Steve: Thank you all for being here today. We're here for you to gain a better understanding of the Contrarian Value team and its flagship FPA Crescent fund. I'm going to start off with a bit about the FPA Crescent Fund's philosophy and process, followed by some fund history, and then conclude with a few more global observations. Then, Brian Selmo and Mark Landecker will review a few investment examples that both reflect current positioning as well as highlight our process.

So, there's an African saying, if you want to go fast, go alone. If you want to go far, go together. One lone ant accomplishes nothing. But when they colonize with others, genius results. Food is procured and stored, and great architectural structures are built. Moving to humans, one individual can really mess things up. You may surmise that someone on my team doesn't like the Cardinals. But unlike ants when you put a large group of smarter people together you frequently get stupidity squared. So taking an object lesson from nature our inclination is to be more ant-like with the whole being greater than the sum of our parts.

I am privileged to work with a smart, committed group of people who allow me to travel farther than I otherwise would alone. Beginning with my co-portfolio managers, Brian Selmo and Mark Landecker, for whose partnership I'm tremendously grateful. The rest of the colony, our analyst team is knowledgeable, curious, passionate, and like ants quite persistent, and thankfully they have enough humor to overlook the fact that I'm comparing them to insects. Andrew August, Anh-Tuan Bui, Greg Crouch, Sean Korduner, Chris Lozano, and Byron Sun, will you guys please stand up wherever you are. Byron and Chris, and their wives each had their first child in the last few months. We're happy to say they're working just as hard as they were before and they swear it has nothing to do with having a crying baby at home. Our team will be around much of the day and we hope you take time to meet with them. I think spending time with the analysts will just further aid your understanding of what we try and accomplish within the Contrarian team. Thank you, guys.

Moving on to philosophy and process. We want to provide, over the long-term, an equity-like return with less risk than the stock market while avoiding a permanent impairment of capital. We have successfully accomplished this for more than two decades over multiple market cycles by maintaining an absolute return focus, investing across companies' capital structures be it in common stocks, preferred stocks, convertible debt, junior debt, or bank debt. We've also invested in other asset classes like subprime mortgages, residential loans, farmland and commercial real estate loans.

A hallmark of the Contrarian Value team is that we're patient. Like a spider that spins its web and waits for its supper to fall into it, we do our work and then wait. We prosecute our philosophy through a process dictated by patience. We deeply investigate the companies or assets considered for investment, and if upon the culmination of that research we find that it's something we'd like to own, but if the price is wrong we'll patiently wait for the price to come our way, recognizing that sometimes it will not, and that all the good work we did might not provide a return. We spend our days thinking about what is most appropriate way to commit your capital, and ours along with it. We wake up each morning not knowing what might drive a stock price. By having an appropriate long-term mindset we feel protected from the daily onslaught of corporate rumors and innuendo that play through a new cycle.

We do look down first. We're a little neurotic in always asking ourselves what can go wrong. It forces us to ask questions like, how will cars be sold in the future? Will Tesla's direct market approach disintermediate dealers. Will there be fewer cars sold thanks to driverless cars and Uber? What industries will be most negatively impacted by robotics and 3-D printing? We think a lot about how an industry can be disrupted.

It wasn't that long ago that we used payphones. I have four daughters who have never even used one. I'm not sure they've even seen a payphone. Yet there were successful companies that used to manufacture payphones and that are no longer in business thanks to the cell phone. And there are other companies that used to operate payphone concessions in airports that no longer exist. A lot of businesses that were once considered good either aren't around anymore or have lost relevance. As they fall out of the stock market indices a survivorship bias develops. Since December 2013 the S&P 500 Index compounded at 7 percent, but that's with numerous companies having been dropped from the Index. Importantly, the S&P's returns weren't harmed by those fading businesses. The stocks dropped from the Index for reasons of relative inferiority or worse, bankruptcy, declined 42 percent. The one thing we're certain of is change. It was not long ago that the average company's lifespan in the S&P 500 was 35 years. Thanks to a combination of tough industry conditions, poor business practices, and M&A, the average company's lifespan today is less than 25 years. Companies like JC Penny Abercrombie and Fitch, *The New York Times*, and Eastman-Kodak either aren't as relevant as they once were, have gone bankrupt or have become a smaller part of a larger organization. Innosight, the company that offers this chart, forecasted "about half of the S&P 500 will be replaced over the next ten years," with the average corporate lifespan in the Index dropping to less than 15 years. There are exceptions, of course. Some companies like General Electric, a current Crescent holding, have remained in the S&P 500 for more than half a century. Unlike GE, it's those companies facing insurmountable odds that we wish to avoid.

