper portfolio and intuitively, better raw materials for prospective returns. Thus, we were pleased that as we move through 2014, we were able to lower the overall evaluation levels of the portfolio from the low 90s to the low 80s. This was accomplished both by recycling from the more expensive positions to cheaper holdings, but also through a very active year on the new investment front. Wally will share more details on these in a moment.

As a result of these actions, one would anticipate that our residual cash position would shrink. On Slide 16, we show the same Russell 2500 return experience but this time we've plotted our cash position along with it. We are sometimes asked about holding elevated levels of cash, whether we’re making a market call, waiting for a market correction or potentially something worse.

As this Slide demonstrates, the answer is that we're just waiting for opportunities to put capital to work and volatility, so often used as a synonym for risk, is often the very thing that presents opportunity for Investors.

Finally, on Slide 17, we plotted the portfolio price-to-value ratio and the Fund's residual cash position together. The purpose of this Slide is to simply reinforce the point that the Fund's cash position is a residual of the overall level of investment opportunities available.

I’ll turn it back to Wally now to discuss some of these recent new ideas.

Wally Weitz: Okay, the next Chart on 18 shows what we're calling portfolio comings and goings. We generally have pretty low turnover in all our funds in the 25% to 30% range on an annual basis and this shows all but new positions and the exited positions during the last five quarters.

We do trade around the positions at time and harvest tax losses when we can. So some of the new stocks came as spinoffs. Liberty TripAdvisor and Liberty Broadband and other new buys were stocks from our on-deck list that finally came down to our price target. Most of the sales were maturities of good ideas; others were short stopped by takeovers, namely Sapient and Catamaran. Then there is Liquidity Services which turned out to be a mistake when they lost a key contract that we had thought was safe, that we sold it. Now Drew is going to give some information on our energy stocks.

Drew Weitz: So one thing we thought we would do because the topic is clearly in the news, a lot these days is discussed, very briefly, our energy positioning within the Fund.

Historically, we've had a low weight in energy companies over time, but as the opportunities have presented themselves, we've begun dipping our toe in the water a little bit more. So as you can see on Slide 20, these are our positions as of the end of the first quarter in World Fuel Services, Core Labs, and Range Resources. I'll talk very briefly about each of these positions.

World Fuel, initially purchased in the spring of 2013, is a distributor of fuel and related products and services; the customers operating on land, on sea or in the air. We were attracted to World Fuel's business model where the company puts buyers and sellers of fuel together, earning a spread on each gallon or ton of fuel sold. And because the company typically does not take inventory risk, World Fuel is sensitive to the consumption of oil rather than swings in the underlying commodity price. World Fuel adds values for producers by aggregating highly fragmented demand into one known and trusted customer with a very strong balance sheet. End users benefit from greater volume-based discounts as well as ancillary services World Fuel can provide.

Contrary to the headaches that lower oil prices create for producers, the company has actually benefited from recent price volatility as it creates greater demand for higher margin offerings like fuel cost hedging strategies, as users look to lock in lower prices. We've trimmed our positions some on strength, but there is plenty of opportunity for World Fuel to gain additional market share either through continued acquisitions or organically in a highly fragmented industry.

Core Labs was one of the new purchases from the fourth quarter, Wally mentioned earlier. We've been patiently watching this one, as it has spent the last five years on our on-deck list. Core's army of long tenured and experienced scientists travel the globe helping oil and gas producers better understand the resource potential to their acreage and how to most effectively extract those resources in over one thousand producing fields today.

This science for higher business model is obviously capital light and generates terrific margins, even better returns on invested capital and a healthy amount of free cash flow. And unlike the traditional wildcatters who put every dollar back into the ground, Core's Management Team is dedicated to returning excess capital to its Shareholders.

Core's business will obviously be correlated to overall spending on exploration and production activities and the current slowdown has obviously taken a toll on both earnings expectations and Core stock price, but businesses of this quality are rare and given its ability to generate excess capital even in the current depressed environment, Core Labs has the

capacity to wait this one out and potentially come out more valuable thanks to a Management Team that understands the importance of per share value growth.

