Partners' Conference
May 8, 2014

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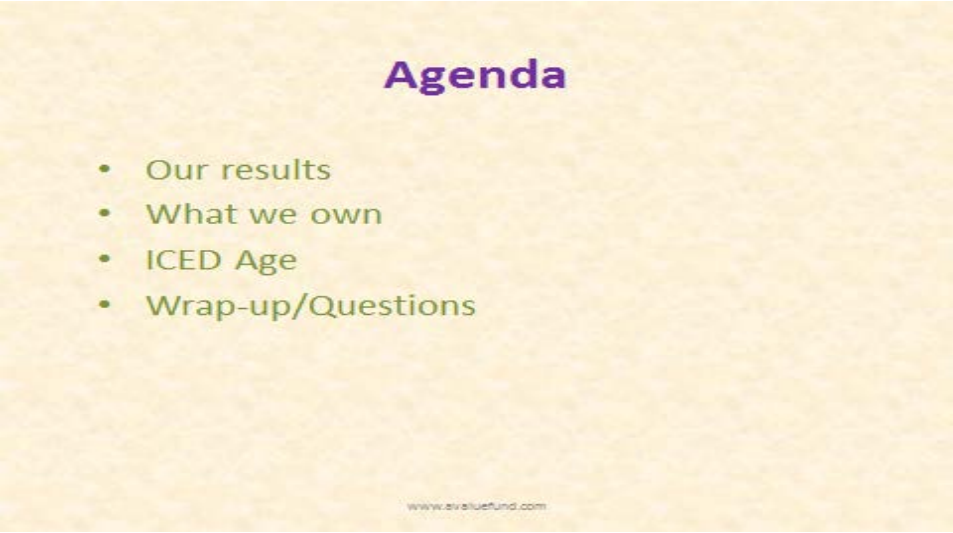
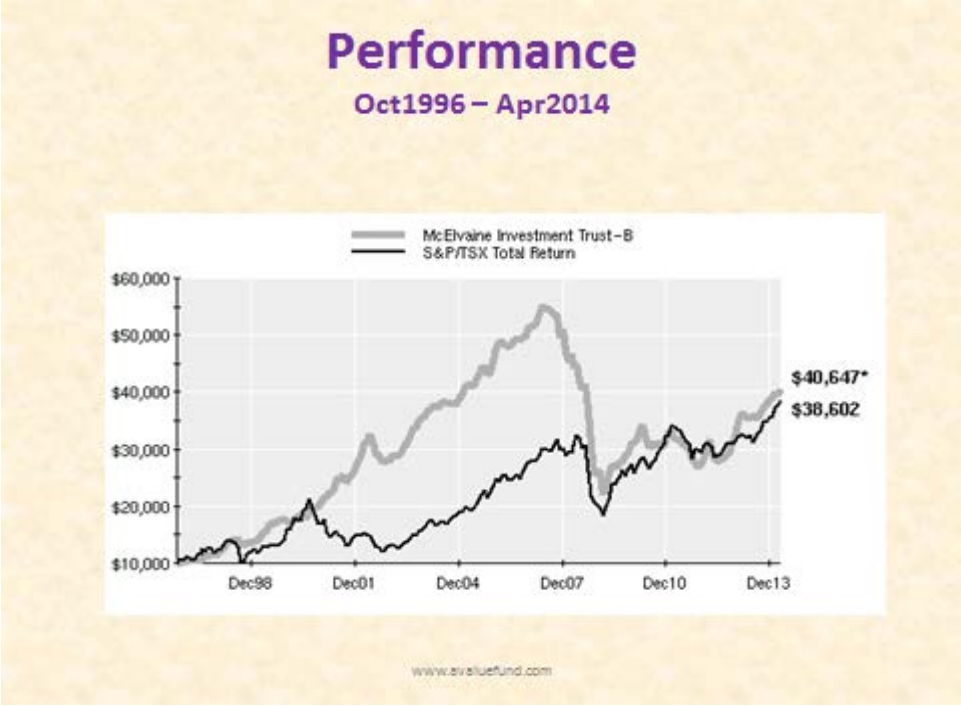
Tim McElvaine:

It is great to see everyone and thanks very much for coming today. Most importantly, thanks for your support over the years. I see a number of good friends and I want to thank you very much for your friendship. When I'm on the topic of thanking, I want to thank Shannon, who you met on your way in, and thanks for my extraordinary and beautiful wife Kate, for all that you do. And thank you to Kim and Di. Diann's not here with us, but Kim's right here. And I miss you Kim, but life goes on.



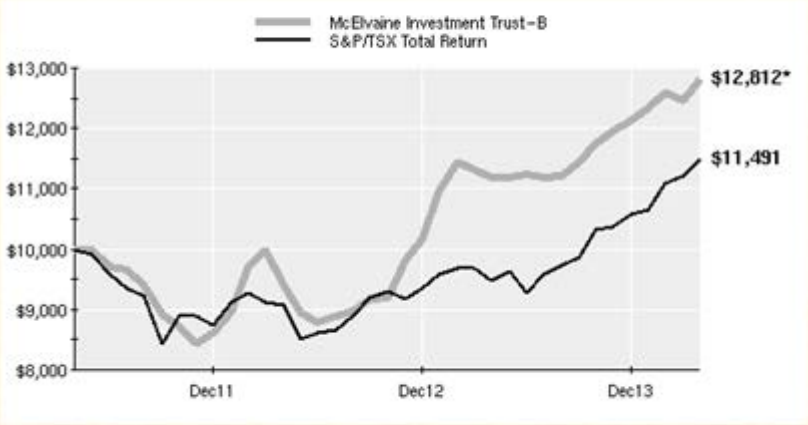
Here is my disclaimer and the agenda, I'll skip over that and move right to performance.



Performance, we're still tracking a little bit better than the TSX over a long time. More importantly, over the last three years since we instituted some of the changes that I talked about in 2011, we're doing better than the TSX with much higher cash balance. There are some copies of the annual report out there as well on our website. So I won't really spend a lot of time on these slides, but that's how we went from return on investments to the net return. And that's where the return on investments came from.

Performance

Last 3 years (with roughly 20% avg cash balances)



Investment Returns vs. Your Returns

for year to December 31, 2013
(Tim's estimates and unaudited)

Returns from investments	20.7%
Operating expenses and related taxes	-0.5%
Return pre-management and pre-incentive fee	20.2%
Management fee	-1.0%
Incentive fee	0%
Taxes on fees	-0.1%
Net return to you	**19.1%**

Returns from Investments

for year to December 31, 2013
(Tim's estimates and unaudited)

Canada related	4.9%
US related	10.8%
Japan related	5.5%
Europe related	-0.5%
Return from investments	**20.7%**

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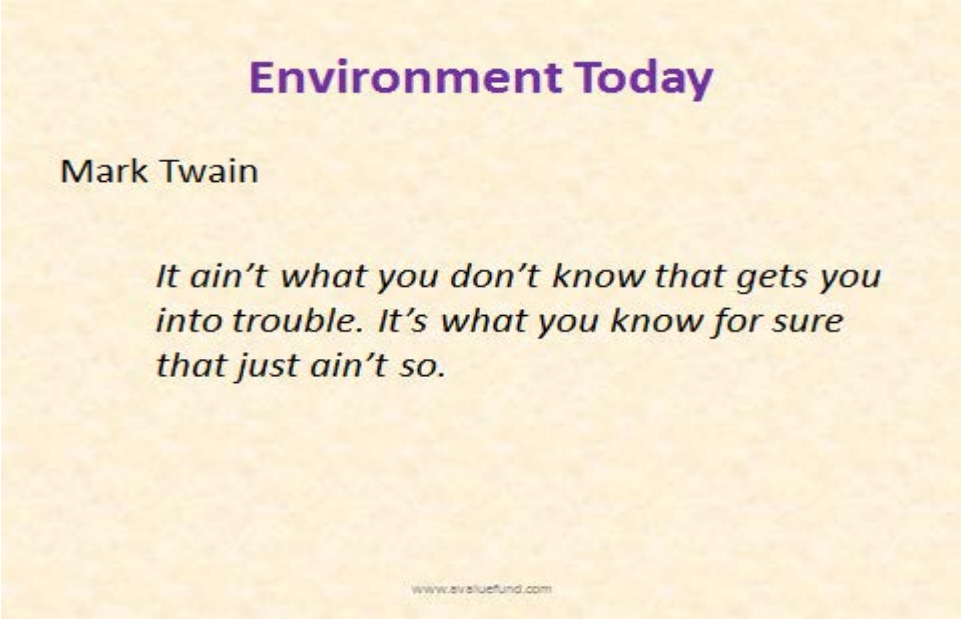
The Canadian stuff was really impacted by EGI Financial if you recall. We spoke about it a couple of years ago. They sold their US division and made some changes, and that was the bulk of our Canadian return, which also was helped by Legumex Walker and Village Farms, which I'll talk to.

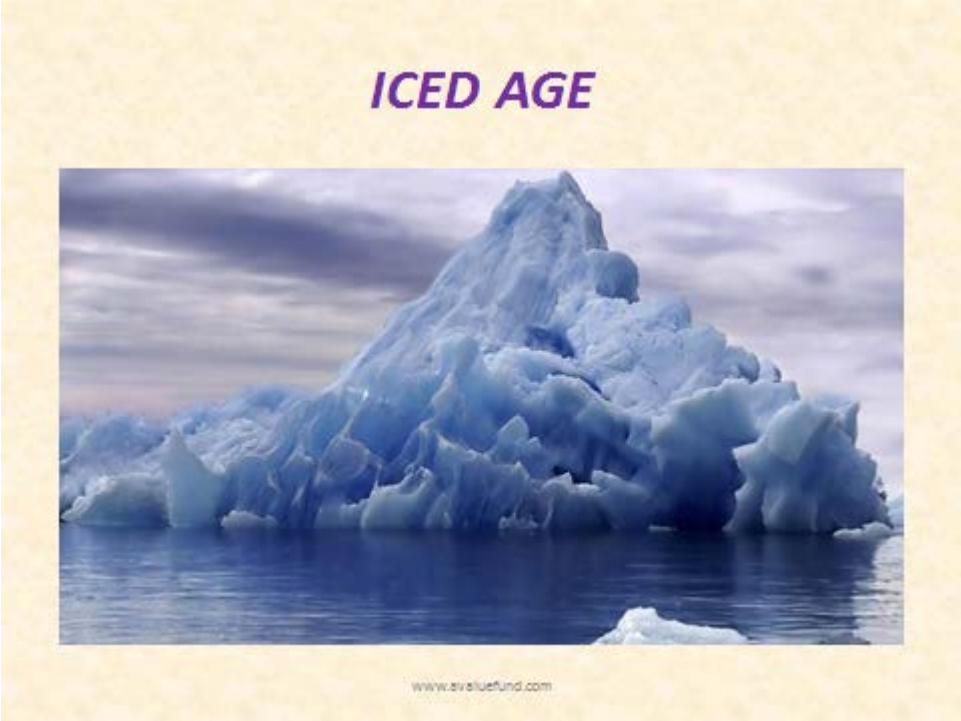
Our US holding returns were really generated by Howard Hughes Corp., which we talked about at last year's conference, has now been sold. H&R Block, which we've sold and Voya Financial, which we continue to hold and we spoke about last year as well.

Japan was really Monex Group. We continue to own, but in a much, much smaller position. We hold about a 2 or 2.5% position now, and it's our only Japanese holding. And Europe was Europe.

Dealing with ideas from last year, as I mentioned, we have now sold our remaining Howard Hughes. We'll talk a little bit more about RHJ towards the end. Voya Financial trades in the mid 30s. It's still quite cheap and we haven't sold any. If you recall, it was a distress sale by ING Group in Europe. We bought it as a dislocation, which I'll talk to more in a second, and we continue to hold it.