A company's fortunes will ebb and flow. We won't see all the tidal changes, but we do our best to understand a business and industry such that we can be prepared for the worst by retaining hope for the best. The companies in this slide encountered serious headwinds that they fought for years, but ultimately succumbed to the larger industry dynamic and filed for bankruptcy. There's some commonality here. Competition that was just too strong, technological disintermediation, poor management, a shrinking customer base, a product that lacks differentiation. One thing certainly of note is they all had red logos. Maybe the conclusion is to have a different color logo, but that didn't help Blockbuster.

I don't want to make light of this. Good people lost their jobs. Twenty years ago if you had a choice for a job at K-Mart or Walmart where would you have preferred to work? Walmart got and retained the better people. They put their customers first and ran the business like the owner-operators they were. Growth offered their employees more upward mobility. But now Walmart is facing its own challenges from the likes of Amazon. For our part, we hope to avoid headwinds and not lose money. We play defense first recognizing that good things can happen to cheap stocks. Nevertheless, we prefer a business that has, over time, at least some unit volume tailwind rather than owning a company that operates the proverbial melting ice cube of an industry. We'd also like these businesses to have some kind of moat and a good return on capital in a normalized environment. We don't try and anticipate what a company might earn in a given year let alone quarter or month. Instead we try and figure out what's normal through a cycle and build our models with a more simplistic low, base and high case. In building our base-case we generally have numbers that we believe are quite attainable and should it come to pass we'd likely end up with a decent IRR. Our low-case shouldn't cause us to lose too much, while our high-case would deliver a great return. To help us better understand a business so that we can build our low, base and high-cases, and then handicap them, we spend a fair amount of time with management. We like the owner-operators, who have a competitive drive, an appropriate vision and plan, and have the ability to execute on that plan and treat the company's cash as if it's their own, because it is.

Revisiting this depiction of risk and reward, the question is always, how far is the drop? What lies below? Is what's on the other side of enough value to make the leap? We don't want a long drop and decidedly deadly result without the prospect of payoff that justifies the jump. Our strong risk adjusted returns have been driven by avoiding these bad bets. As we often say, returns are driven not just by what you own but by what you don't. We prefer it when there's a short drop into some nice warm water if we miss. And there's some reasonable payoff on the other side should be successful. Sometimes when we make the leap we have to wait a long time to find out where we come down. As long as we believe a business' fundamentals and prospects are intact, we will maintain the position and even increase it should its price decline or we see that a favorable outcome will be sooner rather than later. The market solves for price, we solve for value. We do our work, establish what we think is an appropriate target purchase price that offers an attractive risk reward proposition, and then wait until the market price pushes it into our web.

We maintain a healthy respect for a hard earned dollar and we hate to lose any. But investments not working out is part of the process. We don't operate with that fear that can cloud judgment and cause one to forget how to make money. We've had good years and bad years, but overall have returned decently since our inception - exceeding our goals.

We consider our returns over a full market cycle. We have spoken ad nauseam about this and have a white paper on our website. But in summary we believe that the appropriate way to judge a manager is over longer time frames that include a bull and bear market. Crescent has achieved its goals over the two most recent market cycles with greater returns and smaller drawdowns than the benchmarks. But we haven't offered great returns in every period.

In the Internet bubble of the late 1990s from January '98 through March 2000 Crescent was 66 percentage points behind the market, 66. What a difference a few years makes. Taking that horrible beginning and stretching it to 2002, Crescent ended up 44 points ahead of the market for the five years. In the middle of the market cycle all kinds of noise can show up. And the Internet bubble put up a kind of racket we haven't heard before or since.

Doing well over the long-term doesn't mean doing well every year or even the majority of years. Crescent accomplished its objective compounding better than the market despite underperforming the S&P 500 in 13 of 23 years. It's the tortoise versus the hare. This has worked for us because when we have outperformed it has been by an amount greater and great enough to outweigh inevitable times when we underperform.

We've outperformed our balanced benchmark, but we've underperformed in ten of the years.

We have beaten the MSCI ACWI since that index became more relevant for Crescent beginning in 2007, but we've underperformed in more years than we've outperformed.

For the most part, Crescent has outperformed in markets where the returns are less than ten percent. On a rolling 5-year basis we've outperformed in all of those losing periods and 97.5 percent of the time when returns fell between zero and 10 percent. In a robust market, though, Crescent has underperformed more often than not, beating the market in just 15 percent of the instances. When it all shakes out Crescent has met, actually exceeded, its goal of doing at least as well as the market indices but with more downside protection.