Lastly, Range Resources is a company we've owned in other Strategies for a few years but purchased shares for SMID in the fourth quarter as the recent declines brought the market cap into our strike zone. Range is a domestic producer of natural gas and natural gas liquids with enviable acreage in the highly prolific Marcellus Shale. As we have said many times and in many settings, we don't believe that we or anyone else can accurately predict short-term moves in the price of oil or natural gas, but we do believe that over long periods, prices of all varieties must reflect their underlying economics.

Thus, rather than focusing on near- term commodity price forecast, our investment in Range Resources is predicated on their position as one of, if not the lowest cost producer of domestic natural gas. Again, thanks to their advantageous position in the Marcellus, as well as their ability to utilize scale to drive operating cost lower. In a commodity business, low cost production should win. With resources in the ground that can sustain high levels of production at reasonable returns even from these depressed prices and a stable balance sheet, Range is well positioned to ride out the current pressures.

As a reminder, Range Resources is the featured investment in the Analyst Corner section of our first quarter report to Investors which you can find on our website. Now, Wally will wrap things up.

Wally Weitz: Okay, thanks, Drew. The portfolio of the Hickory Fund at the end of the quarter had an estimated weighted average price-to-value in the mid 80% range; that's at the upper end of the normal range. The top 20 holdings accounted for 60% of total assets, which is 75% of our hot stockholdings because of the cash that we hold. We have an on-deck list of 39 companies but their average price-to-value is 90%, that's why they're still on-deck.

In short, we like our companies but we really don't like their prices very much. So, we know that we're measured on a relative performance basis and every day, we'd love to do better than all the market indices but we're owners of the Fund and we care about absolute returns too.

So, I appreciate everybody being on the call. And now, we'll open it up for questions.

Operator: And if you would like to ask a question over the telephone, please signal by pressing star, 1 on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment and that is star, 1 for phone questions at this time. And there are currently no questions over the phone.

Jo Ann Quinif: We did receive one question via e-mail and please feel free to e-mail them or go to - click on the webinar, as well, but maybe while we wait for people to queue up their questions, we'll answer this one first. So, the first question that came in says, you said you like companies you own, so you don't like their prices. I assume that they are not currently priced where you would want to add capital to those but if the portfolio is in the mid-80s P-to-V, I also assume you're comfortable but just not excited. Is that a fair conclusion or can you elaborate?

Wally Weitz: Okay, I'll start on that and then Drew can chime in. This is Wally. When we do our valuations, we make estimates of future cash flows and

discount those back and using a 12% discount rate. So, theoretically, if all our estimates are correct, we could pay 100 cents on the dollar and look forward to 12% returns out into the future but we want a margin of safety. So, when we say a stock is at an 85% of our estimated value and that we're comfortable with it, that's true, but we don't get excited until we see something at 70 cents or 60 cents or 50 cents on the dollar. We're just - we're kind of cheap about that. So, but when a very good company is growing and selling at 85 cents on the dollar, it runs the risk of a market correction taking it to a wider discount but as long as the value of the business continues to grow, we just think that's terrific. We'll just buy more as the price goes down.

Drew Weitz: This is Drew. I think the only thing that I would add to that is to just remind folks that aggregated P-to-V is just that. And that within the portfolio itself, we have a few that are above that mid-80s level and a few that are below, as well. So, it's a useful measure overall to track over time but that's not to say that everything in the portfolio is at that level and in fact, we've recently been evaluating a couple of new potential opportunities that hopefully, we will be able to talk more about in future calls.

Wally Weitz: Yes, and I would also add that our valuation methods are ones that we feel very strongly about in a general way but the - there's art involved and we're making estimates of future cash flows and we're more confident about our estimates with some kinds of companies than others. So we may have a 90 cent dollar that really feels very comfortable because the outlook is very predictable and we may feel more comfortable with that than say an energy company with a 65 cent or 70 cent price-to-value where there is a lot of guess work to be - as to what the pattern of future oil prices will be. So it's - there's a lot of judgment involved in this.

