Sophisticated Process - Equities

Research yielding a consistent investment strategy

While our philosophy may be simple, our strategy is based on very sophisticated investment analysis. We believe an investment strategy must perform well through a variety of market environments, particularly over longer periods of time. To help accomplish this goal, we have identified certain characteristics of assets that often merit further analysis and review. Of these, quality, consistency, and discipline are the key factors that frame our overall investment strategy.

Equities

Our equity investment strategy is based on fundamental analysis and seeks to create a portfolio of companies that grow their profits faster and more consistently than the overall market.

Quality

- Earnings growth supported by similar or better cash flow growth.
- Solid balance sheets that can support the business through uncertain economic conditions.
- Experienced and accessible management teams focused on efficient cash flow allocation.

Consistency

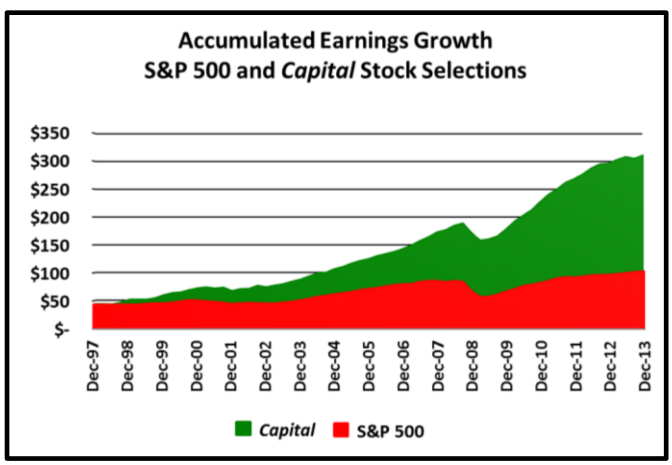
- Market demand for products and services are relatively steady in all economic conditions.
- Flexible business models that can minimize the impact of weak economic conditions.
- Less capital intensive businesses generate high levels of free cash flow that management can allocate (M&A, dividends, share repurchase).

Discipline

- Participate in markets with secular growth dynamic
- Sustainable balance of revenue growth and operating income growth
- Wide-moat competencies supportive of high barriers to entry

More Growth

As demonstrated in the chart, our equity process results in a portfolio of companies that generates faster and more predictable earnings growth than the market over time. The higher level of predictability serves as the fundamental foundation for lower volatility across a full market cycle.



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Equity Strategies

Advanced discussion

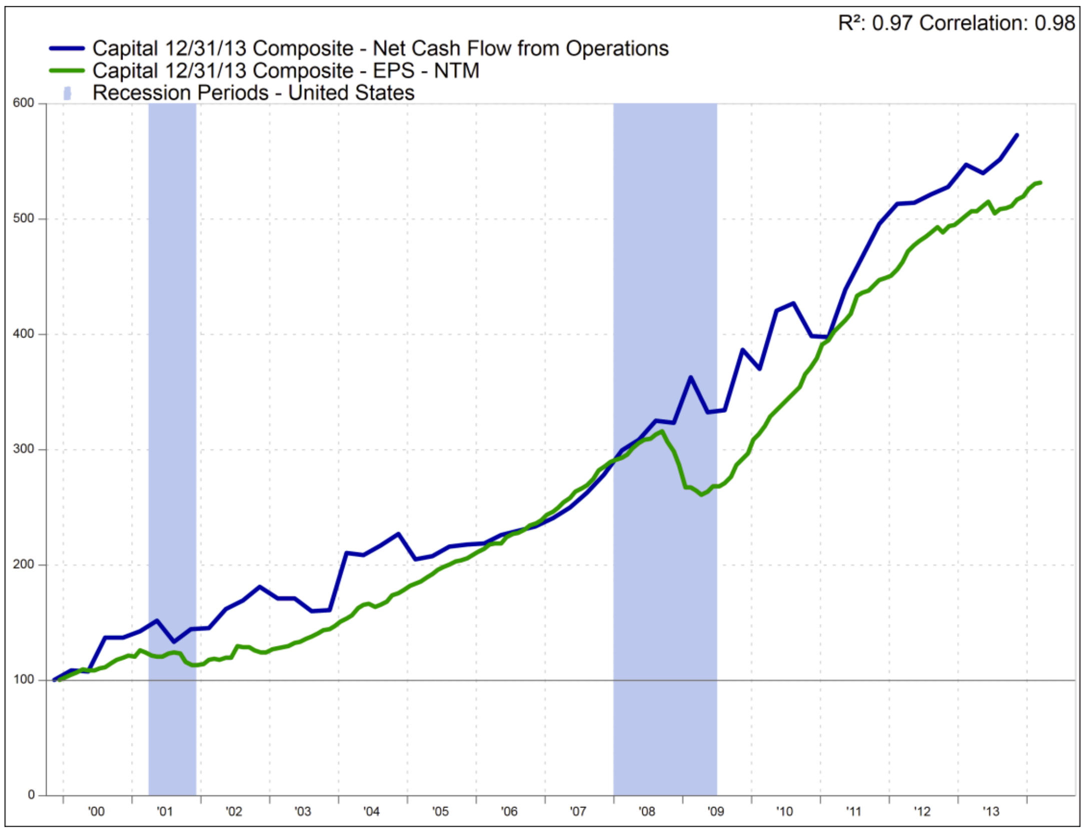
Our equity selection process simply seeks out companies whose fundamentals support our desire for high-quality, sustainable, and consistent earnings growth. This process includes both qualitative and quantitative analysis.