We attribute our solid performance, historically, to security selection. Since this most recent market cycle began in 2007, our long book has outperformed the relevant benchmarks. Crescent stocks beat the S&P in six of nine years, and when we underperformed it was by not more than a couple of points. When we outperformed it was by an average of a bit over six percent. We did better still versus the S&P 500 Value Index which we outperformed every year. Versus the MSCI ACWI, we underperformed in one of those years, but the average alpha in our outperforming years was 7.5 percent.

Although we don’t know what will happen in the future we’d like to think that our consistent philosophy, regimented process, and disaster avoidance will allow for good future performance. Being a value investor means sometimes having a cross to bear. Our returns will disappoint at times. It might be because our security selection is dragging us down.

Maybe with a couple of mistakes in the portfolio or because we lack any great performers. More often than not, though, it has been because the businesses or sectors that are performing well are either priced too dearly or fail to offer an acceptable margin of safety, or there are other businesses with poor long-term fundamentals.

You may wish we'd gone on vacation starting January 2014 and just stayed there as the securities we sold have outperformed what we've purchased. Of those companies that had had positive earnings, though, the average PE of the companies we sold was 19 times and the average price to price to book of those same companies was 2.4 times. That's the section of the cells to the right. Of the companies we purchased the average PE and price to book was lower at 14.3 times and 1.9 times. We're value investors. You all know that. As it happens, at times, the companies are trading at 19 times earnings can move to 20 times, 22 times, 24 times or, really, anywhere. Owning high PE stocks is not our stock in trade, nor will it ever be. If we had to do it over again, and as much as we might've enjoyed some more time off in the last couple of years, we would still sell what was more expensive to purchase that which was cheaper.

We will continue to move the portfolio around as a function of opportunity, agnostic as to industry or asset class. This means at times we might own a lot of one industry while at times none of another. I'll go through some examples. We didn't own financials for years. A stretch of time when they were overpriced, had overlevered balance sheets and a lower quality loan book with inadequate reserves. Not having that exposure helped our performance in the last decade. Stock prices of banks have since declined and their balance sheets and loan books, and reserving have all gotten better, so we've increased our exposure.

We didn't used to own any large cap technology companies either, but now we have 13 percent. Similarly, nothing of mortgage loans became something, but is on its way back to nothing. We used to own a lot of energy, but two things caused us to reduce that exposure dramatically. One, thanks to the technology of fracking and horizontal drilling we saw the potential for supply shocks. Five million additional barrels of oil per day are now produced in the U.S. versus a decade ago. A doubling which has clearly put pressure on the price of oil. And, two, we recognized, slowly, that these companies just weren't good allocators of capital.

Flexibility has allowed us to increase our geographic breadth. The Fund’s global footprint now extends to 45 percent of the companies we own being domiciled outside the United States totaling 25 percent of the equity exposure. More importantly, almost 60 percent of the revenues of the companies we own come from outside the U.S. Herein lies the reason for using the MSCI ACWI as one benchmark. As a side note, in consideration of alternate indices, 48 percent of the companies we currently own are not even in the S&P 500, totaling 22 percent of the Fund’s equity exposure. If one could only invest in U.S. companies then one’s forced to shop at a store that’s priced on the high side. With blue being low and red being high. But if you’re able to expand your horizons a lot more blue shows up reflecting less expensive companies in other parts of the world.

We also offer some breadth and exposure to companies of varied size. Five percent of the companies we own have market caps less than five billion dollars. Another five percent are between five and ten billion dollars. And a total of around 16 percent have market capitalizations of less than 20 billion. Despite the fact that we can invest in many different areas the correlation between them can be quite high. If one industry is expensive, another one very well might be too. The same applies to asset classes or regions. As a result, our risk exposure varies over time as a function of price. Breadth gives us more investment options, but we won't sacrifice an appropriate risk reward just to be invested for the sake of keeping up with the market. We're not afraid of putting capital to work. We just choose to do so selectively. Our exposure to risk assets increases when the market is at a low ebb and decreases when the market is at a peak.

At least relative to ourselves, we know a good thing when we see it. An individual investment's risk reward drives our desire to be invested rather than some larger market view or some emotional need to be more like our peers should they be performing better than us for a time. When we are more invested the returns in the subsequent two years are greater than we were less invested. At the extremes, take a look at the bottom left and the upper right at the table. When the Fund was more than 80 percent invested its returns in the subsequent two years was 15 percent, but when less than 55 percent invested the return was just 6 percent. This is an uncertain time, but when isn't it? Our exposure today is middle of the road. We're running about 65 percent in net exposure. Most of our portfolio liquidity is derived from are far lower than normal high yield exposure.