Jo Ann Quinif: Well that actually plays into this other question that was actually submitted in advance and somebody had asked, why Martin Marietta versus Vulcan Materials?

Drew Weitz: So it's not necessarily a question of either or and in fact we've owned Vulcan in the past and we would certainly own it again if it were trading at the right prices. Right now, Vulcan is at a premium both to Martin as well as to our base case estimate of value there. In general, we like those assets and we think Management's done a good job by focusing in on the aggregates, assets that they have and divesting their non-core ready-mix concrete assets. This is a company that was forced to get their house in order after the failed takeover bid by Martin a while back and they've done a good job of getting cost down sustainably and just - putting their heads down and getting their balance sheet in order and all of this plus a new Management Team hasn't been lost on the Street. So the stock's been well regarded as simply just too rich for us at these prices.

Wally Weitz: Yes, I think we would - you might see us own Vulcan instead of Martin if the price relationships were different. It's the same macro story and the same good assets and Vulcan did pay up for Florida Rock and maybe impaired their value a little bit years ago, but 99%, a matter of price-to-value that leaves us to own one over the other at the moment.

Jo Ann Quinif: So one of the other questions that has come in is, Drew, you mentioned the energy sector and you spent some time there. Are there any other sectors in particular that you're finding interesting right now?

Wally Weitz: I don't think there is a generalization we can make. I mean, we're finding - our on-deck list has 30

some stocks on it, but as Drew mentioned, Core Labs was on our on-deck list for five years before it - we waited for it to come down a hundred points before we were ready to buy it. We've found a few new ones, but we can't mention them until they get publicized at the end of the quarter. But one would be in the consumer goods area; another in a real estate area; within media, there's always things changing, whether it's in the Liberty or - but today, Comcast gave up on the Time Warner Cable merger and that may open up all sorts of possibilities for Charter and others.

Drew Weitz: And we (bought them) as a result. One, I think that brings up the one important point I'd like to make about the energy sector. We did spend some time talking about that and we have dipped our toe in the waters there. But it wasn't a function of seeing a bunch of stocks go down a lot and deciding we needed to have an opinion and get involved. Our ability to purchase Core and purchase Range really is a function of having watched those stocks for a long time. As we mentioned, Core has been on the on-deck list for years and the decision to make that wasn't pure contrarianism for the sake of it, it was having followed the companies and following our valuation discipline.

Wally Weitz: Yes, and one other thing on the energy stocks. We - Core Labs is pretty optimistic about a V-shaped recovery and others are very pessimistic because of the way shale oil can be brought on in short order now that may make this cycle take longer than in the past. So in both the Range and Core, we've got companies that are strong enough and have good enough margins and strong enough modes that if it does take two or three or four years for oil to get back to the prices that everybody is hoping for in the $80, $90 range, they'll do just fine and survive and thrive during that kind of environment. There are some others that might have a lot more upside if the recovery comes soon but they tend to be highly leveraged companies and they might not survive if it doesn't happen soon. So we're - we want to be able to win either way.

Jo Ann Quinif: We have several other questions kind of queued up here. The first one that I think we'll take is, is there a certain price-to-value metric you look for when buying from the on-deck or selling out of the current portfolio?

Drew Weitz: Yes, so the answer is yes. When we're talking about taking the new position in any company really, our starting point wants to acquire shares of really terrific businesses when they are trading at 70 cents on the dollar. Now, sometimes when the competition for capital is pretty high like it was in 2008, 2009, we may have the pick of the litter and it might take a higher threshold or excuse me, a greater discount to get into the portfolio. I think at that point we were looking for new ideas in the 50-cent or 60-cent range.