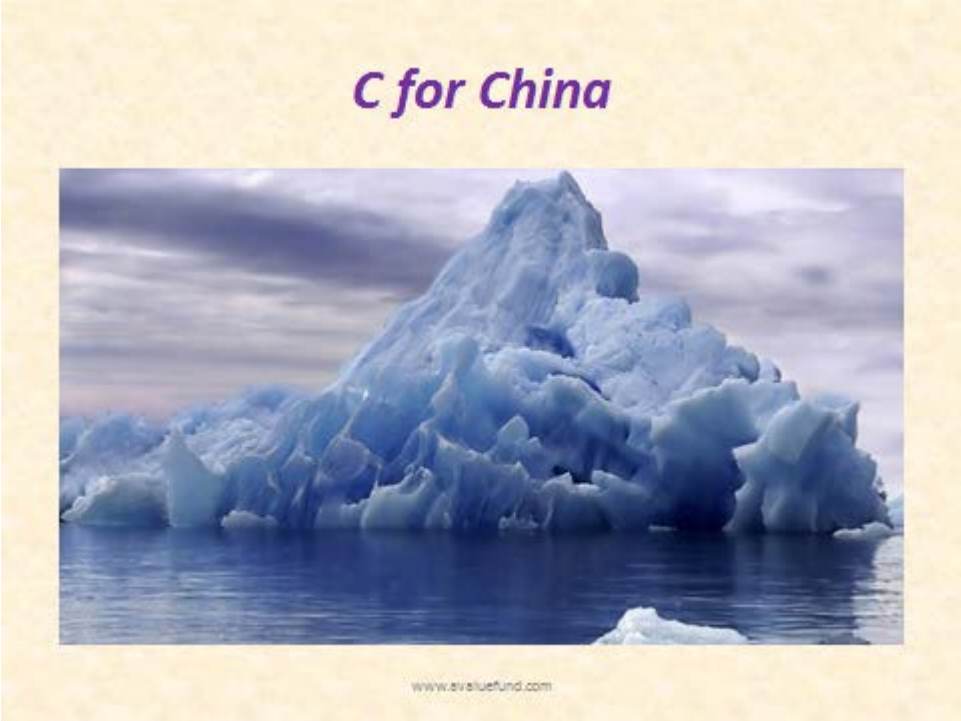
So I thought I'd flip it around a little bit first and talk a little bit about what's going on and then narrow in to about four or five specific names of stuff that we're doing. I'll start with the Mark Twain comment, "It ain't what you don't know that gets you into trouble. It's what you know for sure that just ain't so." And watching BNN and CNBC in the morning, which I try not to do, but I was in the hotel this morning, so couldn't help but watch them, this quote certainly comes to mind.



I'll flip through these few slides first. The ICED age thing I think still applies.

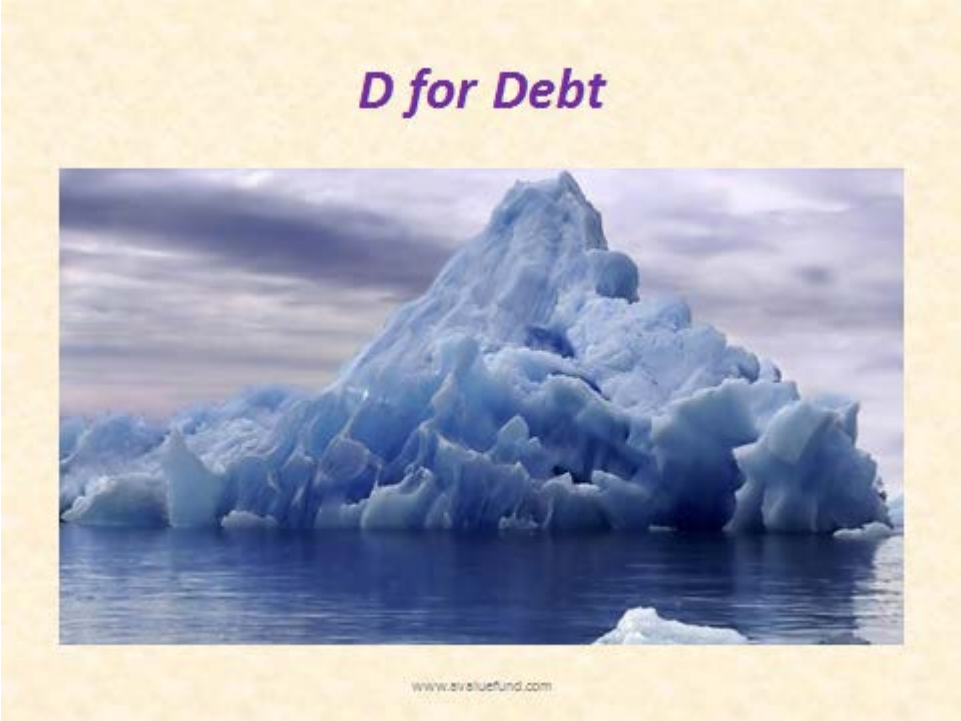
I is for Iran or the Middle East generally.

C is for China

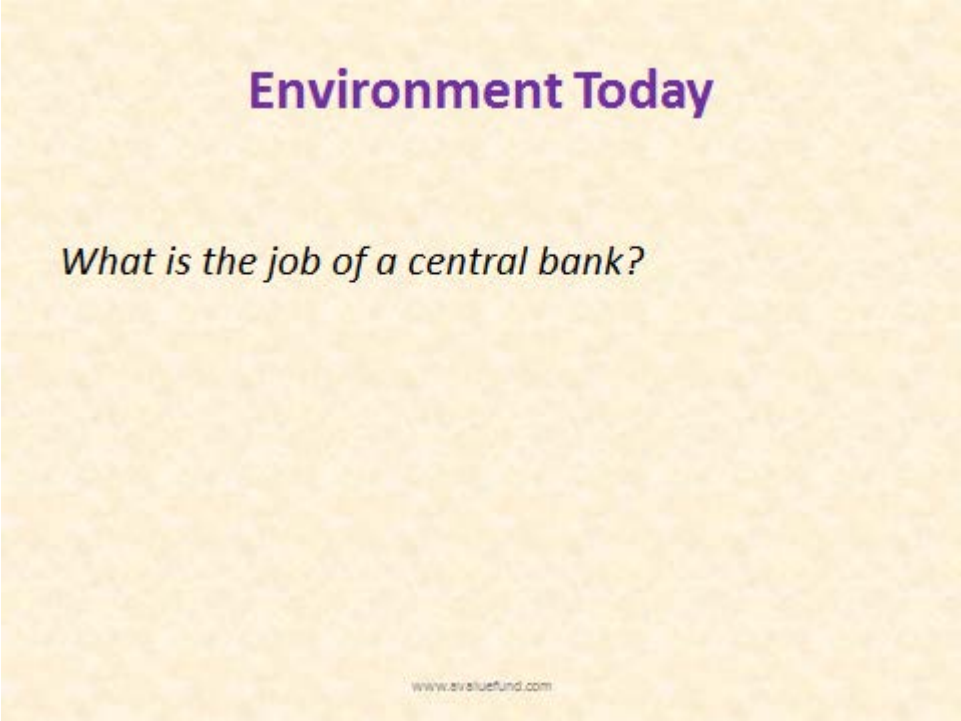


E is for Europe

and D is for Debt



These things were hanging out there as problems, and I don’t think any of them have been resolved, and I’ll touch on it a little bit more as we go along.

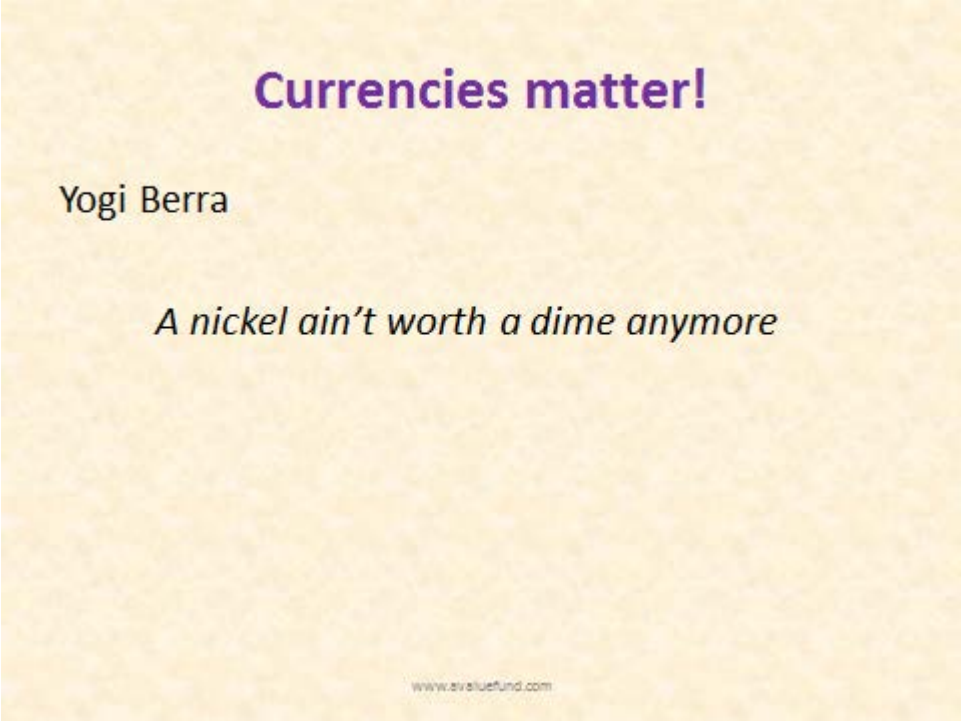


I posed these questions last year, and they're a little bit redundant. I don't really expect to give you an answer, but five years ago it was laissez faire. Certainly in the equity markets, maybe six years ago, it was government stay out of the way. Today of course it's, "what's the central bank going to do for us"? What have they done for us lately? So it's interesting to watch the pendulum swing back and forth.

The other interesting part is fiscal policy has been more or less neutered as you look around the world. And you're left with a whole bunch of monetary policy which doesn't

seem to have a whole bunch of alternatives left. It's a curious time. But as I was saying to Bill a little bit earlier, I started with Peter in 1991 and I've never known a time where I was pretty confident and certain about the future. So from that point of view, it's the same as always.

The final point is, when you have a government sitting in there, whether or not it's fixing wages or the interest rate, what type of distortions does that create over time? I think we're still trying to sort that out a little bit, and you're certainly seeing it in a whole bunch of different areas of the economy. And then how the heck do we get out of this thing?



I want to talk for a moment about currencies because this is an area I think that's a little bit underappreciated, but has an enormous impact, I think, on both companies and returns. As Yogi Berra said, "A nickel ain't worth a dime anymore."

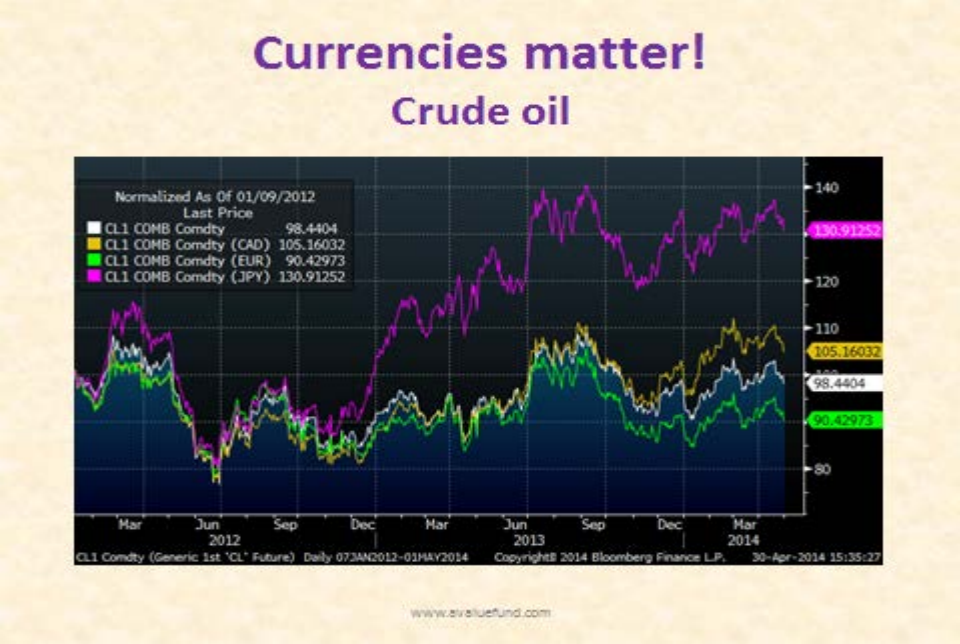
That is the case with our dollar, so to speak, and that's a chart I'm sure you're all quite familiar with. That's going from wherever it was, about—a little over $1.60 CAD to USD which I recall at a Cundill conference people talking about we should peg to the US dollar at $0.65 or something like that. Thank goodness we didn't do that. And now we're, say $1.10.

More interestingly, this is a chart of the US dollar against the basket of currencies. It's not ideal, but the important point the high price was in 2001. That was when the US was at its peak as far as the strength of its currency and it's been a downward slide since then with the exception of the last little while. And I'm going to talk to that for a second.