Allow me to run through some reasons why we continue to take a cautious approach. The stock market's not cheap. P/Es are at their second highest levels in the past 100-plus years. This can be, of course, explained in part by interest rates being at all-time lows. It's not just on trailing P/Es calculated using ten-year average earnings that you see here that the market is at historically high levels. Using the 12-month median for P/E, price to sales and price to book, the S&P 500 is currently at or exceeding levels found at the last two market peaks in 2000 and 2007.

Declining interest rates in developed economies have been a major market driver for the last two or three decades. Low rates justified paying a certain price for an asset that a higher rate might not otherwise support. So a company can borrow to repurchase their shares or build a plant with a lower cost of capital. Consumers can afford a more expensive home. And those that live off a fixed income might be pushed to make investments in riskier assets.

At least in the U.S. we are relatively fortunate because in many other parts of the world rates are negative, or at least we're fortunate for now. You have to go out ten years or more in Germany and Japan to get a positive return. All of the other European countries listed in this table offer sovereign bonds at negative yields for four years and beyond. The blue bars that you see are the negative yields. Investors are now paying borrowers, primarily governments, for the right to hold $8 trillion worth of their money. It's actually more now. With residual equity value being greater thanks to a lower discount rate, companies are therefore more valuable, all else equal. Note the graphical depiction of the inversely correlated stock market to declining rates.

The expanding balance sheets of central banks have helped drive the market as well. At some point the nuttiness stops and eventually reverses. We just have no view as to when. There are unintended consequences of low rates. Certain businesses are structurally challenged like banks and insurance companies, but far closer to home, you know, it might be those accustomed with living off of a fixed income. They have less today than they had a decade ago. In this example that I lay out here, I lay out the investment portfolio of a retired person. I've given no credit to them for owning a home or benefiting from Social Security for the benefit of simplicity. This couple's life savings of $2.5 million is far, far greater than average. By comparison, 30 percent of the people older than 55 have no savings. Another 26 percent have less than $50,000 put away. A decade ago buying a 5-year Treasury would've given our hypothetical couple almost $90,000 in annual income. Today with lower rates it would be less than $30,000. So how does a couple combat that 67 percent decline in income? If they were accustomed to living off a fixed income they were left with just three choices: spend less and reduce your lifestyle, use principal to subsidize your income, or increase risk. More often than not option three is the chosen path. When increasing risk, familiarity drives the decision. They're used to investments with an income so they gravitate towards higher yielding investments first like junk bonds, MLPs or REITs. And there might be other higher dividend paying stocks and so on. This drove prices higher and yields lower.

The Wall Street Journal published this table last week that also shows the increasing need to assume risk to get return. If you want or needed a 7.5 percent return 20 years ago you could've had your whole portfolio in relatively conservative bonds. To achieve that same 7.5 percent return target a decade ago, half your portfolio would have to be public and private equities and real estate. You have no shot at 7.5 percent today with virtually any low risk, fixed income.

So capital flows to higher risk, fixed income pushing the yield-to-maturity of high yield bonds down to 8.6 percent. That's 1.7 percent below the historic average albeit with spreads a bit higher than norm. If it weren't for the many bonds of energy and metals and mining companies that trade at sizeable discounts to par, yields would be lower still. Although those industries have made back a small amount of the recent losses in 2016, thus far. For the most part, high yield bonds have performed well, attracting more investors in their quest for yield. The size of the high yield market is now about $2 trillion including leveraged loans. More than two times the size in 2007. A high yield market of this size has never seen an economic downturn. Even more remarkable is that's in its 30 odd year existence it has never experienced a rising rate environment. What's more, there's huge refinancing coming down the pike. With almost $1.5 trillion coming due between 2020 and '22, it'll be interesting to see how this plays out. We'll be happy to have liquidity available for the inevitable disruption.

U.S. Equity EFTs and Index funds continue to be the fastest growing segment of the mutual fund marketplace and now total $4 trillion or 34 percent of the U.S. Equity Fund Market. With ETFs and Index funds being indiscriminate buyers and sellers, if the flows were reversed in any kind of size we'd expect it to create some bargains. As support for ETFs as a market driver look how closely the high yield market has been tracking high yield ETF flows over the last year or so. If there's a large exodus from high yield ETFs, we'd guess that most investors don't recognize how small the exit might be for those trying to find their way through it. Such a liquidity of junk bonds would then justify the premium we are currently paying to maintain the liquidity of cash. We'd be happy to deliver our cash to a forced or panicked seller in exchange for a bond of both good quality and high yield.

Meanwhile, although not horrible, we're not exactly living in a robust economic environment. In the U.S. this is about as bad an economic recovery relative to the size of the downturn that we've ever seen.