So, by and large, we tend to use 70 cents on the dollar as our starting point and as I mentioned on the call, we'll be opportunistically trading around portfolios - excuse me, around portfolio companies throughout our ownership. We don't have a hard and fast rule that says at a specific P-to-V of 85 we begin trimming; that gets to Wally's point about not being too fooled by the precision of a DCF model. We're informed by what we think of as being the relative upside and downside provided by our low and high case business estimates. For those of you who may have seen the chart, we sometimes talk about that as our cone of outcomes. So, by and large though, as we're scaling out of the position as P-to-Vs elevate, typically we'll be looking to be out of a name as it - as it's at or exceeds our base case business value.

Wally Weitz: And sometimes - if you remember last October, right around the middle of October, there was a sharp drop in the market. I think the general market went down 79% and several stocks went down more and we took our first, what we considered - we hoped to be our first heart of a position in several new stocks and then it immediately - the market immediately bounced back up so we ended up with a few small stranded positions like Post and some others.

We never know how far down, down is, so we tend to scale into a position as the stock falls and scale out of a position as the stock rises, so we try to be flexible and not really dogmatic about precise numbers on that.

Jo Ann Quinif: We have a couple of questions specifically around the market cap size and the range for potential companies that we consider for Hickory and also if there is - are you strictly looking at the market cap or total capitalization. And then you already talked about sell discipline but maybe as it relates to capitalization and I think you mentioned it earlier, but maybe if you can just recap?

Drew Weitz: Yes, and I'd be happy to review that. So we generally think of this SMID universe when we're putting capital to work as being between $250 million and $10 billion at the time we're committing that capital and so, you know, that's a pretty wide range, as it relates to the upper end of that. We're very happy to have a full position in a company at $9 billion and to let that appreciate over time, understanding that we won't sell it once it hits $10 billion. We'll just agree not to add additional capital to it at that level and that's mostly just too kind of make sure we're staying in that sweet spot of the $250 million to $10 billion range.

Wally Weitz: Also, I think there is - you had a question about enterprise value. We think it's good for certain companies and certain kind of businesses to use a prudent amount of leverage, and we have a few companies where that prudent amount is a large number so that the enterprise value might be well above $10 billion, even though the market cap is well below, and we are strictly looking at the market cap of the shares.

Drew Weitz: Yes, as we're thinking about eligibility for new capital deployment, we will be thinking about the equity capitalization. but as Wally mentioned, obviously the full balance sheet is something that has the attention of all the Analysts and Portfolio Managers here and we look to make sure that we're investing with Managers with prudent discipline around that.

Jo Ann Quinif: Along that vein, one of the questions here is about Post holding and have you talked to and had interaction with the new Management Team, and how does the level of leverage at Post affects your conviction level?

Wallace Weitz: Well, our Analyst, Barton Hooper, has had ongoing contact with the Management and with the CEO when he was with other companies, so he is a known quantity and we know that they are very comfortable with leverage. They've made quite a few acquisitions to diversify the food portfolio away from cereal. This is at least in part a bet on a proven leader, Mr. Stiritz, and I believe that he understands what he's doing with leverage and that they'll work it down over time, but the raw numbers of six or seven times leverage is not a level that we're - people are looking for it very often.

Drew Weitz: Yes, I think I would just follow on that by saying that while I mentioned that sometimes the market gives us very

brief opportunities to acquire shares at pretty meaningful discounts, Post was one of those times, and I think as you look at our holdings as of the end of the first quarter, our position is around 1-1/4% of net assets. You know, I think balance sheets of that size we're obviously very cognizant of and that's a function of what we think about when we're doing position sizing in general, as well. So Barton - as Wally, said Barton has had a chance to interact with the new Management Team. Stiritz obviously is now in the Executive Chairman position, so we think the playbook is very clear. The Malt-O-Meal brand acquisition is a part of that, as well as the diversifying acquisitions as well, so we're comfortable with Management Team there and comfortable with the balance sheet and look forward to that coming down.

Wally Weitz: We were very price sensitive about it and that's why when it dipped down to about $40, $41 on that - those few days in October and we took our pilot position, the initial position, we didn't add to it as it's bounced up. There is a lot more potential volatility involved in something with the balance sheet like that.