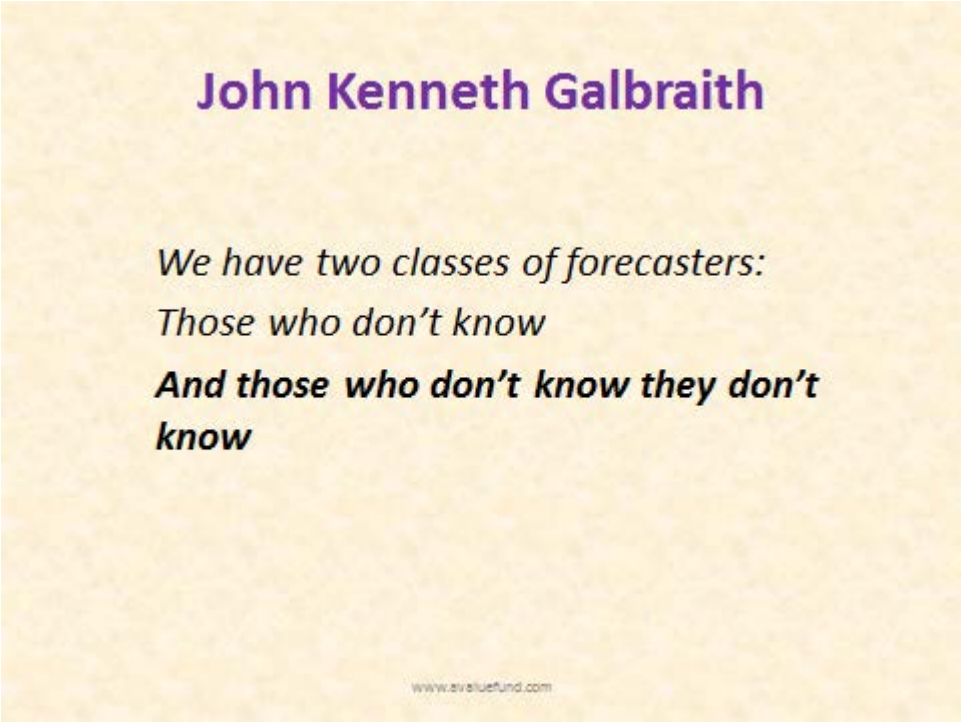
How would you have done if, over the last five years, you had been in a different currency? Over the last five years, the yen has actually strengthened against the dollar. In 2008, what would have bought 100 yen, would only get 91 yen today. So in spite of everything you've seen, the yen is actually stronger than it was five or six years ago. That's the Chinese currency down in pink and the Canadian dollar and the Euro up above.

Getting back to my premise in the beginning which was where you're investing from and what currency you're in, does matter. I chose a time period here where the TSX was somewhat flat. I've kind of cherry picked my times. You can see against it that if you were investing from US dollars, you're actually down. The TSX is flat. And if you're investing in yen, you're actually up 10%. So once again, what currency you're coming from made a big difference.

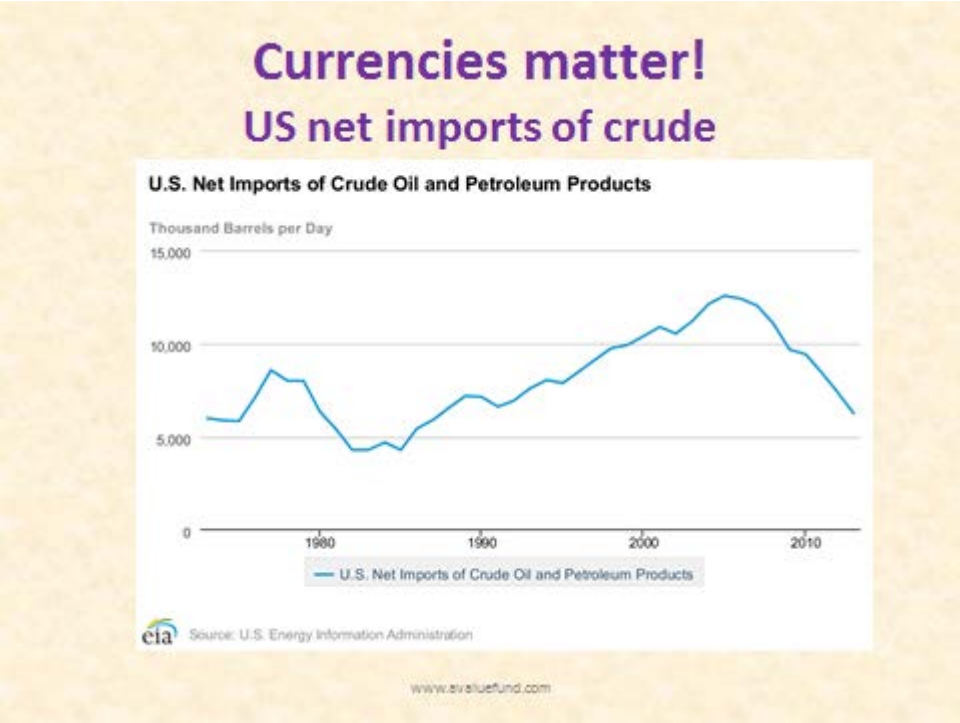
This is also quite interesting. This is from the very bottom in the Nikkei, or the Japanese stock market index. It was up about 75% to when I printed this chart. Now, if you had been investing in Euros, you would only be up about 27% during that period. So the change in the currency had a big impact on the returns. And of course, from the Canadian dollar, the return was about 40%.



Another example of currency matters is crude oil. You can see crude is up about 30% in yen, but actually down in Euros. So once again inflation, your idea of returns is all somewhat currency dependent. So your base currency matters and change in the price of currency matters.



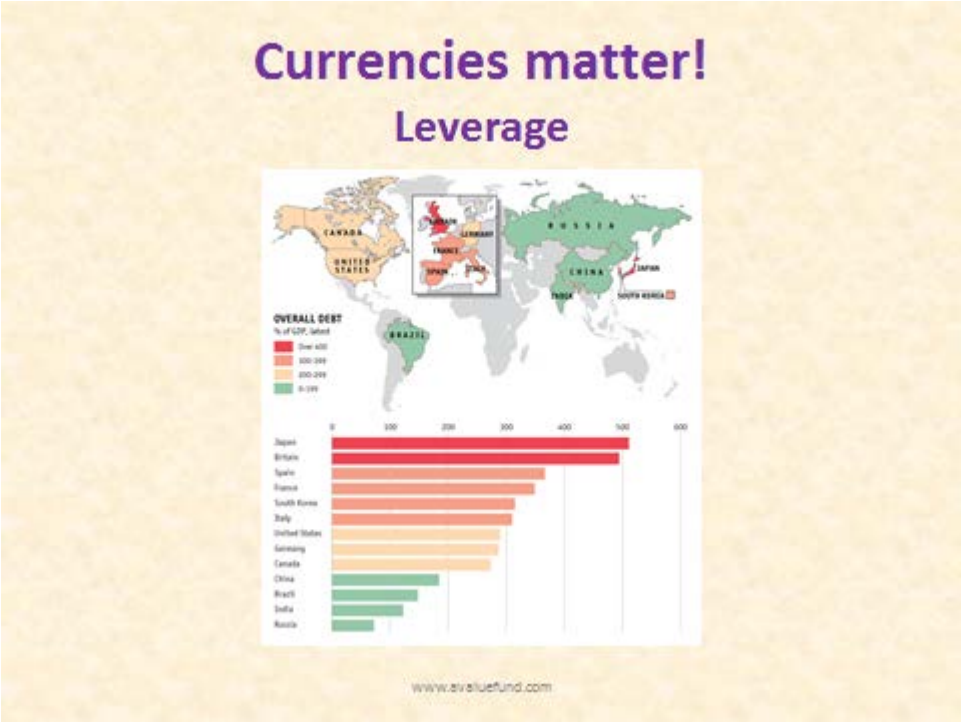
I'm going to make a couple of forecasting type comments. The first thing I wanted to do was use a John Kenneth Galbraith disclaimer. There are two kinds of forecasters: Those who don't know and those who don't know they don't know.



If you think about the US dollar, one of the impacts on it, of course, has been net imports of crude. You've all heard about the shale revolution and everything like that. I don't have any comments on how long it will last. I hear everything from 2017 to the early 2020s when the peak will be hit. Who knows? But the impact on the net imports of crude has been significant.

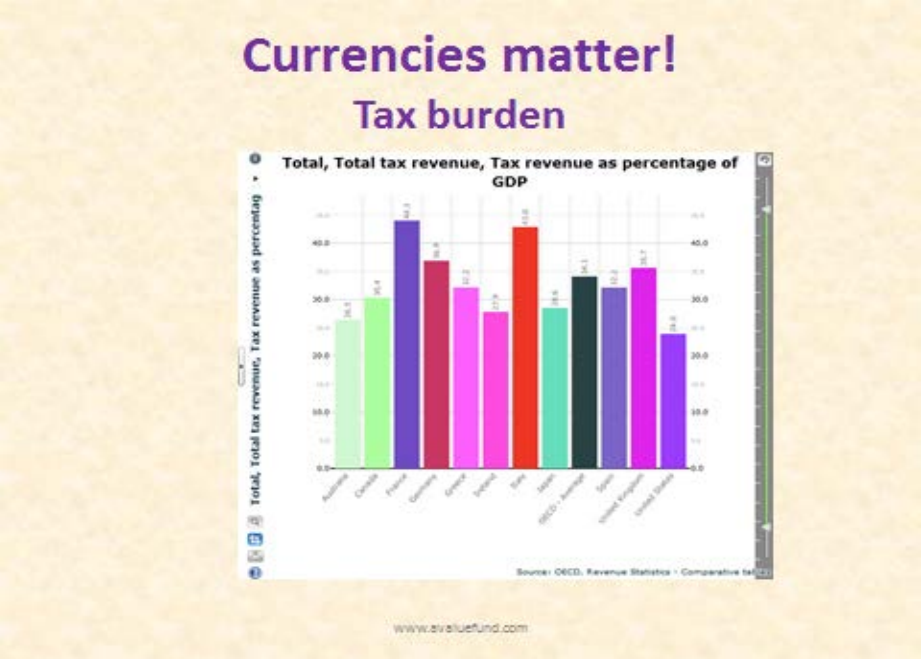
This, of course, follows all the way through to the current account, because if you're spending currency to buy crude and you have to buy less crude, it makes a big difference

to your current account deficit. This is somewhat recent data, and of course, it doesn't talk about whether or not exports will improve or not. But the bottom line is, fewer US dollars have had to go out of the US to buy crude oil.



The second thing is leverage. Now there have been a lot of comments about leverage in the system, and I have some slides on Australia versus Canada but I'm not going to include it in the bulk of the presentation. If someone wants to ask me about that at the end, we can pull them up. But the main thing I want to point out here is, the US, sure, has some leverage, but it's kind of like me in an old age home. I'm kind of relatively young, so to speak, but that doesn't mean a heck of a lot. The US is a little bit better as far as its balance sheet goes, but that doesn't mean it has a balance sheet that you'd ideally like.

While I'm on this topic, you'll see some of the worst balance sheets, ignoring Japan, are Europe related. Wherever you have debts, you also have to think about cash flow to pay for it? And how I gauge that is the tax burden or the capacity to tax.



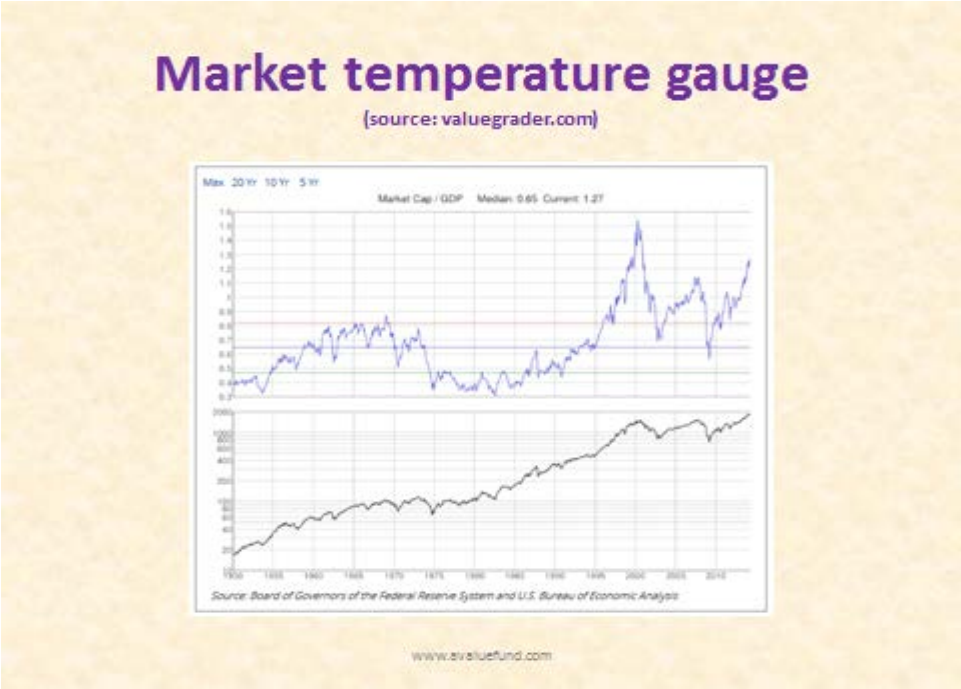
If you look here you'll see the US actually has a very low tax burden relative to everyone else. So its capacity to tax or—not saying it would be politically acceptable, but the ability to increase taxes is perhaps a lot more possible than if you're dealing with France, which is up towards the higher end.