Insights are more meaningful when they are supported by numerous factors. The greater the number of confirming variables the higher the level of confidence we can have as an investor. Numerous qualitative elements are considered in our selection process including the experience and track record of senior management, economic and industry dynamics, and sustainable competitive advantages.

We also incorporate a wide variety of quantitative variables. Below we share some of the key factors and ratios. Although these are important, they only represent a sample of our analytical efforts.

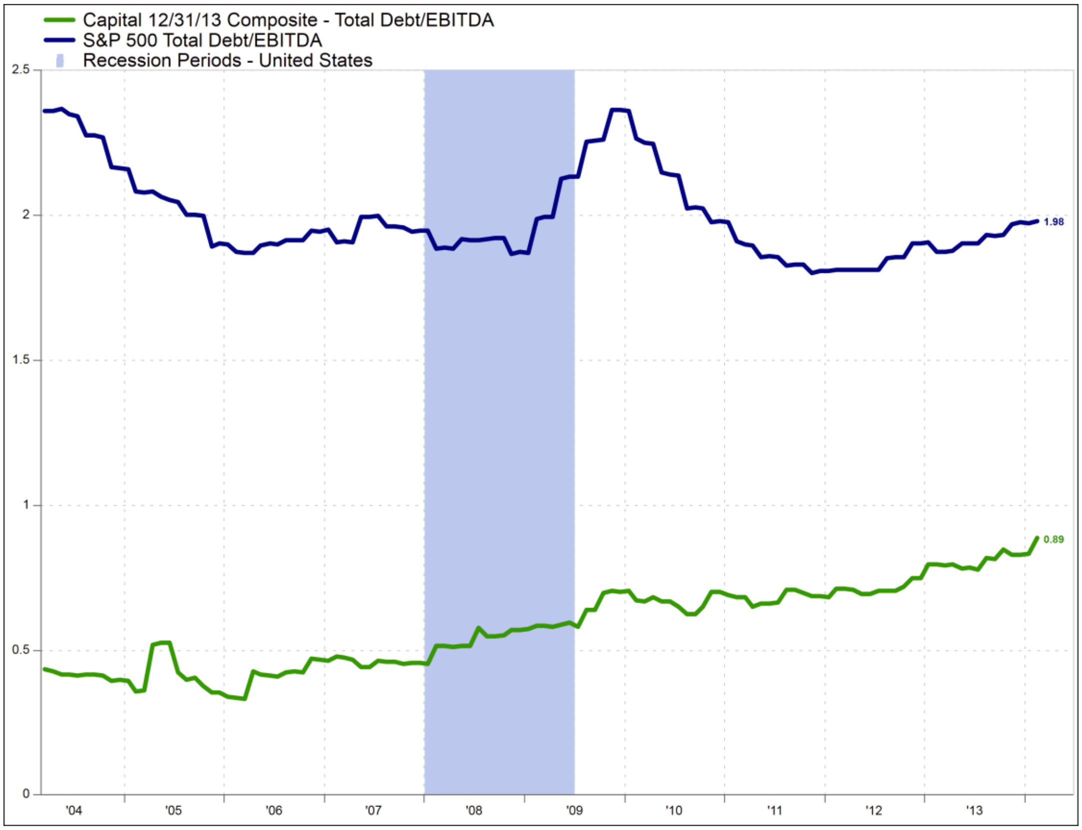
<u>Quality Growth</u>

Earnings Growth and Cash Flow from Operations Growth should be consistent over time. In the chart to the right, we compare cumulative growth of earnings and net cash flow from operations for a sample portfolio of companies. Although Operating Earnings are the most commonly watched fundamental indicator for most investors, Cash Flow from Operations incorporates the management of working capital to run the business and indicates the important level of cash generation that company managements can allocate to sustain profit growth which will benefit shareholders' returns. Major uses of Cash Flow from Operations include:



- ✓ Capital Expenditures
- ✓ Dividends
- ✓ Debt reduction
- ✓ Share repurchases

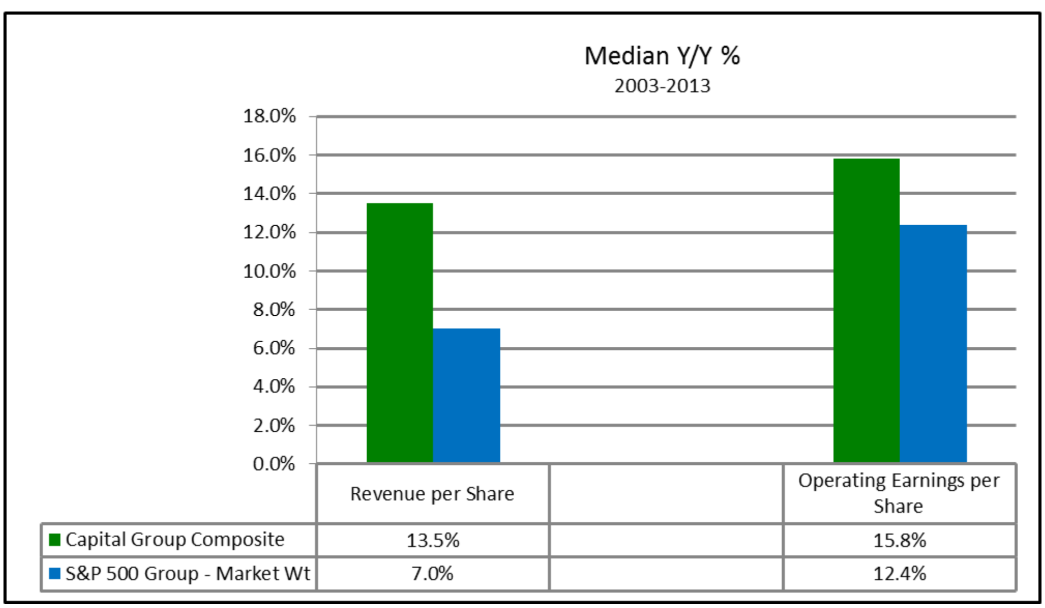
Strong Balance Sheets



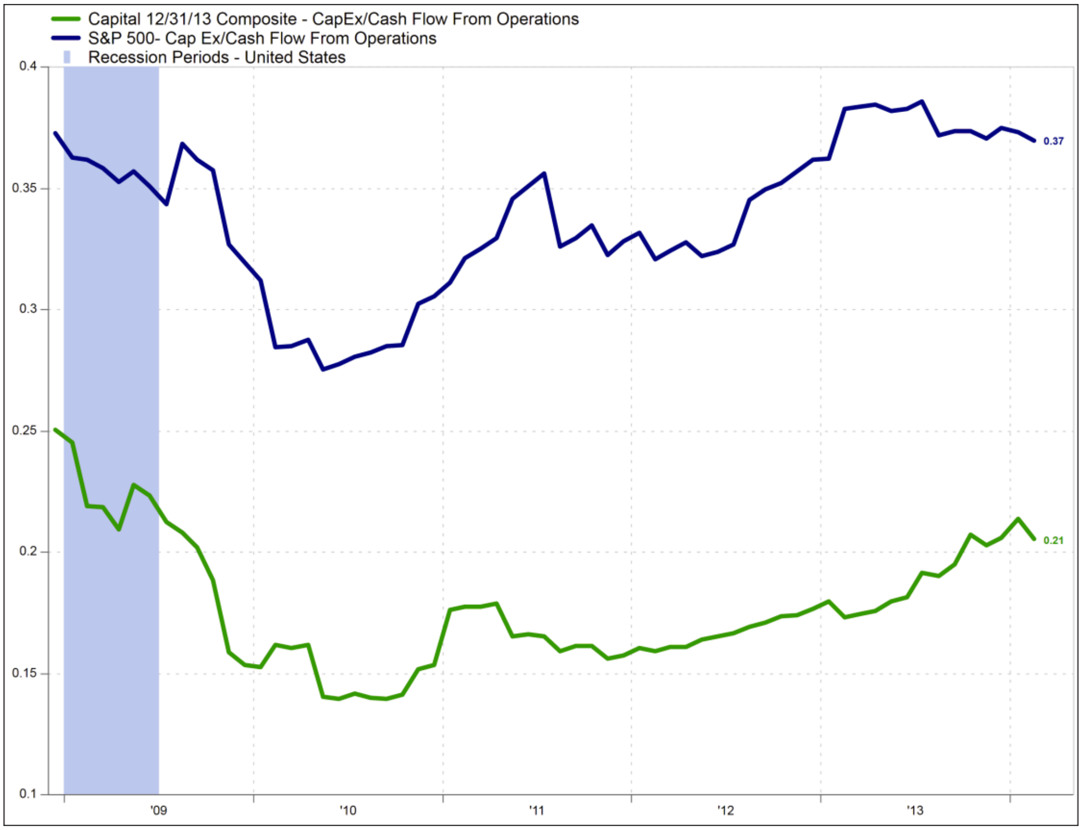
A strong balance sheet allows a company to handle adverse marketplace conditions better. During difficult conditions, weak balance sheets become exposed and limit management's flexibility. Balance Sheet strength can be measured multiple ways. One of our preferred methods is to compare the total debt held by a company to its ability to service the debt. In the chart to the right, we compare the Total Debt/EBITDA (raw cash flow) ratio of our portfolio to the companies in the S&P 500. Combined, our portfolio companies hold Total Debt equal to 89% of the EBITDA generated. This compares well to the S&P 500 companies that hold 198% of Total Debt to EBITDA. In difficult times the more cash flow available to service debt obligations the more flexible and nimble a company can be.

Sustainable Growth

The strong relationship between profit growth and price appreciation over time implies that if a company can sustain profit growth for an extended period, its shareholders will be rewarded with attractive appreciation. A consistent balance of revenue growth and operating earnings growth over time is one of our preferred indicators of sustainability. Too much dependence on margin improvement (the difference between earnings growth and revenue growth) could lead to problems when economic conditions are unfavorable. In the chart below, we compare our portfolio companies to the S&P 500 companies over the last 10 years.



Consistency from flexibility



A significant factor in a company's ability to consistently produce profit growth is the capital intensity of the business. More capital intensive businesses use higher levels of capital expenditures to support growth and, therefore, tend to experience more earnings volatility over time. Likewise, less capital intensive businesses require fewer expenditures to support growth and allow management more cash flow flexibility to enhance shareholder value during all economic conditions. The chart to the right compares the Capital Expenditures to Cash Flow From Operations for our portfolio companies and the S&P 500 companies. Presently, our portfolio companies spend slightly over 20% of Cash Flow From Operations on Capital Expenditures compared to 37% for the S&P 500 companies.

Our goal is to maximize the probability of achieving superior results. We believe our disciplined adherence to our fundamentally based investment process gives us the best opportunity to reach our goal.