Jo Ann Quinif: Are there any questions that have been posted via the phone before we move through to a couple more of these maybe? I just don't want people to wait if they're on the line.

Operator: Not at this time.

Jo Ann Quinif: So the other question that is somewhat related to what we've been going through is that Hickory is underweight financials versus Russell 2500 and maybe you can talk a little bit about being benchmark agnostic and I threw in the benchmark agnostic - but why are you underweight financials?

Wally Weitz: Well I think there are maybe a number of reasons. There are a lot of different kinds of financials and I think many people think of banks and thrifts immediately when they hear that term and in past times we have owned small-cap or mid-cap banks, reasonable banks, but we just don't think they are particularly attractive as a group at this point. We own a couple of insurance brokers that are really - they're not financially sensitive in the sense of taking credit risk or interest rate risk, they are really sales organizations that are sort of getting a royalty on the insurance cost of businesses and so it's really an entirely different animal. Historically, we've not been or I've not been comfortable with casualty insurance companies unless I was awfully sure about the reserving. And so, in our other funds, we've owned Berkshire Hathaway forever but we've rarely owned a small casualty company. And there's another kind of financial, mortgage REITs, and we've owned Redwood Trust for now over 20 years. We were original Investors when they were forming the company back in the 90s and that's the company that for the first 15, 20 years of its life, was really a collector of mortgage assets and they were holding the equity part of a mortgage fund and they were very good at credit risk and we're not taking interest rate risk. That company's been evolving the last few years, and it's becoming more of a traditional mortgage banking company which is not quite as interesting to us but we still like the Management and think it's reasonably priced.

So, lots of different kinds of financials. A lot of the financial - big financial companies that we're very comfortable with, like Wells Fargo for example, are too big for Hickory, so they - you would find them in our other funds but not here.

Jo Ann Quinif: Okay. So, there are two questions here that I'm actually going to

combine into one and the questions actually are how new companies end up on your on-deck list and then the other one is regarding overlap in the holdings with our Partners Opportunity III Fund and I thought it might work to have that conversation in one answer.

Wally Weitz: Before we answer that, let me add one PS to the financials question. With interest rates artificially low because of what the Fed’s been doing, the environment is just odd and not built for banks and spread lenders, and it could well be that when that situation normalizes, that you would see us owning one kind or another of what I would call spread lenders.

Drew Weitz: So then addressing the - how do we get new names on to the on-deck list, really that's - I'm wearing my Analyst hat, that's what we're charged with working on everyday and the way that we go about identifying new opportunities is through a lot of reading. We try and read everything we possibly can whether it's popular financial press, whether its trade magazines related to particular industries, whether its sell-side brokerage research, in some cases whether it's the writings of respected thought leaders within our industry, as well. And each of us is out kind of pounding the payment as often as we can, going to conferences, meeting with Management Teams there. We try very hard to set up our own interactions with Management Teams. We try and go out and visit them, see whatever kind of offices or plants or just in general try and get a tour of their operations where possible, and really try and do the leg work to go out and find those opportunities. Once we've identified them, the process to get them on to the on-deck list which I'll review very briefly - each of the companies in the portfolio are on the on-deck list has a sponsoring Analyst. That Analyst is charged with doing the due diligence, the deep dive. Different members of the team may help with due diligence visits to have second set of ears, second set of eyes and a second set of questions, but ultimately, we have one sort of sponsoring Analyst who creates the financial model, does the DCF modeling and then writes the company report to be vetted by the whole team.

And that report, what we're trying to identify is, what does the company do, what is their sustainable and durable competitive advantage, what are the characteristics of the industry that they operate in, the competitive landscape, the general idea of what the financials of the company look like over time, whether or not this is a talented Management Team that behaves with integrity and understands the value of per share value creation. And then that process is followed the written materials and the model is presented to the group and we sit down, we vet that in one of our research meetings. Everyone tries to constructively poke holes in the investment pieces. Once that process is done and ideas considered, and there is any follow up that needs to be taken care of, the company will be considered to be on-deck. So that's the process there.