Now without a doubt, society views impact this somewhat significantly, but that just gives you a little bit of a range. You have a current account that has come down a little bit. You have a relatively better balance sheet. You have more capacity to raise taxes if you had to. And then the economic outlook you might think is somewhat more positive.

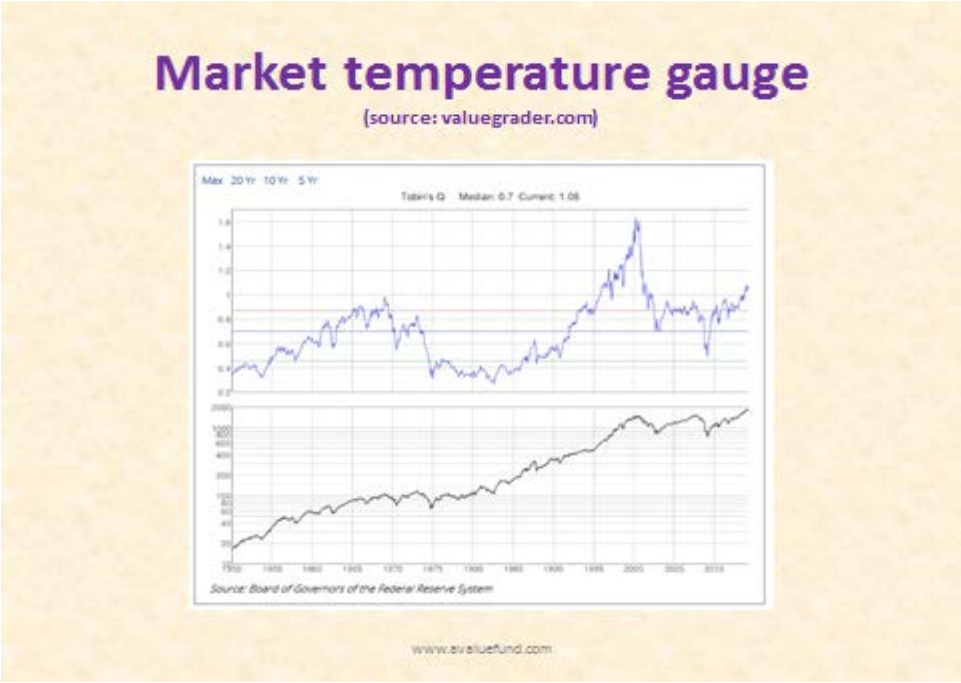
When you think about the US, instead of a declining currency like we saw before, it is now an appreciating currency. This will flow its way through into earnings and margins and everything like that.

It also brings up the question of the Euro. If there's ever a kind of a replay of Japan happening in slow motion, it's kind of what's going on in Europe a little bit. Europe has a very strong currency leading to deflation, very tight money and a banking system that has probably been recapitalized to the tune of about $60 billion. The US was recapitalized to the tune of almost $400 billion. And the European banks have three times the leverage of the US banks. Finally, they have a whole bunch of emerging market, especially corporate debt, which one might be a little bit sceptical about. And I think they've dealt with none of those problems.

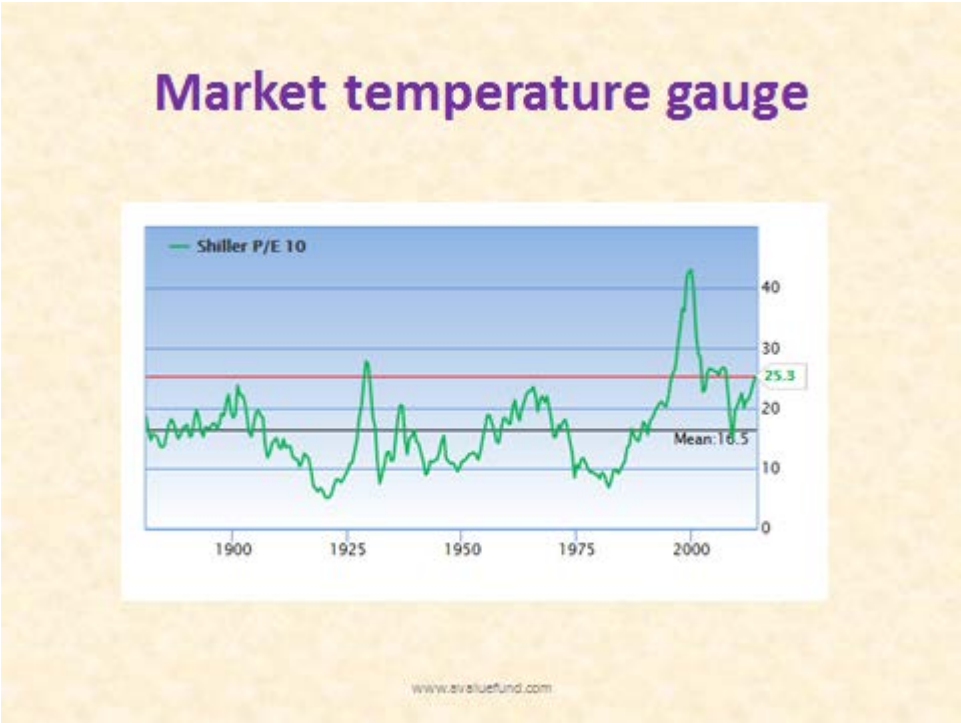
So if there's one area of the world that I think we're a long way from saying everything is going well, it would certainly be Europe. And it continues to be an area that I'm a little bit cautious about.



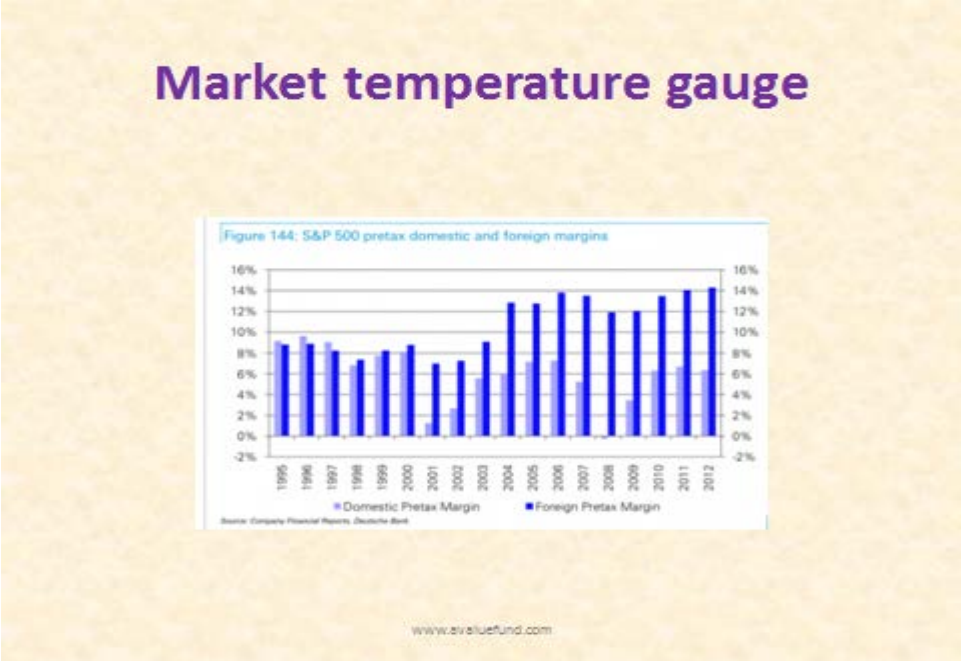
I thought I'd talk a little bit about market gauges. And the most important thing here is none of these charts have any predictive ability. It's kind of like when you take a temperature, you say, all right, is the temperature a little bit above normal? Does that say something about perhaps the level of risk? It doesn't say anything about whether or not the next 20% is up or down. It just says, what's the risk level like? This is market cap to GDP. I think Buffett said this is one of his favourite ways to look at the market. You can see in 2009 it didn't really give an overwhelming buy signal. So as I said, it's not really a good timing device, but it gives you an idea of temperature. Without a doubt, we're relatively high.



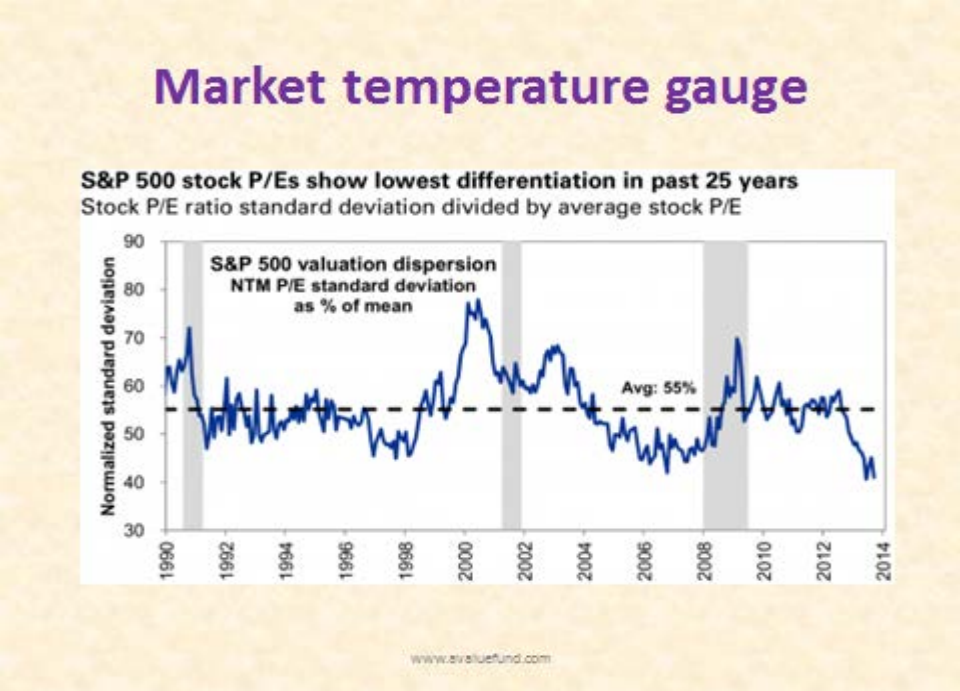
The Tobin's Q is a measurement of replacement cost. Basically when it's below one, it's cheaper to buy an asset in the stock market. When it's above one, it's cheaper to build an asset. You can see Tobin's Q is relatively high once again. The interesting thing is you would think this would cause a lot of companies to invest in physical infrastructure rather than look at M&A activity. But, of course, the opposite is actually happening at this time.



This is Shiller's P/E, which has recently received a whole bunch of talk in the marketplace. Once again it isn't much of a timing device, but just says, how are we valued relative to the past? So I would say that all three of these gauges say that your risk level is, let's say flashing orange.



The final thing I wanted to talk about here is getting back to where I started, which is the currencies. If you recall, the period of about 1991 to 2001 had an appreciating US dollar, and here you can see during that period, foreign profits as a percentage of US profits and their margins were relatively low. The last ten years, with the exception of last year, have had a depreciating US dollar, in which case we've seen an enormous expansion of the foreign pre-tax margin. So if our next ten years have a somewhat stronger US dollar, and with such a simplistic graph, you hate to make any predictions on it, but one would think that it would lead to some difficulty as far as margins in the US.



This is the graph that I find most interesting to me as a value investor. You know that old joke that you can drown in one foot of water if the range of depth is from 60 feet to 6 inches? It's the dispersion of the depth that matters. This is the same thing with the stock market. It says how much difference is there between the most expensive stocks and the cheapest stocks?

Now if we look back to 2000, and Antonie, you'll remember these days well, there was lots of stuff for us to do in spite of the technology stuff. You can see there was a fair amount of dispersion between the cheapest and the most expensive stock. Today, we're at the opposite, where the range is much, much tighter, at least in the US.

