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- Gwin: 00:00 Hello, and welcome to the Price-to-Value Podcast with Southeastern Asset Management, where our global investment team discusses the topics that are most top of mind for our clients from our Business, People Price point of view. We at Southeastern are long-term, concentrated, engaged value investors, and we seek to own high quality businesses, run by capable people, at a discounted price-to-intrinsic value, or P/V. I'm Gwin Myerberg, Global Head of Client Relations and Communications, and I'm joined today by Mason Hawkins, Founder and Chairman, Staley Cates, Vice-Chairman, and Ross Glotzbach, CEO and Head of Research.
- Gwin: 00:42 We announced today that Ross has transitioned from President to CEO of Southeastern, effective January 1st, 2019, as part of our long-term succession evolution, while Mason remains Chairman, and Staley remains Vice-Chairman. Additionally, Mason has agreed to sell a portion of his equity ownership, primarily to Ross, along with a few other operating leaders of the firm. Mason remains the largest shareholder in Southeastern and Staley the second largest. But now Mason, Staley and Ross will hold more equitable amounts of 24% to 34% each. Mason, can you start us out by discussing why we are making this announcement now, and how was Ross selected for the CEO role?

Mason: 01:24 Well, first we thought a great deal about and discussed Southeastern's management succession and future leadership for almost a decade. We're making the announcement now, to your question, because we believe Ross Glotzbach is the right chief executive for our company, hopefully for the next 43+ years. And because we have department leaders in COO Steve Fracchia, CFO Jessica Pressgrove, General Counsel Andy McCarroll, Risk Manager Jim Barton, Client Relations Partner, you, Gwin Myerberg. And head of trading, Doug Schrank. That will allow Ross to focus on investing and continue leading our global research efforts.

Mason: 02:20 Ross has been an important contributor to our investment success of the past 15 years or so that he's been here. He's hugely respected by all of our associates. Ross is the most humble team builder, leads by asking wise questions, is quick to give credit to others and immediately takes responsibility for our challenges. Most importantly, I'm confident Ross will protect our culture and improve our investing. On both scores, I think Ross Glotzbach is going to do a better job than I've done.

Mason: 03:00 Also, our board thought it was important for Southeastern Asset Management to remain independent, so we could continue to provide career opportunities for our team members and work without distraction for our clients. Ross assured Southeastern's independence when he agreed to buy a significant stake in our company. He will become Southeastern's third largest shareholder.

Gwin: 03:26 Mason, you talked about Ross protecting our culture. Can you talk a little bit about how you would define Southeastern's culture?

Mason: 03:34 I think our governing principles that you've seen in almost all of our publications clearly define our partnership investing culture and the values that we think are critically important. I won't read those, but to me, that delineates exactly who we are and why we think it's important to carry on with those front of mind.

Gwin: 04:04 Staley, you've been a mentor for Ross over the last 15 years that you've both been working together. How do you find working with him? What skills do you think will make him a good fit for this role?

Staley: 04:15 Well, I think the answer to both of those together is, and Mason alluded to some of it, but the team building part - getting everybody to work together in a calm way. He is first and foremost, calm. And I think that's a great thing in both the investment process and in running this company, which is the CEO part. We have found that we've all made each other better as far as questioning each other on names, versus if any of the three of us were maybe left to our own devices on the stock picking part. He's extremely smart. He's smarter than the two older people on the call here. He's probably better read. And he's already, and I've told multiple clients, he's already done a better job as research director up until now than I did because things are more systematic, things are clearer, things are better organized. The job he's done in the last few years as research director, to me, is prelude for what he can do as CEO.

Gwin: 05:24 Ross, now that we've embarrassed you a little bit by talking about how great you are, can you walk us through how you started at Southeastern? And did you always know that you wanted to be an investor?

Ross: 05:39 When I was growing up, I was always interested in finding things for less than they were worth, if it was a lemonade stand, or baseball cards, or some used video game business I tried in elementary school that got shut down. Eventually, that got me to investing. And I read through all the different kinds of investing, as others have. Value investing just far and away makes the most sense. I was lucky enough to get to know people at Southeastern that I could ask about investing. And I tried various other ways to learn about finance, so when it was time to graduate from college, I wrote Southeastern a letter, tried to work there. And they said "No." And that was probably a good move on their part because I didn't really know enough then. I'd just done some investing on my own, and I worked for Stephens for a little bit.