This isn't a surprise given the slowing trajectory of U.S. economic growth which hasn't had a year above three percent real GDP growth in a full decade for the first time in its history. Europe's not exactly doing well either. Japan's worse still. And China, while still exhibiting 6, 7, percent real GDP growth, isn't the global engine it once was. What little growth we've gotten has been thanks, in part, to an increasing borrowing base. In the past five years the change in GDP is a function of the five-year change in debt and the U.S. continues to decline. In other words, we've had diminishing returns on our ballooning debt. It's ironic, as we said before, that what we can't afford individually we can somehow, as a nation, afford collectively. Diminishing returns on increasing government debt is a story being played out overseas as well.

President Obama's own econometrics firm, the OMB, expects that our rising national debt, combined with increased spending and a high rate of interest, will cause in just under a decade our interest expense to make up 13.9 percent of our federal budget, about double its current level. We can only wonder where Peter will borrow to pay Paul if this comes to pass.

The policy response to this higher level of debt is to try to inflate our way of it. That is generally deemed the politically acceptable path rather than austerity or default. This shot of the money stock depicts the powder keg, but we have yet to determine what will finally ignite it. We don't see inflation around the corner anytime soon and suspect that we're on a deflationary path to inflation. Maybe that's, in part, due to an underutilized labor force. Too many people are not working at their ideal job. Wage growth has been poor and a lot of people have just given up and exited the workforce. If as many people wanted to work today as wanted to work in 2007, unemployment would be 9.3 percent rather than the reported, far more politically appealing, five percent.

So I don't end my part on a downer, I'd like to point out it's not all bad out there. U.S. household debt service payments have declined as a percent of disposal income. It's the lowest it's been in more than three decades. U.S. natural gas prices remain low, stimulative, along with oil price, also stimulative. And along with these metrics I probably should include a slide of housing starts which are still running under 1.2 million annually. Getting back to normal would probably mean at least another few hundred thousand homes. Lastly, I can't help but share this recently published chart that shows value stocks have had the longest losing streak since the Great Depression. That's bound to change, someday.

Let me now turn it over to Brian Selmo to begin to walk through some investment examples. Thanks.

[APPLAUSE]

Brian: Thanks. Thanks, Steve. As Steve mentioned I'm Brian. I co-manage the Contrarian strategy with Steve and Mark. Before I get started I'd like to thank Mark Hancock and his group for putting on this weekend. They take care of all the arrangements and setup. And, in particular, I'd thank Dan Grimm for helping me put together the slides you're about to see.

So I'm going to talk for a little bit about the credit exposure in the Fund and go over our process as well as one bond that we own currently.

So, first, in terms of credit, what we're looking for or what we're doing is really three different types of investments. One, performing loans. So these are the top of the credit structure. These would be bonds or bank debt that we expect to make interest and principle payments whether in or out of bankruptcy. And we're looking to earn 10 percent plus or L + 700 type returns on them. Moving down the credit spectrum would be stressed bonds. These would be bonds, typically senior bonds, maybe not the senior-most part of the capital structure, but debt trading anywhere from 50 from 70 cents on the dollar or there's some reasonable probability that the company's going to go through a restructuring. We buy these on a two-pronged approach. One, we want an attractive yield-to-maturity or contractual yield to improve credit, 15 percent plus. And, second and importantly, we want to create the underlying company or the assets at a price that we'd be happy to own the new co, the equity or whatever we might be issued as part of the restructuring, if it were to go that way. So even though these are stressed or distressed credits, they're underlying assets that we're attracted to and we think are of high quality. The most junior in the capital structure when we're thinking about credit would be reorganization bonds. These will be bonds that are either already in bankruptcy or very likely to go through a restructuring. And this would be the part of the capital structure that's going to be issued new equity as part of the transaction or part of the process. And this would be a situation where we're doing similar work as we would on any other equity except with the added complexity of the bankruptcy case. And here we're looking to create the new, better financed re-organized company at an attractive entry price.

So where have we been in credit? If you go over—and I think Steve had this similar slide—the history of the Fund we're very opportunistic so the credit exposure generally responds to our opportunities in the market here depicted by option adjusted spreads. Credit exposure peaked during the financial crisis at up over 30 percent, got down to about 1 percent in 2014, which was a time of very low starting yields as well as low spreads on high yield bonds. And then in the last 12 to 18 months we've seen the credit exposure start to pick up again. We're up to around 5 or 6 percent. And this is in response to wider spreads and greater opportunity. I would think this trend continues over time in terms of this pattern of us having more exposure and credit when yields are wider on high yield and less exposure when yields are more narrow. And it's, in some ways, impacted, also, by the absolute or starting yield on bonds. When the starting yield is 5, 6, 7, 8 percent on Treasuries you don't need quite as much spread on your debt in order to achieve an equity-like return.