Market temperature gauge

(source: gurufocus.com)

Country	GDP ($Trillion)	Total Market/GDP Ratio (%)	Historical Min. (%)	Historical Max. (%)	Years of Data	Country ETF
USA	17.15	115.4	35	149	44	SPY
China	9.17	41	41	862	24	MCHI
Japan	6.31	111	56	366	30	EWJ
Germany	3.44	55	16	56	24	EWG
France	2.62	63	54	183	24	EWQ
Brazil	2.59	44	25	108	17	EWZ
UK	2.49	133	47	206	42	EWU
India	2.15	68	41	165	17	IGE.SG
Italy	2.11	15	9	45	14	EWI
Russia	2.08	30	22	142	14	ERUS
Canada	1.82	130	78	190	24	EWC
Australia	1.63	120	94	229	14	EWA
Spain	1.47	61	50	235	21	EWP
Korea	1.31	83	38	140	17	EWY
Mexico	1.17	38	12	46	23	EWW
Indonesia	1.01	47	19	108	17	EDIO
Netherlands	0.82	86	51	261.5	22	EWN
Switzerland	0.62	282	84	431	24	EWL
Sweden	0.56	123	63	159	13	EWD
Belgium	0.47	224	80	224	4	EWK
Singapore	0.29	137	92	418	27	EWS

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Looking around the world—I'll put this on our website later, so I don't expect you to take it all in right now, because there's a lot of numbers here. The most interesting thing is the cheapest areas are the same ones you would expect if you read the news. China, Brazil, Russia, maybe with a little bit of Italy tossed in there. The pendulum never stops in the middle and that of course—both means on the way up and on the way down.

Tim's Truisms

A pendulum never stops in the middle

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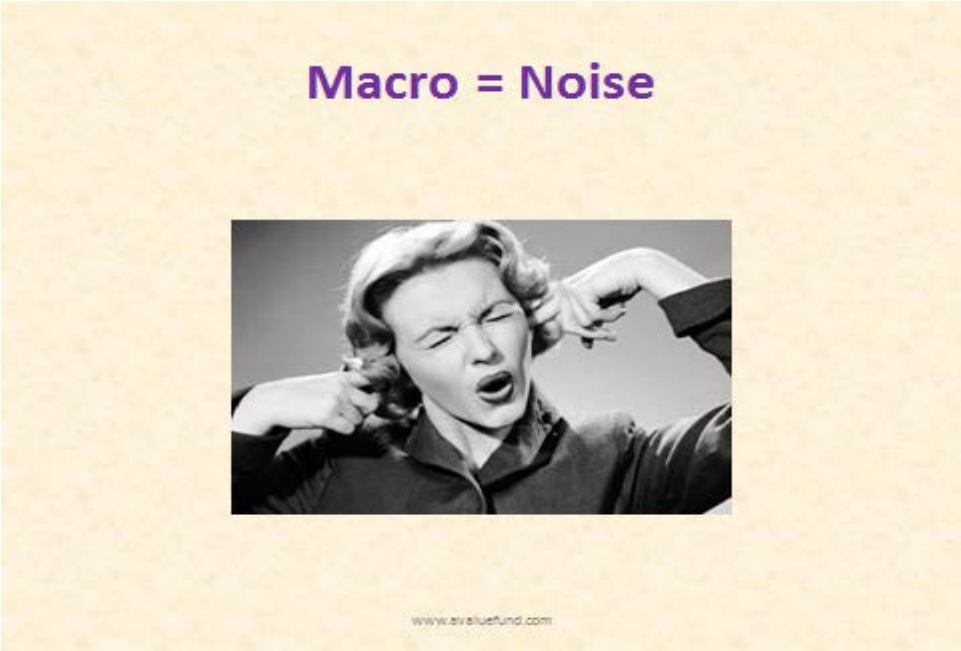


Every day that I come into the office I don't spend a whole bunch of time thinking about the macro stuff. My focus is very specific.

If there's some discussion on the radio or in the papers about this being the future, there are two alternatives:

One, you get of stuck, frozen in fear. I was talking with someone a little bit earlier about when you end up doing nothing, which isn't—from a value perspective, the way we would operate. That is dealing in the macro.

The second alternative is, how do we build our igloo in this area that may be stormy, may be sunny, or may be whatever?

First thing is, we try and have a competitive advantage in buying. That means when we actually look at a security, we're trying to buy something that other people don't want. And that gives us an advantage in the price we pay.

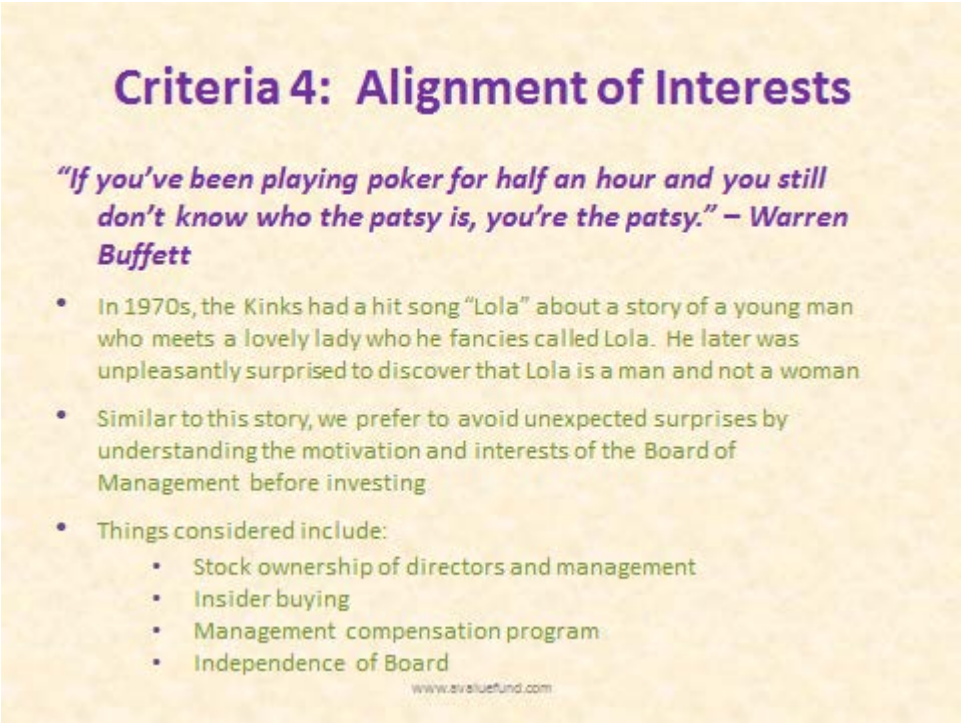
You've seen this slide before. Basically, the competitive advantage is in the pricing. So something that we bought just last week, which I'll talk about, was a dislocation, a spin-off. ING or Voya, which I talked about a little bit earlier, was a spin-off. So situations like that where there's a real dislocation is of interest to us.

Discipline determination of the pricing.

This is the value approach of margin of safety that Peter Cundill and Ben Graham talked about.

Minimize financial risk, which is this concept of a brick house that I use the analogy of the three little pigs. You know the straw hut or the stick hut and the brick hut.

Finally, alignment of interest and this is an interesting one. There have been a whole bunch of studies done about how much management ownership is the right amount. I don't know, but if you have—especially a board or a CEO who owns a lot of stock, it takes a lot of the difficult conversations off the table because they're thinking about the same things as you are.



As you know, from time to time I go on boards, and that's one of the things I think you can really influence as a board member, is trying to line up the alignment of interest. If you get that right, a lot of other things become less difficult to do.

I'll talk about this a little bit. If you want rules of thumb - if they have say, five times their salary in stock ownership, that's somewhat interesting. If it's a small cap company, ideally you don't want them to own 25% or more, because that'll restrict some of the alternatives and pressures in the future. Equity ownership is better than options, and there's a whole little checklist that I go through.

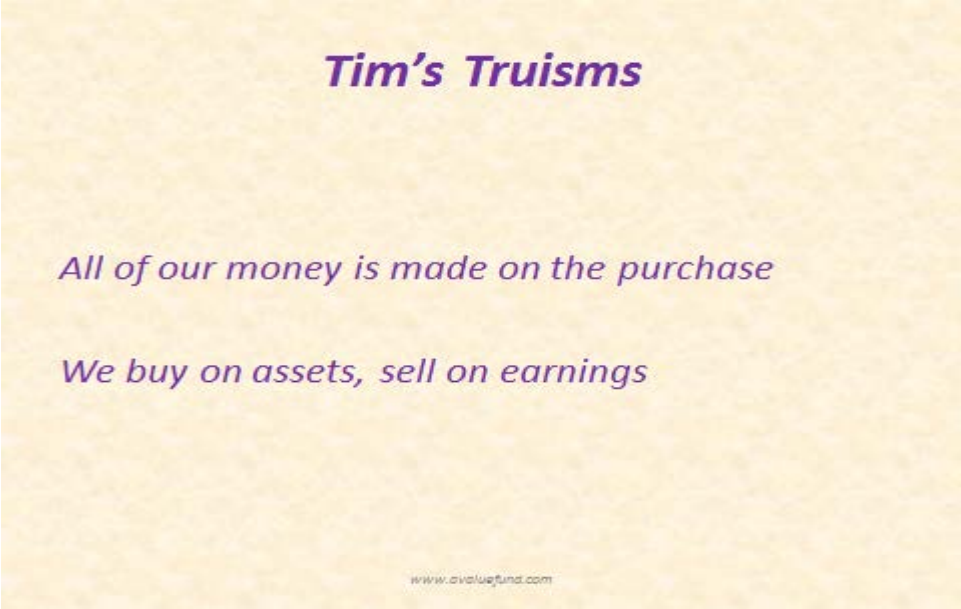
The final thing we've done, which is kind of the fifth leg to the chair, so to speak—I'm a value guy, so my chair has five legs—is I set up an advisory board of three guys. All are quite successful investors and have been members of many, many boards, including chairperson. They don't act as an investment committee, but rather what they do is look at risk control and ask me questions. "Have you thought about this? Have you thought about that?" This is very similar to how Peter operated in the early days when I was with him. You might recall, Bill and Brian, when he had the board of directors of Cundill Value Fund. The board didn't have any investment role, but they did act as a little bit of an overseer. They kept Pete's feet to the fire a little bit. That's the role of this advisory committee. I meet them about once a quarter, give or take.

I have just reframed this ABBA thing as; competitive advantage in buying, disciplined determination of pricing, financial risk minimization, focus on alignment of interests, and then the advisory board oversight.

This leads back to the concept of our igloo. We'll keep the bear at bay and try to build our igloo in a somewhat uncertain environment.

Let's get to maybe what's more important, which is what are you up to? Here are our top ten holdings.

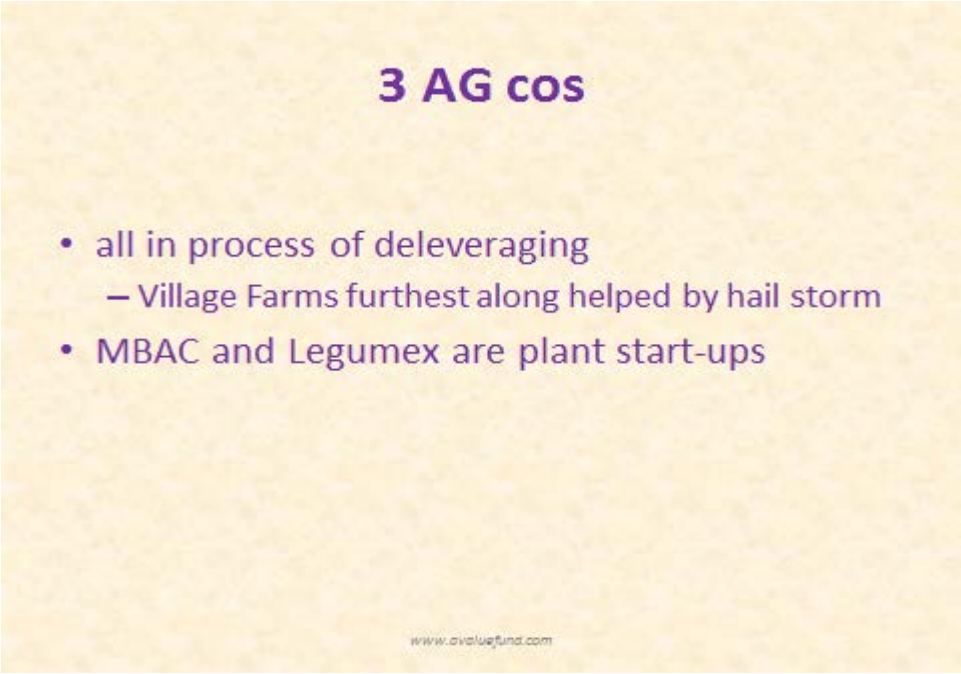
We currently have about 15 or 16 real holdings in the trust. We have about another four, but they're things like Deans Knight, which really have no market value and no cost. They just kind of sit there. So in total we have about 20 holdings, but maybe 15 matter and the top 10 represent almost two thirds of the portfolio. This is them. I can talk to any of the specific ones, but I wanted to go through a couple of them. Cash is in the centre because it's always our default. We'll stay in cash unless we find something to do and today it's about 25% of assets.