Ross: 06:39 Luckily, eventually Southeastern asked if I was still interested. They got me to do a research project on Deltic Timber, which they owned at the time. I came over and interviewed, and I guess it went all right. I quit Stephens the next day, and I've been here for almost 15 years at Southeastern. I started off as a junior analyst, just doing whatever anybody needed, and was able to gradually find some names that worked and get some more responsibility. But I still view myself as an analyst first and

foremost. That's still the most exciting part of all three of our jobs. And it's just wonderful to get to work here with all these great people.

- Ross: 07:24 You asked the question earlier about mentoring. The best kind of mentorship is people who lead by example, and that's Mason and Staley, just getting to see how they've built this company, lived their lives. And that's big shoes to fill, but I'm excited about it.
- Gwin: 07:43 Well, it's pretty unique to have three generations of leadership in place and actively working together. Can you talk a little bit, Ross, about what that's like on a day to day basis?
- Ross: 07:54 Yeah. I think we've touched on it a little bit. We feel like we make each other better. I mean, we agree definitely enough so that we're all on the same page, have the same kind of investing goals and principles. But we disagree enough, as well, so that the discussions are interesting, and we all learn things when they're over. Yesterday we were sitting in Staley's office talking about a way that we could be positively engaged with the company. And Mason and I had been there with them in person. [We] had an idea, and Staley had a better idea. We talked about the new idea with the company, and they got fired up about it. So we're pushing ahead on that, so that's pretty good.
- Ross: 08:39 And then just for the continuity that our clients want, in the unfortunate case if something happens to one of us, you've still got two. And that's pretty powerful as well. You can't find that in many businesses anywhere. We think it's a pretty unique situation.
- Gwin: 08:54 Well, on that note, Mason, I think probably the natural question is: What does this change mean for you for your day-to-day engagement at the firm? And how long do you plan to stay at Southeastern?
- Mason: 09:06 Well, on the first part, I'll remain Chairman of Southeastern and continue to lead our quarterly board meetings. This change obviously is going to provide more time to read, think and discuss investment opportunities. And, as Ross alluded to in our get-together yesterday, assist with the company management engagement, where we think it'd be helpful and productive. I guess it's obvious how we feel about this. But we have terrific people in London, Singapore, Australia and Memphis, and I certainly

enjoy working with and supporting them. I certainly hope to be able to do that for a long time, so we'll see.

- Gwin: 10:08 Staley, you talked before about how one of the positive aspects of Ross is his calm personality and being able to keep everybody pretty calm and rational in their decision making and discussions. What personalities come into play for the three of you when you're making decisions together?
- Staley: 10:27 Well, we could list the various personality traits, some of which would need to have us committed at Trembling Hills. But I think the more important part is actually deflecting the question a little bit into what comes out the other side. Meaning, yes, various personality stuff comes into play at the beginning of the process of going through a name. But the whole name of the game, and Ross's strength, is taking the personalities out of it, actually, and just distilling this down to the facts of the case, and Business, People, Price - the template that it's always been and always will be. Getting those questions answered, where it's all about the investment facts, actually, and totally minimizing the personalities. That's the goal.
- Gwin: 11:15 Mason, could you step back a little bit and talk about when you first founded Southeastern 40+ years ago? What inspired you to build the business back then?
- Mason: 11:26 Well, in late 1974, a nonperforming Real Estate loan portfolio and the control of the currency forced First Tennessee National Corp to cut their SG&A expenses by a third and to dramatically increase their loan loss reserves. I had joined First Tennessee Investment Management as Director of Research in June of 1974 to build and grow their asset management subsidiary. With pressure from the regulators, the bank's board and its Chairman, Ron Terry, mandated that all of the subs underneath the holding company cut their overhead in draconian kind of ways, even though none of the non-bank businesses had extended the bad credit.
- Mason: 12:34 This decision essentially catalyzed the creation of Southeastern Asset Management in 1975. And of course, we all had "PhDs" in Ace Greenberg's vernacular, of Bear Stearns' fame, who thought that it was mandatory for business success, these PhDs. And what he meant by that was you had to be "poor, hungry, and determined", so we

had that covered. And that's really the very rough description of the origins of Southeastern.