Now, in the last 18 months what's happened is, you can see here, is that the yield on the energy and metals and mining bond parts of the high yield market have been more than double the rest of the high yield market. And so what this means is that that's been the area most distressed. So Mark's going to come up a little bit later and talk about high qualities and compounders, businesses and industries we follow and want to be in, just kind of a question of when in price. On the debt side we're really running to fires. So these aren't necessarily going to be businesses or assets where we spent a long period of time pining away to get a chance to own them. It's going to be in response to credit spreads blowing out like this, where we start chasing the opportunity and spooling up and learning about what the opportunity set might be.

So, in particular, last year Chris Lozano and Sean Korduner spent a bunch of time looking at the coal industry and at the natural gas industry. Now these are stock prices, but you can see both industries have been crushed, gone through a number of restructurings, continuing to be under stress. And they would've been markets that we wouldn't have spent a bunch of time following prior to last year and prior to the stress developing in the credit market.

So Chris spent a bunch of time on coal. Sean spent time on natural gas. And before we bought bonds or before we invested in companies we wanted to understand what the backdrop was, what the industry looked like and what the assets were that we were looking for. So we had to make some conclusions on the demand and supply. Now, we're not building some kind of complex model where we've got to necessarily set price and where we think coal or gas is, but we need to understand, as Steve mentioned, what the headwinds and tailwinds are. So in coal we would've said that we would guess that over the next five or ten years demand for thermal coal in the U.S. is going to be down somewhere like 30 to 50 percent. On the other side of that from natural gas we think there's probably secular growth there. One, replacing the demand from coal for electric generation in the U.S., and then, two, satisfying international demand of LNG which as those facilities get built will take up some of the U.S. gas supply. And then when thinking about commodity assets we want to not only understand what the demand might be, but then for individual companies, individual mines, individual assets we need to understand where they sit on the cost curve. Because it doesn't really do us much good to have the demand picture roughly right if we end up buying assets that are not going to be relevant in the environment that develops.

So that is a background. We went looking through the credits that had been displaced and one that has become our largest investment is Consol Senior Bonds. So Consol is a situation where we think it's a business made up of very high quality assets in a deeply stressed and distressed industry. So specifically the major assets at Consol, and they've got a disparate set of assets. But the ones that really drive or carry most of the freight in terms of value are coal and natural gas assets. So I'm going to briefly review the company's coal and natural gas position, and then go over how we thought about the value, and then what we think the investment opportunity was.

So Consol, this is a picture of their gas assets, has significant gas assets in the Marcellus down here in the southwestern Pennsylvania area, and then in the Utica in the northeastern Ohio area. So these are the most attractive maybe with the exception of northeastern Marcellus. But the really most attractive areas to drill for natural gas in the U.S. is really the part of the country that's likely to supply all of the growth over the next five or ten years. And so in the case of Consol they have a massive acreage position. And something that's interesting and exciting, you can see in purple, this is actually acreage that's owned outright. Almost all oil and gas companies don't really own the underlying property or the minerals. They just lease it. Consol has an advantaged position, again, in these very productive counties by virtue of their long history and an outright ownership position.

So, we're able to determine that they have an attractive acreage position. And then in looking at the company's results we can see their finding and development costs are highly competitive. So not only are they in the right geography, but they've shown a proven ability to operate as a low cost finder and developer of gas. This leads us to conclude the gas assets or Consol are economically relevant and likely to be productive over the next five or ten years.

Now if I move over to the company's coal assets, the major coal mines at Consol are a thermal mine here in Pennsylvania and then a mine that's been sold in West Virginia which is a Met coal asset in Virginia. You see on the bottom long lifed, recently mechanized, largely automated. Another important attribute of the thermal coal assets is the company got out of their legacy assets, sold them to Murray and those with a long… with that assets sale when a lot of the legacy liabilities. And so on the coal side if we think the market for coal is going to decline dramatically it's very important to be in a low cost position. You can see here the history of these mines is that they've earned about twice the margin of other peers. So that would suggest a very low cost position in the thermal coal assets. But we wouldn't want to stop at kind of just want the company presents or looking at the comps. What Chris would've done is gotten Wood Mackenzie data. And this would be a consulting firm that gets mine by mine information where you can get to the cost curve of each individual mine. We would've narrowed that down to what we think are the six or seven mines in the country that are going to survive, be profitable, and make sense over this declining environment of coal demand. One of those mines would've been the Baily Complex for Consol.

So after building up that understanding it was important to also, in terms of their cost position, also understand what the defensibleness of their position is being here in Pennsylvania. So the load-base for coal electric production is all right through here. So Consol's position geographically creates an advantaged transportation versus mines that are low cost in Illinois and out here in the Powder River Basin. So taking that in combination we think about even if the coal demand is going to be down some 50-odd percent, what the pricing umbrella might be and what the earnings power might be in that reasonable worst case scenario for Consol's coal mines.