So getting back to what I talked about a little bit before with the concept of disciplined pricing, it's like a real estate guy said to me many years ago. He said, "You know, all my money is made on the purchase. That's the only thing I can control, is when I buy the real estate. I don't know what's going to happen after that." And that's the same thing on the investment side. We kind of buy on the asset side primarily, and then when earnings eventually come through and people start putting a P/E on it or whatever, that's where we tend to sell.

I wanted to start off with a couple of areas, and all of these are positions that we own. Kate, please hand out the tomatoes. I brought you a present today. I've been told you don't need to wash them, so you can eat them as is. This is a product of Village Farms, the Marzano tomato, which I really like. They're not the cheapest tomatoes, but they're pretty good little guys. We don't get them over in Victoria, so I have to go by Village Farms whenever I'm over here.

I want to talk quickly about three Ag companies. Now as I was joking with Hugh at the beginning, an agricultural company is like this Buffett joke about a race horse. A guy said to him, "How do I sell my race horse that sometimes limps?" The guy answered, "When it doesn't limp, sell it."



That's basically how you can summarize something in the agricultural business. All three of these companies are in various processes of de-leveraging. Village Farms had kind of an Act of God help them in that a hailstorm hit their business and damaged two of their greenhouses, which generated about $50 million--$47 million in insurance proceeds. So if you're not farming, you may as well have something else that helps. But nevertheless, I'll talk about Village Farms for a second.

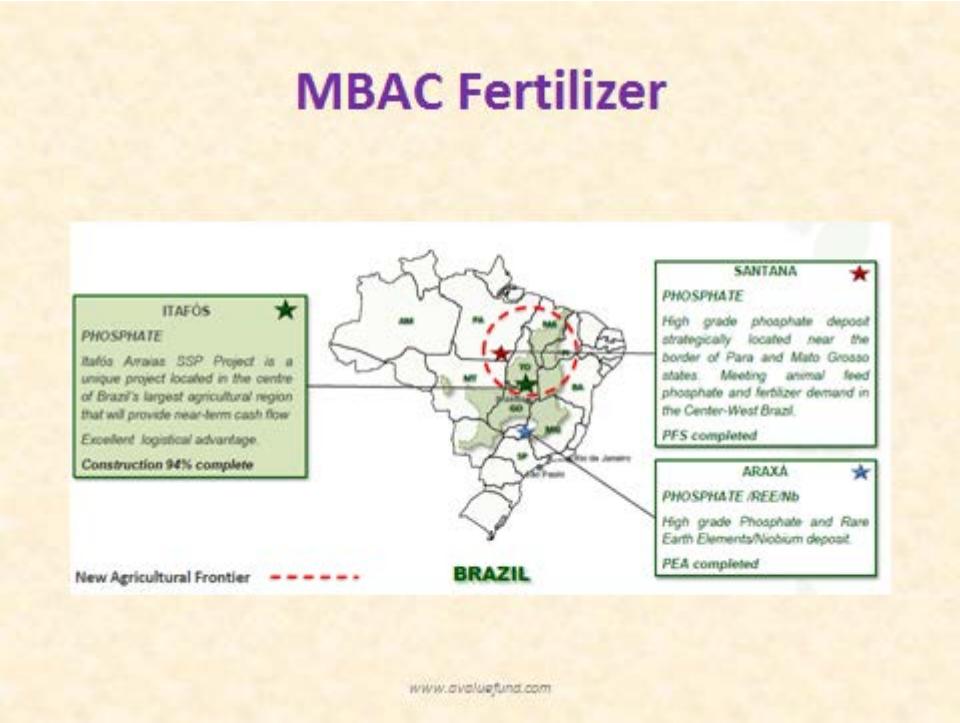
It's the furthest along out of all three of these agricultural companies, and it's the one that's probably closest to a sale from our point of view. So take this all with a grain of salt. It's had a pretty checkered history.

This is a picture of the greenhouse. They have about 240 acres of greenhouses, which to visualize, I think the CFO told us it was like, 80 football fields. They have about 110 acres out in Delta, just as you're going along 99 by that airport, Boundary Bay. If you look to your right as you're driving out there, you'll see their greenhouses.

This Marzano Tomato is one of the products they grow there. The stock trades about book value, maybe a little bit above book value. Replacement cost would be significantly higher than that. Because they had this difficulty in their US greenhouses, they own about 110 acres or 120 acres of greenhouses in Texas, they managed to pull down their debt significantly. It's about $35 million, give or take a little bit now. They generated about $160 million of sales of these tomatoes and they'll free cash flow before expansionary cap-ex, somewhere in the low teens I would suspect.

Here is a picture of it, and there are some characters of somewhat suspicious origin in there as well, as the two Hughs know. Note I did not include the picture of myself, so there's some advantage to being the host, so to speak.

So that's Village Farms. Cheap on a price to replacement point of view. Very free cash flow generative right now. Balance sheet in much better shape. Management owns about a third of the company. And it's been, certainly for the last couple of years, it's been a good story as far as performance of the trust goes.



At the other end of the spectrum is MBAC Fertilizer. What they produce—and I'm not going to spend a lot of time on this one, it's the most risky of the three. It trades about $0.55, give or take a little bit. It has a book value of about a buck. They just finished constructing a phosphate facility in the middle of Brazil. The key things are, and this will be like the last idea as well, it was a plant start-up. Quite often when you find plant start-ups, people are very enthusiastic in the beginning. They get very excited about the idea of a plant, and then they actually start constructing the thing and investors go, "Oh, well, that's not so much fun." There's no earnings and there's a whole bunch of cash going out, and that process lasts about two years.

Then of course, there are problems in getting the plant started and people get a little bit annoyed. About a year and a half or a year after they finish constructing, they finally get a plant up and running and everyone begins to get excited again. With MBAC, we're right in that middle stage. They finished the plant in December. The key issues are, does the plant work? And the answer is yes. Is there a market for the product? The answer is yes. Do they have the financial capacity to keep the wheels on the bus until they get the production up to say 80 or 90% of capacity? They just completed a rights—or an offering about two weeks ago. So I think they do. It's a little bit tighter than they originally thought, for sure.

This is an asset that's capitalized at about maybe $100 million in the marketplace, which has the ability to generate north of $50 million a year in free cash flow, and has a 20 year plus mine life, as well as a number of other facilities. So it's interesting. It's a growing area in Brazil, the supply of phosphate fertilizer. It's a unique asset with some protection because of its location. The board is somewhat shareholder friendly. It is a very cash generative, long life project. But as I said, there is some risk with this one because it's the most levered of them all.

The last Ag company I want to talk about is Legumex Walker. Similar to the other three, they came out and announced they were building a facility. Everyone got really excited. The stock, I don't know, was somewhere in the teens. They actually got around to constructing the thing and the stock fell as low as, say $3 bucks or so. We acquired some of our position, and now it's about $4. So it's up a little bit. I'll talk a little bit about their businesses and the facility in particular. They have two main lines of business, specialty crops and canola products.

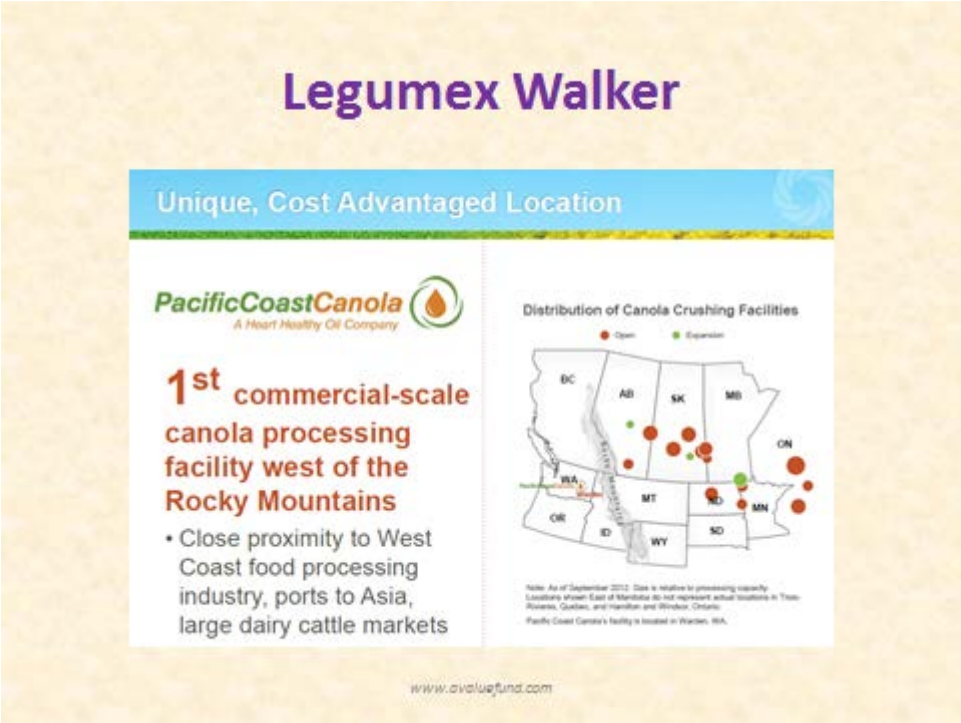
Specialty crops do about $300 million a year in sales. Produces about $27 million of gross margin, and then has SG&A. It's roughly split between all three of these. It varies year by year because it's Ag, right. Some year peas are going to be doing better than kidney beans, etcetera. But you could say about a third of their contribution comes from each of those assets. Although one part of the business, peas, takes a whole bunch more work to get that—you need a lot more volume. But that's nevertheless what they do.

They sell primarily to the Americas, meaning everything from South America up. And if you look to the right, that's basically their breakout.

By the way, I'll say one of their highest margin businesses, and I think of this now every time I think about buying some, is actually bird seed. You can make more money selling bird seed than you can to sell a bunch of chick peas to human consumers. So I don't know what that says about us. But nevertheless, feed the birds, so to speak.

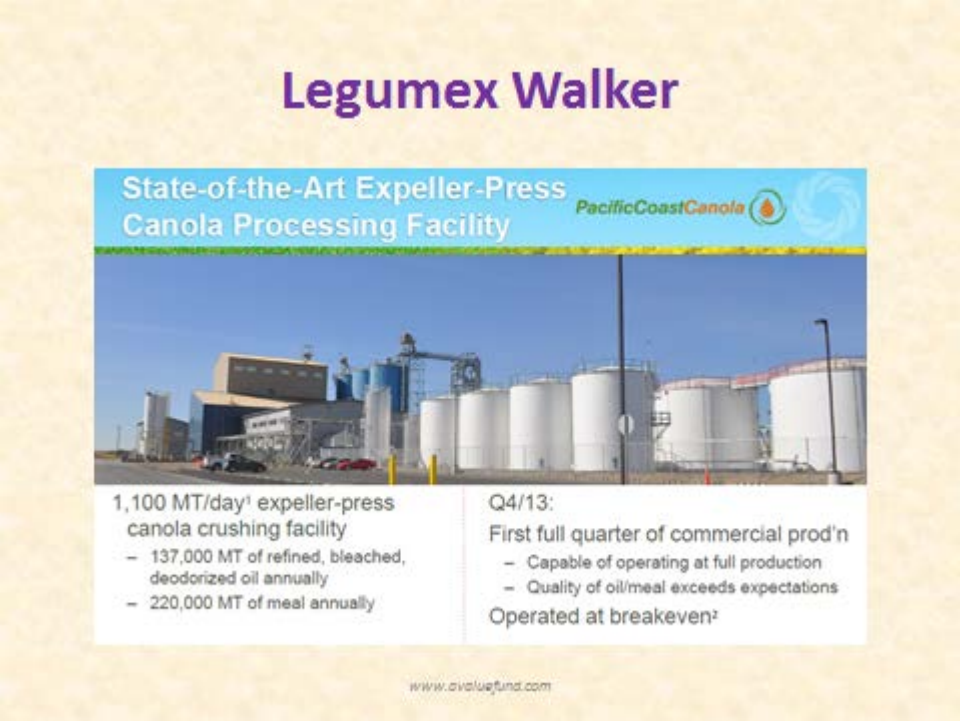
The other business that they have is, and this is what caused them both the excitement and the pain, is they decided to construct a facility to produce canola oil in Washington State. It's in a place called Warden, which I've visited. It's about three hours from Seattle.

You know, you've heard everything about canola oil, Frito-Lay and McDonalds are going to use canola oil and some states banning trans-fat.

