Exclusive Transcript

(lightly edited, may contain errors)

Guest: Amit Wadhwaney, Third Avenue International Value Fund

Host: Oliver Mihaljevic, oliver@valueconferences.com

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Q: It's a pleasure to have with us Amit Wadhwaney, the Portfolio Manager of Third Avenue International Value Fund. Welcome.

A: Thank you. Thank you very much.

Q: Amit, before we begin I'd also like to thank Chris Swasbrook of Elevation Capital for making this conversation possible.

A: Absolutely, and so should I thank Chris as well. Thank you, Chris.

Q: Amit, before we get into the investment approach of Third Avenue and how we can all learn from Marty Whitman and what wisdom he has shared over time with us, it would be great to hear a little bit about your background and how you got interested in investing.

A: Well, there was a succession of coincidences and interesting sort of succession of curiosities which got me into this. Years ago I studied engineering and mathematics. I stumbled into economics, a subject I actually thoroughly detested. Of course, if you are at all interested in economics you're often interested in pricing and how things are worth and what they're valued at, how prices are developed in markets. That's sort of one part of it.

When I studied for economics, I wound up getting Marty's book. Completely by accident I encountered a review of the book, Marty's first book *The Aggressive Conservative Investor*. I promise you it's a terrifically turgent read. It's probably one of the most informative and I think one of the most thought-provoking books about investing that I've read over the years. It was my first book. It's a very tough spot if you don't know much accounting, which I did not at that time. And nonetheless it was intuitively obvious, very engaging and I thought that was the beginning of something.

I went to business school after that, and of course business school was completely the opposite. It was an efficient market school, one of the schools where they teach you everything that's known as embedded stock prices, which is diametrically opposed to this book.

Returning from the business school I re-read the book and I thought I was pretty well hooked at that point. It's intuitively a totally reasonable area, totally reasonable way of thinking and approaching investing. And over time I suppose this interest deepened. Again, I can't say I know lots about other kinds of investing, because what's been of interest to me is value investing and various outfits of incarnations, various versions and types and different ways in which it's done. But value investing is something that's obviously very engaging and it started probably in 1979. I had the option to come work with Marty Whitman, and that was an even bigger part of the learning experience.

Q: So tell us a bit about that experience and how did working with Marty Whitman influence you. What are some of the key take-aways and learnings from one of the investment greats Marty Whitman?

A: Well, Marty is very, very focused on value investing, but value investing in his own way. Now, what is value investing as per Marty, as per Third Avenue? It really is a focus on a few things, a few very, very important things. One, of course, is intense risk aversion. The other is valuation, buying things cheaply. Again, that's at the core of what we call the safe and cheap approach to buying businesses or assets at a meaningful discount of what they'd be worth to another cash purchaser at a non-hype, non-distress type transaction.

There's a few things about this approach to value investing which puts us at one end of the spectrum of value investors. Now, again, value investing is a very broad term, it's gotten broader over the years. There's a great diversity of practitioners in this. And value investing as practiced here at Third Avenue revolves around a few things. First, we're bottom-up investors. Bottom-up investors tend to be focused really very much on the business or assets that they're buying and the securities that they're purchasing. This is not to say that we're oblivious to things macro. We're obviously intensely aware of macro. In our case and in my case we focus really in a great way on companies outside the United States, across a wide variety of geographies and political regimes and governance regimes. You obviously have to worry about things which affect the company from the outside. So while we don't do lots of forecasting and we don't use a form of macro forecasting as a basis of investing, we will if we suspect or we discern a company's vulnerability to adverse macro developments, we will all certainly not buy it. So certainly we are very much bottom-up investors, very opportunistic, trying to buy businesses cheaply.

Now, a by-product of this is your selection process will result in a collection of securities which base no resemblance to any index whatsoever. So a portfolio selected in this manner is quite unusual, relative to a conventional, traditional portfolio.

The second aspect about this is conservatism that I alluded to, conservatism in valuing a business. Now, there are obviously different valuation techniques that are used by different investors. Some people are great fans of a discounted cash flow approach. Others will project earnings and earnings multiples. We don't do much of that. Look, we focus on what we know, the here and now, which is of course given our myopia about things macro. But in the absence of forecasting things macro, what do we know about a business here and now? What we know is a snapshot of the business as given to us by its balance sheet.

We take the balance sheet and parse it, split it up into its component parts. The left-hand side, which is the asset side, we will value the individual components as conservatively as possible. So, if you're thinking of a business today and had to close down the business today and sell off the pieces today, what would it be worth? What would it be worth if the business just closed its doors? So I'm not paying for a rosy future, or for a future for it for that matter. So our valuations and the assets typically tend to veer towards the very conservative ones.

Symmetrically the liabilities, that's the right-hand side of the balance sheet, because most businesses come with liabilities the liabilities are sitting on the balance sheet. Then there are other liabilities that are off the balance sheet, things that the company's committed to spend, the company's required to spend, needs to spend just to stay continuing in the business. So stuff that's known. And so going down the same line of reasoning, there are some recurrent spending items that occur for any company in its existence, so I call them the general business liabilities which are neither on nor off the balance sheet. And that is my big lump I call general business liabilities just for continuing the business. I capitalize it and deduct that.