In terms of summing up or taking away what we're trying to do on credit, we want to be into bonds with attractive yield-to-maturity. So if everything goes well, we make equity plus returns, and if it turns out that the downturn is worse or something happens at the company or the capital markets close and they can't refinance, we want to be super comfortable in terms of the assets that we're buying through the debt.

[APPLAUSE]

Steve: We've left time for Q&A. So I thought we'd just turn it over to you and make it more interactive. So I don't know. Do we have microphones floating around? Yes, we do. So I'm going to stand up here with this—hard to see out there. Go ahead.

Q: Can you talk about Alcoa in terms of the break up and what you're looking for there, and then you can you talk about GE and what you're looking for long-term as it makes its changes?

Brian: I'd encourage you, also, to ask our speaker that Mark will introduce later who is both a leader in the advertising industry as well as a director at Alcoa. We're very encouraged by the break up at Alcoa. We're excited about the breakup of Alcoa. We think it's the right move strategically. I think getting greater focus on the high performance, the engineered products business is a good idea, and I think there's room for improvement in that operation over time. So it's something we continue to expect to happen in the back half of this year, and then we'll see how the two pieces do.

Q = Question

Steve: It's been underinvested in.

Brian: And then on the GE side… I'm sorry, you were going to say?

Steve: Let's just stay on Alcoa for one second. That business has been underinvested in relative to the biggest known diversified competitor in Precision Castparts. So our hope is, is by having this division that you actually have a greater, clearer, better allocation in capital.

Brian: Yeah. And, look, they've underperformed Precision Castparts over time and this is going to make it very difficult for them to hide, I think, when you split the businesses apart. And there are strategic… certainly we'd be interested. I mean, Berkshire paid a very healthy price for PCP which is world-class in the space, but that valuation difference is going to be highlighted when the spin happens, I would think.

Mark: There's also been an improvement in the board?

Brian: Yeah. I mean, recently there have been three new directors added to Alcoa and I think that that's a step in the right direction also. It hasn't gotten a ton of press. It's a been friendly situation, but Elliott had taken a big position in the company and the company kind of, of their own volition, I suppose, or certainly at least willingly put on some directors with some particular expertise in aerospace and in auto, and then someone with some corporate finance expertise which also hopefully will be helpful. And then on GE I wasn't sure…

Q: Oh, just more on the future in terms of how you're looking at it, in terms of improving the price you bought it at, and where you want to take it.

Brian: GE was something that when we got into it they had an investor day December '14 where they essentially said they were going to break up the business and get rid of the finance side. Kind of nobody believed them. The stock went down. We bought it, and then a month or something later they said, "No, we're really going to break it up and we're going to do it in 16 months," or something, and then since then the stock's gone up. I mean, GE continues to have a little bit of a bloated overhead structure. There's been some discussion about what they can do in margin, but it's a series of world-class businesses that, I think, was cheap when we bought them and now is at more fair price.

Mark: GE was very much bought under the guise of a compounder where if we looked out three years it was hard to think that we'd lose money given the proportion of revenue that comes from the aftermarket across all their different industrial exposures. And so it's not necessarily that we… you want to fill in? The thought was it would double. So we had a freebie on the fact that it was going to split off, the financial services, and maybe then the industrial business would get a bit of a rerating. And we were confident in the earnings power as well. Energy's in there, but they'd already started to take it on chin when we got involved.

Steve: There's a lot to be said for companies that get too big and they get too many different divisions to be run and managed effectively, and there's competing interest for that capital. And to some degree there's arguments that this was a job retention act for the CEO because there are people engaged who said if you don't perform you're going to not have a job and we're going to make things happen, which is a favorable statement for activism. Activism keeps people honest.

Mark: If you go back to the conference call where the break up was announced, the first question was from the Barclays? Was from an analyst who says okay, I guess you get to keep your job now. On the GE call when they announced the spin. So there was clearly movement afoot and pressure was felt.

Q: Can you talk to us a little bit about the size of the Fund and if that prevents you from investing in some smaller companies or debt issues? I

Q = Question

know you guys have been closed in the past. I just wondered how you guys see things.

Steve: We've taken the stance for some time that we're not going to be on the road marketing and trying to raise capital, recognizing that if you are closed there is a certain… we find that small cap, mid cap chart… pull that out in the chart book, please—recognizing that it's hard. Managing a public fund when you have inflows to a rapid degree or outflows, redemption cycle, to any kind of great degree makes it more challenging to manage. So we do our best. It's more art than science. We're trying to balance and manage it. We're very comfortable with the capital that we're managing today.