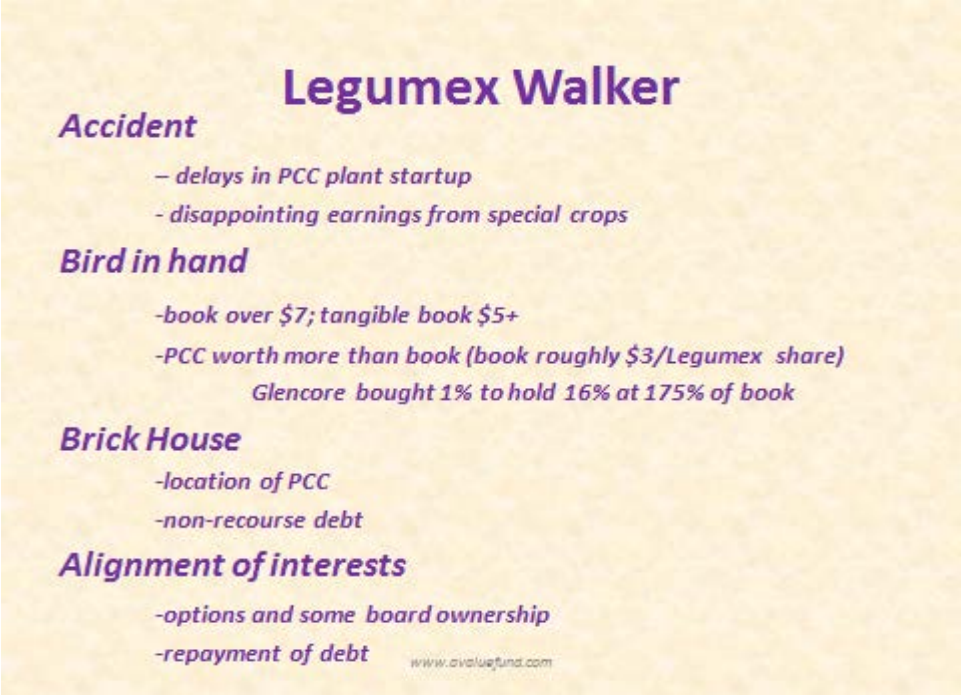


The interesting thing about these guys is the facility that they constructed in Warden uses what they call an expeller press. The bottom line is it means there are no chemicals added in the production of canola oil. It's one of only two facilities in North America that can do that. So they produce a kind of non-chemical, healthy canola oil, and they also produce a non-GMO canola oil and meal as well. You can see their location. If you looked at it from a competitor point of view, everyone else is on the other side of the Rockies. So they're good as far as being—proximity to the end customer, meaning primarily California. They also have a little bit of protection over supply. The amount of canola that they've been able to source locally is about 50% and they're hoping to move that up to about 100% over the next little while.

One of the main sources of difficulty to them in their plant start-up, has been getting seed. As you've all seen or you've all read, everyone seems to be shipping their oil by rail these days, which has caused some real difficulty for people like Legumex Walker, to get seed into Warden and then also to get oil out. That's one of those things that doesn't really matter two years from now. But right now if you listen to a Legumex conference call, all the analysts are all over, "How much extra will it cost you to truck," and this and that. That's clearly where I think we as investors have a real competitive advantage, because that doesn't matter at the end of the day. What matters is what I said before: a/ does the facility work? b/ Do they have customers that they want what they produce? c/ Will they be able to get up to 90% plus capacity? d/ And do they have the financial standing to be able to get through this so it doesn't get too dilutive to the equity owners?



Here's a picture of the facility. If you wanted some numbers, it does about 370,000 metric tons of canola oil, which is a heck of a lot of canola oil. A lesser amount of meal. They also have this concept called a "crush margin," which is basically how much money you make when you process. The standard crush margin is about $100. These guys, because they do expeller press, because they do non-GMO, should be able to get a premium to that, and they just started in December in their production.

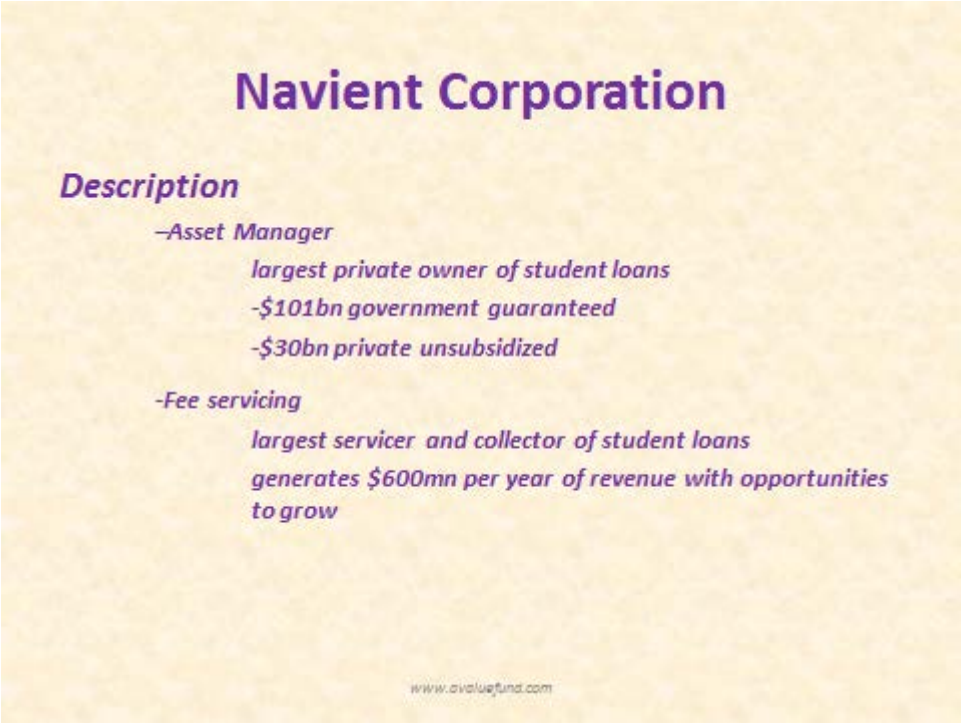


This summarizes Legumex in our format. The accident was delays in the plant start-up, disappointing earnings from specialty crops. So people weren't too interested. Our margin of safety, book is over $7, tangible book is, $5+. Glencore owns about 16% of the Warden facility, and they bought 1% just a couple of months ago at about twice book. So basically the valuation of Legumex Walker is covered by the canola business, with the specialty crops business free. There is some leverage in this one, so you have to be a little bit careful.

At the end of the day—once again, when you look at what's happening in the stock market, does that impact MBAC? Does it impact Village Farms? Does it impact Legumex Walker? No. These guys have their own drivers as far as what's going to create movement in the stock price over the next couple of years, and that's kind of what we focus on, in spite of my spending ten minutes talking about the macro view.

Two other ideas and I'll move through them quickly. As I said to you before, we do spin-offs. Why this is interesting is you get a certain amount of dislocation, which is, analysts aren't really providing coverage. A shareholder ends up with two share certificates. What that spin-off is, by the way, is one company decides to split into two pieces. So if you owned a share of a company, you suddenly own two shares of two different companies. People quite often don't know what to do with them, index funds, it can confuse them.

That's an area that has become relatively expensive lately, but it's an area we keep an eye on. A spin out that just occurred about a week and a half ago was something called Navient, which is part of the old Sallie Mae.



Navient, which has about $7 billion market cap, so it's not a small little company here, is basically an asset manager who manages about $100 billion worth of government guaranteed student debt. This business is in somewhat of a decline, but it generates probably pre-tax about $600 million a year. But that's in decline. They're by far the biggest and the lowest cost servicer of this business. So they'll be able to acquire additional student loans. But that business, the first part of the business is in decline.

Private unsubsidized education business produces about $500 million a year in pre-tax cash flows to Navient. They should be able to keep that balance relatively stable over the next little while.

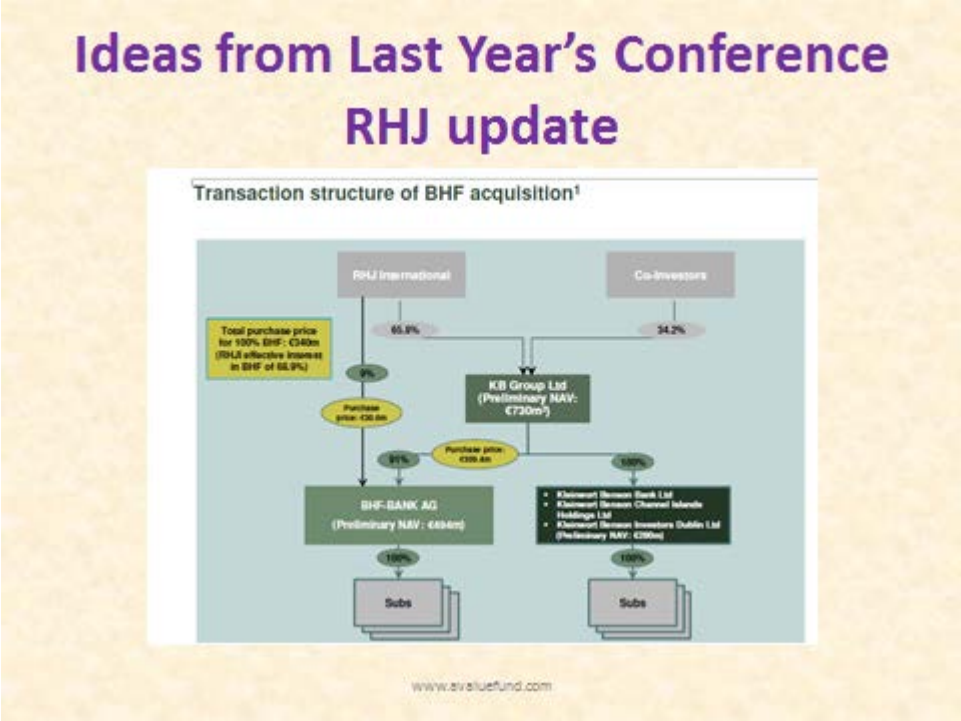
Their third business is fee servicing, which basically means they're the servicer, the collector of student loans, and they generate $600 million a year of revenue and about $350 million of pre-tax.

So a real business. They have well over $1 billion plus in cash flow. Cap-ex needs are very modest. Free cash flow is very, very significant. So put into my format, the accident was the dislocation. Book is about eight, somewhat higher because they're over-reserved on some of their loan. EPS is say $2 plus. Free cash flow is significantly more than that, allowing them to do dividends, stock repurchases, all that type of stuff. A lot of the debt's non-recourse.

But the most interesting thing is you had a CEO who, when they split Sallie Mae into two, decided to go to Navient. He has about a million shares, so $16 million in shares and he probably has another three million shares, in the money options. So this guy has, let's say $60 million, give or take a little bit tied up in Navient.

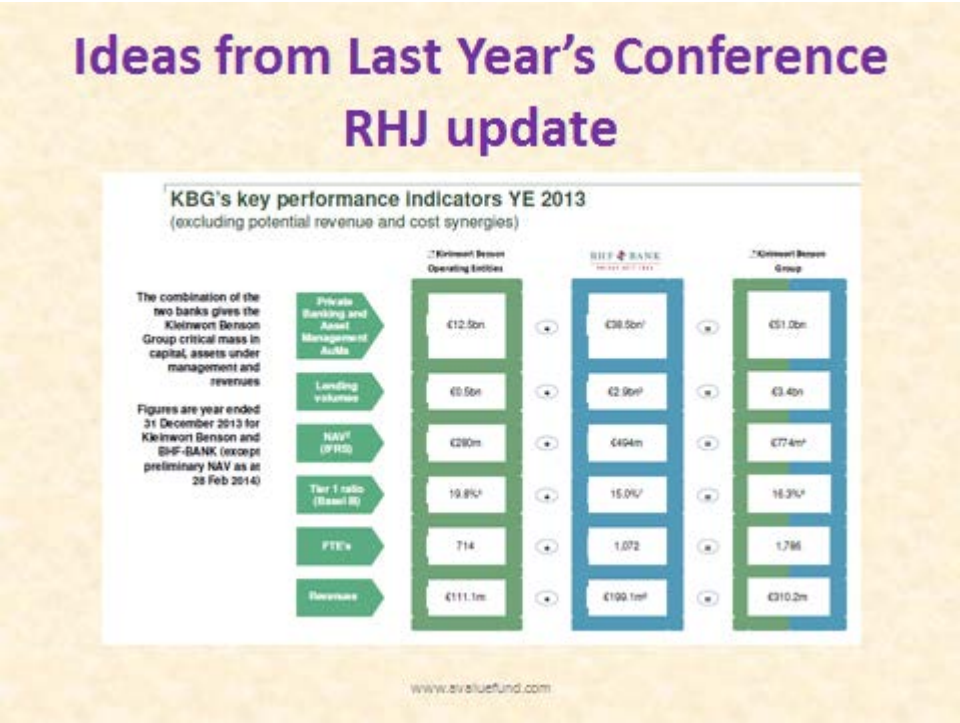
The analysts' view of it right now is, we don't really know what their game plan is going forward. So let's wait and see if they could actually grow this business or not grow this business, or is it just a cash flow stream? That is the type of situation we look for.