As it relates to the combined question that Jo Ann mentioned about overlap with Weitz Partners Value - excuse me, Partners III Opportunity Fund and the Hickory Fund, I think the holdings overlap is something in the high-teens in terms of company names; the weights of those we’ll need to follow up with.

Wally Weitz: Yes, I was just looking down the list of Hickory Holdings and it looked to me as if around 3/4 of them were also holdings of Partners III. But since Partners III is allowed to own much larger companies also, and some of my very favorite companies at the moment are large, the percentage of holdings

that overlap would be a lot smaller than that 3/4.

Drew Weitz: And one other point I think I'd like to make about the overlap too, given Hickory Fund's size again relative to the Partners III Opportunity Fund, Hickory can take a full position and have it be meaningful to the Fund at the lower end - at the very lower end of that market cap range. So Hickory has additional flexibility in the lower market cap spaces than might otherwise be available.

Wally Weitz: Yes, another way of looking at it is that I manage Partners III by myself and if I like something well enough to get it in - put it into Partners III and it's under $10 billion, I'll lobby Drew for that and since when we buy something in Hickory, we have to agree on it, I'm likely to also put it into Partners III. So there is - the names will probably always overlap quite a bit but the weightings will change from time-to-time. If Berkshire Hathaway is the biggest weight in Partners III and doesn't fit in Hickory, it's going to ((inaudible)) that overlap. It's the same mindset - as Drew said earlier in the prepared parts, we have the same mindset, the same process, the same - we're looking for the same things for both. It's just that Hickory has to be the subset of smaller companies.

Jo Ann Quinif: Yes, it's interesting, I was looking at the top 10 for PIII which - in Partners Opportunity III is about 46% of the portfolio and seven of those names I think are large-cap and so they just wouldn't be inspiration for Hickory at all.

Okay, so we have one last question and it is regarding your kind of macro view and your outlook and the person was saying you don't take a macro view.

Drew Weitz: Thank you.

Jo Ann Quinif: But they're wanting to know kind of what you're seeing through the companies' eyes. Are they still borrowing, are they buying back shares, do you see any themes, kind of in what the companies are doing with?

Wallace Weitz: Well I'll start and Drew can chime in. I think for the most part, even though the U.S. economy has been so-so and the parts of the global economy especially Europe have been weak, that our companies are feeling pretty good about their businesses. They're finding ways to cope. They are expanding when they can do that opportunistically. The ones that are having softer stock prices, like the ones in energy are buying back stock - I think Drew was saying that Core Labs bought back a little over 1-1/2% of the total outstanding shares in the first quarter. So, the business is not bad and the outlook is fine and the companies are finding things to do but, I personally, I say I don't have any macro opinions but I can't help but think that $4 trillion of freshly printed money force-fed into the securities markets really seems to have inflated securities prices to some extent. And it seems very possible that stock prices are a year ahead or two ahead of themselves and that we could have company value go up but stock price go down which actually would be heaven for us. And so, outside of something extreme like energy, I think it's just patiently plodding forward.

Drew Weitz: You know, I think I would just sort of emphasize that, that kind of environment is a good reminder of why we're always kind of looking for Management Teams that, as we like to say, can make their own breaks. Those who are able to create value either by repurchasing their own shares when their stocks are weak, like a Core Lab; or those that can take advantage of historically cheap financing in order to do very accretive acquisitions, like Charter has before it and which we own by virtue of Liberty Broadband. So, we really like it when we can find

Management Teams that we can partner with that are sort of all season players and that's really the heart of what we're trying to identify.

Jo Ann Quinif: So, unless there are any other questions on the phone portion of this, I think we've answered everyone's questions and we certainly appreciate everyone attending this afternoon. As I mentioned, our next call will be on August 20 and we'll be reaching out to you and sending out information on that as we approach that time. We're always happy to answer questions in the meantime. So, please don't hesitate to reach out. And we look forward to seeing you or talking to you on the next call. Thank you.

Operator: There are no further phone questions at this time. This does conclude today's conference. Thank you for your participation.

END