There's no question that we're not going to be a… benefit from small cap exposure. But where one door closes another opens, and we're able to do other things and have a bigger team and many of whom you can meet today, and we can underwrite with greater breadth and greater depth which has allowed to go around the world and dig down into companies in ways that we weren't able to do previously. And when—do you have that one up Elliott? Okay, and if you also think about with small cap, when small cap's out of favor so is mid cap. I mean, when liquidity hits it hits a lot of different things together and this shows the correlation.

So if you look at the Russell 2000 versus the Russell Mid Cap, and we do have these solid mid cap businesses in our portfolio with roughly 10 percent, running less $10 billion, 10 percent of the invested book. It's a larger percentage of our exposure. So you can see on this chart right here which I'm sadly standing in front of, that when small caps are cheap, mid caps are cheap. When small caps are expensive, mid caps get more expensive. So these are the kinds of things that given that they move together we still feel a great ability to exercise our process in such a way…prosecute our process in such a way that we're able to meet our goals. If equity rates return with less risk in the market, avoiding those impairments of capital. And that's what we always circle back to when we think about… when we come in every day, can we meet our target, our goals that we've stated to all of you and to ourselves.

Mark: Only because we discussed aero today, I'm not sure what the technical cutoff is for small cap, but I'd say Esterline probably meets that regard…

Brian: Circa 2 billion market cap.

Mark: Yeah. And Meggitt's maybe in mid cap range, but just for that industry you can see how we can get exposure to those type of companies. We're not actively looking to invest in companies that have a sub-billion dollar market cap. Let's just put that out on the table. Every now and then a unique opportunity may present itself for some reason where there's liquidity that's sufficient for us to make those type of investments. So I'll say we passively watch those with a chance… if you look at Esterline, for example, we own 10 percent plus of the company because there was a block available that allowed us to get the liquidity. So we pay attention to these, but we're not actively looking. Those opportunities admittedly are no longer fertile hunting ground for the Fund, that's sub-billion.

Brian: Yeah. So we're focused on 2 billion-plus market cap from the equity side. Occasionally we end up with smaller ones and on the debt side we really need a billion-plus of issued debt and probably even a billion in trading value. But occasionally the same thing, a big, chunky seller's there or there's a bank debt placement or something like that, where actually, to Steve's point, being sizeable can help you get the allocation in some cases.

Steve: And I expect that when the next cycle rolls around, on the high yield side I'm talking about, and assuming that our capital is where it is today, who knows, I would expect… size does gives us a seat at the table in certain other types of financings which allow us to step up and participate in bank debt deals. We did some CIT, you know, bank debt back in, was it 2009? Along with—in the second tranche we didn't get to bite at the apple the first time, but we were able to step up and participate. Now, we were able to participate because we partnered with a New York-based firm because we couldn't take the whole 250 million dollar… or it was 220-40 million dollar block down ourselves. We had to share it with them. So it's the kind of thing we can now do ourselves. We can get that seat. People know that we are, you know, available capital for that. We have time for one more question, and again, we'll be available throughout the rest of the day. In the back.

Q: Could you just talk to sectors and maybe even specific companies that you dislike? I know you have a small, short position in a few companies as far as telecoms, utilities, and some of those names.

Steve: I mean, we try and stay away from the businesses that have those major headwinds, those structural challenges. We don't want to be the position

Q = Question

of talking publically about different companies we short, but certain industries and certain asset classes, as I mentioned, in the prepared remarks, you know, as people have gravitated to get something they're familiar with, with these higher yields, but we've been talking about MLPs in a very broad way for many years about how ridiculously they were priced. People didn't understand. These were still tied to the oil business. The real question surrounding their depreciation. Again, everything has a price. I'm not suggesting that all MLPs are bad by any stretch of the imagination, but prices get completely out of whack because people just bid things up. So we've stayed away from those things that have those higher yields. The market was getting more attractive so we… you can go back and look at our exposures relative to market valuations. I mean, not that we look at the market and say, oh, the market's cheap, let's get more invested. It has nothing to do with that. We're looking for companies from the bottoms-up. It so happens that when there's disarray that there's opportunity and our exposures go up when there's disarray. Things on average in the market are less expensive. So we want to, again, always avoid those more expensive companies and industries where it's attracting too much interest, where there's a sex to them, whether it be the

Internet and tech stocks back in 2000, but that can turn into an opportunity for us ten years later when people have kind of forgotten about them, and leaves things like Cisco and Intel, Microsoft, and Oracle into the portfolio.

All right, well listen. Thank you all very much. We'll look forward to speaking to you the rest of the day.

[APPLAUSE]

[END FILE]