- Mason: 13:14 Importantly, we believed we could create an investment operation founded on Ben Graham's disciplines, where a margin of safety was a driving force for long-term, intelligent investing. We knew that if you got your appraisal approximately right, and bought at a large discount, you could deliver good returns with minimal risk. This approach contrasted *dramatically* with the two dominant trust investment companies and their promoted beliefs that you could make one decision and pay anything for a top business in America and get acceptable results. Not unlike the FANGS and indexing of today, big capital flowed into the "Nifty 50" at the expense of almost everything else. We were given many good businesses at bargain prices that delivered great returns for many years, while those preferred, "must have" stocks like Digital Equipment and Simplicity Pattern and AVON and Polaroid and Sears and Kmart, and most of the others in that universe of 50 collapsed by big, big numbers, or went away entirely, so that was part of it.
- Mason: 14:39 Sir John Templeton, who was from Winchester, Tennessee, was a huge inspiration and an enthusiastic encourager in Southeastern's creation. John was an invaluable mentor for me and stayed such in our formative years. And he later became a most valued client, so that's background on our origins.
- Gwin: 15:09 Can you talk a little more about what Southeastern was like in the early days, and maybe one of your most memorable experiences from the first 10 years or so?
- Mason: 15:18 Well, it was exciting to be able to report to the person you saw in the mirror in the morning. And yet, there were many disappointing, long days. Probably the most memorable experience is when we drove to Chattanooga, Tennessee and on up to the top of Lookout Mountain, where we stayed with my wife's parents, obviously because it was free. We made, I think, some 40 presentations to prospective clients. And we got almost across the board, a universal refrain, "Well, why don't you come back when you've got some gray hair?" I was 26 at the time and had a lot of gray hair, so it was a very most memorable experience to get back in a non-air-conditioned station wagon and drive back to Memphis with no business.

Mason: 16:36 I wish those people were still alive so that I could go back and show them that I don't have much hair, and all of it's gray. But anyway, You asked for one. I could go on all day long for memorable experiences, but that was a very memorable occasion that stuck with me.

Gwin: 16:58 Staley, could you maybe share one of your memorable experiences as well?

Staley: 17:02 Well, the early, most memorable, which would cover bad and good together would be the crash of '87 because one day before the market peak of '87, which was actually in August, is when I became a partner of Southeastern. So like on all timing on all things I recommend, it was immediately down. And then the crash itself was just an unbelievable lesson for an early analyst, ranging from cruising into that with literally 5% earnings yields, i.e, 20 PEs versus 10% government yields, and wondering how that could possibly work. And then of course, it didn't. And then seeing what happens to liquidity in a bear market.

Staley: 17:47 I remember calling a trading desk, because there was not Bloomberg, and on Marsh Mac [Marsh & McLennan Companies], there was an 11 point spread. It was something like 43 bid, 54 ask, or something, roughly a \$50 stock with roughly 11 point spread. And I remember that imprinting. And then the other thing was the virtues of holding cash as you come into something like that because we had a lot of cash going into it, and we put that to work and made a lot of money coming out the other side. And that was the good part of what can happen.

Gwin: 18:21 That's a pretty formative first day of being a partner at Southeastern. How do you take that away and apply it to a market like today, or to some of the other subsequent downturns that we've seen between then and now?

Staley: 18:36 Well, it gets to the coaching of many of the greats who have written about the investment process, which is just focusing on the inputs, not the outputs. The outputs will drive you crazy. The messages that come from stock prices, which is how most people take their messages, is so bizarre and flawed and all over the place, that you just have to only focus on the inputs, and every single day, just try to make the right decision fact-by-fact. That's not just a recipe for investment success, that's just the way to stay sane in this business, especially at a time like now as well,

or the internet bubble, or 1990, or that crash. It's just pretty common.

Gwin: 19:20 Ross, you've been at Southeastern for 15 years now. How have you seen Southeastern change over the past 15 years you've been here?

Ross: 19:29 Well, I think there's definitely much more that has not changed than changed. The principles that Mason and Staley have already talked about, we have not deviated from those one bit. We're still all about alignment, all about doing the right thing for our own money, all about bottom-up stock picking. And we haven't changed our discipline to chase stocks that people like, compounders, other things like that. I think that's very important. There are two things that have changed a little bit, one on the business side, one on the investing side. On the business side, I would say our talent level has gotten even broader. I mean, there are just more people who work at our company now. And that's a good thing.