The last one, and you've heard me talk about it in the past, is RHJ.



We acquired most of our stock at about five Euros. They executed on their disposition plan, which was basically to go from a Japanese centric industrial holding company, to a financial services business based on a private bank, Kleinwort Benson. They then attempted to buy BHF, which was a private bank owned by Deutsche Bank, and they got stuck in regulatory approvals in the EU, which has been a very painful process. They finally come out of that.

RHJ closed their BHF acquisition just a couple of weeks ago. Next week they're going to come out with their targets and everything like that. So this is somewhat off the cuff numbers by me, but I just wanted to briefly touch on it because we talked about it in the past. It's a very confusing diagram, but the bottom line is they've got three investors, Tim Collins, who was the principle owner of RHJ. Fosun, who is a Hong Kong based holding company. And Stefan Quandt, whose family owns BMW. They all put in some money. RHJ tossed in Kleinwort Benson and put in some money, and they bought BHF to form the Kleinwort Benson Group, which will then operate this private bank.



This is the more interesting thing. Under Kleinwort Benson, which you can see over on the far left, the asset management under AUM goes from $12 billion to $51 billion. That is a huge increase. Tier one capital, which is the amount of leverage the bank has, still remains relatively low. And then you can see the revenue.

When you think about the private banking things, it's really two things. It's an asset management business, and it's a private bank. From my point of view, private banks, if you can get more than book, that's great. Asset management business, that's kind of the gravy of the operation. That's what's been basically created by the merger between the two. It's very much dependent on execution going forward.

Ideas from Last Year's Conference
RHJ update

- Tim's valuation:

– 65.8% KB Group @ implied valn	338	
– 9% BHF @ cost of 5.5m shrs given up	20	
– Quirin @ market	16	
Total Financial Services	374	4.11/shr
Investments and loans at market	18	0.19/shr
Cash and liquid assets	66	0.73/shr
Total	458	5.03/shr

My valuation, this is really back of the envelope. I revalued the whole group to basically what they paid. That's how you get this four Euros a share for the total financial services business. I think the businesses could easily be worth more—say twice book or more. This valuation is 70% of book.

Adding in the cash and everything else, the result is you come up with 5 Euros and change a share. The stock trades for about three fifty. I'm tossing a whole bunch of numbers at you, but basically with Kleinwort Benson valued at 70% of book and you get five Euros, and we're trading at about 70% of that today. So 70% times 70%, we're trading about $0.50 on the dollar, so to speak, because of the double discount. Plus I think that valuation can grow over time, but it's very much execution related. So a cheap stock, a good balance sheet, revitalized management and we'll see where it goes. But it's been a long wait.

I've talked for about 45 minutes so I'll wind up. I talked a little bit about some of the challenges outside in the economic environment. I coined this thing, "our igloo," which as I said was, competitive advantage in buying, disciplined pricing, minimized financial risk, focus on alignment of interests, advisory board, kind of the risk control. The portfolio that you own in the The McElvaine Investment Trust is nothing like the index. Our position sizing has been disciplined. Our top five or top ten positions aren't particularly expensive, because when things tend to go up, we tend to take money off the table relatively quickly.

I think our top positions are inexpensive and Kate and I have all of our money in our stuff. Our cash balance today is about 25% of assets, and we have as modest put position as a hedge on the NASDAQ. So that's where we stand today.

Before I turn it over to questions, I just want to say, it was a different format this year. I appreciate, as I said in the very beginning, all the support that I've received over the last couple of years. And thanks very much for coming again here today. Thank you.

Q&A:

Bob?

Bob: You mentioned MBAC as one of your holdings. Obviously it's an out of favour space, the big cap and junior mining. Do you find other stocks in that area? That probably is one of the most out of favour areas in the world right now.

Tim: Yeah, I've been a little bit cautious about doing some of the other miners. I was interested in MBAC primarily because they have a competitive advantage because of their location. Their market is large and growing, and they're protected somewhat. So it's not like they're producing—they are producing a commodity type product, but there are some pricing advantages they have in where they're located. I've looked at a couple of the others. I really hate mining, that's kind of where I'm starting from. So maybe we'll do some more, but I'll try not to. Does that answer your question?

Yes Sanjeev?

Sanjeev: So you're recently appointed to the board of Glacier Media. Any comments, ideas, anything you want to add to that?

Tim: Well, it's interesting. As Sanjeev says, I was recently—joined the board of Glacier, which has been a long time holding of ours and has not been a stellar performer during that period. And you kind of go from there.

I really just joined, so I don't have a lot of comments. The people are very good. The business is very cash generative, and we'll see.

Jeff?

Jeff: Tim, a few years ago you made a great buy of CBS, which did very well. I look at how I watch TV these days, it's kind of changed a bit. And I wonder if you still study that industry and have any thoughts on the broadcast television?

Tim: You're always more insightful than I am, so I'm sure you have better comments than I do. We no longer own CBS, sadly, because it's actually done quite well over the last couple of years. I think the Internet is one of those things that there's a lot of hype to it, but there's a lot of danger to it too, as far as some of these basic businesses go. Something quite as simple as banking—I was looking at something the other day that was trying to match people who wanted loans with depositors on an aggregating basis. It was basically just intermediary'ing the whole banking system.

I have no idea if that works or not, but that's some of the type of the dislocation that's going on. As far as CBS, I'm sure any one of those guys would trade their position today for black and white TV with three stations. But that's just not what's happening. My daughters, I have one who's now gainfully employed and has graduated from university, she doesn't even have TV. She doesn't need it. And that's one of the realities that the broadcasters are facing today.

So something like Netflix I watch with a lot of interest to see how they can stick handle the changes that are going on. So I don't know if that answers your question, but it's interesting times.

Larry?

Larry: I wondered if you'd talk a little bit as you go from universe of stocks that exist to a portfolio of 20?

Tim: Yeah, it's—we've had people comment in the past on, how do you look at the whole world? Well, the thing is, I don't look at the world, right. You're looking for problems, dislocations. There may be what, I don't know, 30,000 securities in the universe. But if you're just looking for a specific thing, your subset's got an awful lot smaller. And my predisposition is to invest in companies where I can actually read the annual report. So that narrows it down a little bit further once again. And then you'd say, I like to be able to trust the annual report, which narrows it down perhaps a little bit more again.

So New Low lists, spin-offs, they're probably the two main areas. If I were to look outside of North America right now, areas like Brazil, for example, we don't own anything there other than MBAC. I would say to myself, there are some real companies there. What's the pricing like? Can I get an idea on whether or not the management, there's an alignment of interests? And that's probably the biggest thing that I try and get my mind around when I go outside of North America. Does that kind of answer it?

Larry: Yeah, I always find when I look at your portfolios, I wonder how you got there. I mean, I know that they're cheap stocks [inaudible] a dozen people and you find a dozen lists of cheap stocks.

Tim: Have you ever heard the Rascal Flats, this twisted road that brought back to you or something like that? That's kind of how you put together a value portfolio. Any value investor will have a—Sanjeev's portfolio I'm sure is much different than mine, as well as the stuff that Jeff does is much different than mine. Part of it is have I seen something similar before? For example, Voya reminded me very much of a spin-off we did in Australia maybe five years ago. So there's a fair amount of bias that comes in Larry, that's I guess what I'm saying.

Larry: I want to thank you too, for your candour and increasing ability to talk about what you do [inaudible] wonderful.

Tim: Yeah, that wasn't a plug, but that's good—thanks. You know, I'm appreciative of—you've been with me a long time, since we had lunch in Victoria many years ago, as with a number of people here, and I appreciate very much all the support I've got from you guys. So I really feel good about what we have in place today, and I'll always try and tell you exactly what's going on, whether or not it's good or bad.

Hugh?

Hugh: Somebody's got to ask, what about Rainmaker?

Tim: Well, Rainmaker is either on the cusp of darkness or the cusp of greatness. The difficulty is deciding which way it's going to go. We have a great management team. Craig talked about it last year. The biggest issue with Rainmaker in its past, as Jamie knows, was they decided to get into what was a terrible business. This predates me. And then they actually didn't have any salespeople to make sure you got revenue. Those two aren't good combinations.

We're still in the lousy business that we were before, but we actually have a very strong ability to generate business now that the potential—backlog is not the right word, but the amount of volume that we could get through is the best that it's ever been as far as the time I've been on the board. So from that point of view, everything's very optimistic.

It's a tough business. In Hollywood, a contract is more an item of some oddity than actually a binding contract. So litigation is kind of part of what you do in business. It's a totally different world down there. I think we have a good team with Craig, Michael, Kim and Bryant. I think they're operating in a tough environment. The production slate that we have is amazing relative to anything that Rainmaker's done.

But you have to get it manufactured and you have to get it distributed. And they're the two humps that we wait and see. So I don't know, I am cautiously optimistic, but—it's been a long one.

Hugh: [Inaudible] what about—I think [inaudible] a really good move [inaudible]. What do you think the company's going to do with all that cash [inaudible]?

Tim: Yeah, I don't know. Torstar, as I said in the Globe last week, was a little bit like the 16-year-old who kind of fleeted from one fashion to another, and those of you who have 16-year-old girls know exactly what I'm talking about. So now Torstar has happily entered the middle ages, at least as far as age goes. Hopefully not as far as corporate governance goes, but we'll see. There was an article today which was a summary of the speech that was made yesterday, that I would say I read with a little bit of caution.

Ideally, to my mind, Toronto Star should be put together with the Globe and Mail. National Post should be driven out of business, and Torstar should not make another acquisition with their money. They should return it to shareholders and just look at an exit. Will that happen? Very unlikely.

But the stock at $7, or give or take a little bit, we bought a position somewhat lower than that earlier this year. It's cheap and the dividend yield is very high. The balance sheet is much improved. They have a wonderful asset in their Toronto community paper business, called Metroland, less so in their daily. And for those who didn't know, they sold Harlequin for a big price.

So cautiously optimistic. Cheap stock. If you said what do I expect them to do? Probably pay a buck in special dividend in the fall and make an acquisition. That would be my guess. Is that ideally what I'd like? No.

Dave?

Dave: [inaudible] BlackBerry?

Tim: Yeah, we still have—we haven't bought any. We haven't sold any. It's trading more than our cost. So from that point of view is good. It's not one of our larger positions, so that's why it didn't show up there. But I've heard the new CEO, Mr. Chen speak. The balance sheet is not ideal, but gives them some time to execute. They really have four things: the handset business, which really shouldn't view as anything more than noise; the enterprise business; BBM, which I don't know if they'll ever be able to monetize, and; QNX, which is basically a dominant software system in automobiles. QNX isn't very large relative to everything else at BlackBerry.

So we'll see. The positive is they have what seems to be a very competent guy running it, and they have some time to execute. The negative is, it's a tough position to be in.

Dave: [Inaudible].

Tim: No, the main negative is, what happens with this whole patent discussion that's going on down in the US. Part of our premise was cash, plus patent value, plus some real estate, which they just sold, was worth well more than the stock price. As long as everything else wasn't a huge negative, it didn't matter. And I'd say that's still the case today, but we'll see. I have a BlackBerry and I miss my iPhone.

Dave: [Inaudible].

Tim: Yeah, I saw another question over here, was it—or was someone just stretching?

Audience: I was just going to ask about BlackBerry.

Tim: Oh, yeah, you guys—you know how to hurt a guy don't you?

Yeah, John?

John: Can you just give us a sense of [inaudible] position size [inaudible].

Tim: We started off with position sizes between, say probably 3 and 10%. Then in the middle 2000s, when there wasn't very much to do, we got a couple of position sizes well into the teens. That was very, very painful. So like a cat doesn't jump on a hot stove twice, I am going to be careful. But I'll never have small position sizes. The ideal position size would be 5%-10%. We'll go at the higher end sometimes or we'll go somewhat lower, depending on the situation. Especially if time's gone on, it's more likely to be a larger position. That doesn't mean the stock price has done well, of course. I've just spent more time around the company.

For example, Glacier is a larger position. Part of that is because I think it's cheap, and part of that is I have a high familiarity and comfort level with what I see there. Something like Navient, even though a much bigger company, is a relatively smaller position, about 3% of assets. Relatively new and we'll watch it. Voya is about a 5% position. So it goes the full range.

Let's stop there as I don't want to hold anyone hostage. So I'm of course around here if you'd like to chat. But mostly I appreciate very much everyone coming out today, and I look forward to seeing you next year.

Thank you very much.

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