Ross: 20:17 And I think you especially see that playing out internationally, where, when I joined, the International Fund [LLINX] was still relatively younger. It's turning 20 this year. It's got great teams on the ground, and we're really starting to see that in its results. We're very proud of that, and we're ready to keep it going. On the investing side of things, we have, I think like most value investors, learned even more about the virtues of the qualitative over the virtues of the quantitative. We still want both, but if you've got a 65 cent dollar with great partners and a great business that's getting stronger, and you can understand it, that might be better than the 60 cent dollar with questionable partners and a business that's less control and more volatile and just not as good. That's something that we've learned and keep learning.

Gwin: 21:21 Mason, with your gray hair and 40+ years now, what advice, if any, do you have for Ross for taking over as CEO?

Mason: 21:29 I'd keep doing what he's doing in terms of bringing our worldwide team together and leading our weekly research calls as we vet various investment opportunities. And just encouraging the behavior that he's exemplified in the last 15 years. He just said that more is the same than has changed. I hope almost everything that we've observed and witnessed from Ross carries on.

Gwin: 22:19 And Staley, I'll ask you the same. What advice would you have for Ross?

Staley: 22:23 Well, now that you're in charge of a team of investment professionals in an active value shop, as well as strong-willed operational heads, I would say now is a good time to start drinking. And then on the more serious, while I would like to answer that with "reach for the stars and do your best and keep on keeping on, and disruptive paradigms and go where the hockey puck's going to be," any magic bullet, it's not that at all. It's what Mason said. This is a marathon, not a sprint. It would just be the daily, any advice I have for him, he knows what that is in real time, versus a podcast sound bullet, so we'll keep going.

Gwin: 23:07 Ross, with all that in mind, what would you say is your vision for the firm going forward? Do you foresee any changes?

Ross: 23:17 Yes. The vision is a scary word that when CEOs start going off on those tangents, we often say, "Whoa." I definitely think there is, as has been a theme here, more staying the same than changing. We've got great principles that we were set up on over four decades ago. You don't want to mess that up. Of course, you want to get better. And I guess if I had to say a thing or two that we will be focused on, number one is delivering great absolute returns for our clients with a minimum amount of risk. You do that, you get the clients you deserve. You get the right companies, the right investee partners, and it makes a lot of the other stuff easier.

Ross: 23:58 And then I also just want to keep making Southeastern a great place to work, maybe make it even better. Then we'll get the right employees that we deserve, and the right long-term partners. And that's how you keep going for more decades. But there are no big targets on AUM or other things that are just artificial and the wrong way to run the business. We just want to keep doing the right thing and stay at it.

Gwin: 24:26 One of the key ideas of your evolution, Ross, over the past couple years has been to allow Mason and Staley to focus more exclusively on investing, which is where their passion and best value-add for clients. Staley, can you end us by talking about what opportunities you're most excited about today?

- Staley: 24:43 Yes, I would come at that two different ways. One would be on the opportunity that, to me, is most compelling: and that would be in the category of time arbitrage, the short-term versus the long-term. I think the reason that's so compelling today is in a society that is so, so, so short-term oriented, that's what creates those arbitrages. But then also, with all the quant power and the competition out there and the things that people assume make markets more efficient, all that quant power and things like that actually don't close time arbs. They are focused on short-term and quarter and things like that, so it's both the cause of the opportunity, and it's why we get the inefficiency writ large.
- Staley: 25:32 For example, FedEx is having big problems in their current year, and earnings guidance warnings and whatnot. And the long-term could not be more detached from that. CenturyLink, our largest position, is painted as an old legacy phone company. It is all about Metro Fiber in the long haul. That is an incredible difference in perception. General Electric has been a story that everyone is familiar with, and a total mess. And coming out the other end of the pipe, you're going to have an incredible aviation business and an incredible medical business with one of the best CEOs out there. I think just that category that covers a lot of geographies and a lot of names would be the thing I'm most excited about looking at it that way.
- Staley: 26:17 And then the second way would be geographically. I just think our Non-U.S. right now, led by the Asian meltdown and U.S., China stuff going on, leads us to some Asian bargains that will thrive despite all that stuff. And likewise, Europe has all kind of problems that are real and that are in the media every day. But a couple of our foundational holdings there are just going to have a fantastic three, five, 10-year future. And so we're very excited about those.
- Gwin: 26:52 Thank you Mason, Staley, and Ross. And thank you to all of our listeners for tuning into the P/V Podcast with Southeastern Asset Management. We hope you enjoyed the discussion, and we look forward to speaking with you again soon. If you have any questions or would like to share topics that you'd like to see us cover in future episodes, please feel free to send us an email at podcast@SEasset.com.