So you're going to see a very large chunk of liabilities deducted from the assets, at the end of which you're going to see a very conservative net asset value. And what we try to do is buy at a discount to this net asset value. The reason for going down this path is it is robust in terms of being relatively limited in its use of forecasting the future. We're fairly modest in our ability to forecast the people, unlike other people. Many people have, of course, pressure, can't see many years out, they pick the correct discount rate and forecast inflation and do all these things, these arithmetic things that produce numbers for them. We're not that clever. We're focused on the here and now, what is. What we see is what we do.

Now, again, this is not to say that we will not look for hidden values in assets. Visualize, for example, an asset. Think of this wonderful plot of land you may have between two big high rises. And it's a little townhouse maybe sitting there, carried as a townhouse. Or, for example, one actual example that we encountered a number of years ago, five years ago, was a parking lot. A terrible, decrepit six-story parking lot in one of our companies in Singapore had in the middle of a central business district. It was probably carried for $40-50 million. If you looked around it it was surrounded by 60-80 floor buildings. Now, this lot, this parking lot can be repurposed and a building constructed in the place of the parking lot. The lot was not worth $40-50 million. It was probably worth a few hundred million dollars. And that's, of course, ultimately what happened. But you have to think about your asset values not just conservatively and mechanically, but you also have to think of them creatively in terms of you have this asset, what could it be worth reasonably?

Third characteristic which is very, very important, it's not just a matter of cheapness, you could buy lots of cheap companies that wind up going bust. That's obviously what we strive to avoid. What we are trying to do is buy businesses which have survivability, which have staying power, staying power in the face of adversity of elements, both at the level of the business and both stemming from environmental factors. Again, I harp back to a comment I made earlier in terms of adverse macro economic developments effecting a business. And a company should be able to stay the course. So something that's cheap not only does not stay cheap forever but it grows as a business and can make its way through adversity.

So safety to us is really not the day-to-day stock price volatility, or market risk as people call it. People are very focused on that. That really is a distraction because once you made the decision to invest in something you are going to be taking on market risk. So that's a fact of life.

So what is the risk that we are trying to avoid? We are trying to avoid the sort of risks which stem from anything that's internal or external to the company resulting in the company losing value sharply, be permanently impaired, be not able to function as a business or going bust. So it's really survivability of a business, that's what we are interested in. Again, factors internal to the company would be bad balance sheet, bad management, bad business model. This is the sort of stuff that saves you a lot of grief. It's the sort of stuff that if you just mechanically can actually look at, think about and avoid you can save yourself a lot of grief.

And two small other characteristics of what we do, as I mentioned before we're very focused on balance sheets, mostly income statements. That obviously guides us. And finally we're long-term investors. Think in terms of investing in severely depressed securities for three to five years, and preferably a lot longer than that. And that's what we do.

Now, the reason why we talk in terms of three to five years is because when you buy things that are so out of favor it sometimes takes time for the clouds to part and the sun to shine through. So for example, factors depressing a company or a business or an industry need to work out over time for things to right themselves and sensible valuations to reassert themselves.

So these are sort of five quick characteristics: bottom up, very conservative valuations, avoid risk that can impair the value of your business, focus on balance sheets, focus on being a long-term investor. That's what we do here.

Q: You would think this focus on the balance sheet and also some of the asset heavy businesses that you tend to invest in, asset heavy businesses are seldom great businesses in the sense of a **Coca-Cola** [KO]. Potentially inflationary period could a focus some tangible assets rather than intangibles create some challenges?

A: Let me think back to some years earlier when I was growing up. My first exposure to the world of investing and investments in 1979, that was a period of high inflation. Pretty high inflation. The Volcker days. And inflation's really been coming down since '82, '83. Asset heavy businesses, the thing about asset heavy businesses is sometimes asset heavy businesses can present tremendous barriers to entry. They can be constructed in periods when there's either some sort of a bubble - witness, for example, fiber optic cables. Late fiber optic cables was an artifact of the telecomm bubble. The TMT bubble made doing stupid things like investing in fiber optic capacity very doable because people were willing to pay over the odds for what seemed to be negative net present value of things by just shoving cash at it.

If you can get a company with fiber optic cables embedded in the ground today this is something which is a very, very expensive thing to do now. And were inflation to rise further, were inflation to accelerate it'd be even more expensive. So the owner of such assets, given that there'd be very few new or additional capacity being put in the ground, would benefit from that.

Or, yet another example is this fiber optic cable idea is not entirely extract. We own such a company in Poland, for example, which was a creation of the telecomm bubble, whose original owners went bust because they leveraged out too much. So what you got was you bought an asset which could have cost you $1.2 billion to put into the ground. Initially you were paying about $300 million. And then during the 2008-2009 crisis we actually were paying an implied value of $200 million. It is currently the market value at about $700 million. We believe it's obviously worth a lot more. Not because of inflation but now it has a very large subscriber base and to replicate that would cost much more than $1.2 billion.

Q: Is that the example of **Netia** [Warsaw: NET]?

A: Netia, exactly, this Polish company. Another example of an asset-heavy company is a company which was just taken over. Actually, takeover is not finished yet; it should finish in about a month or so. It's a company called **Viterra** (Toronto: VT). Viterra is a Canadian agricultural grain handling company, listed in Canada but with a footprint both in Canada, Australia, New Zealand and the Ukraine. Its big business was owning grain elevators. Grain elevators, of course over time, are fairly capital intensive things to put in place. It's also sort of an oligopolistic business.

Viterra, for example, handles in Canada for western Canada currently about 46% of their shipments of grain that goes out from western Canada. And now that deregulation is beginning to take hold in August it's probably about the mid 50s. This is an agreement for handling infrastructure which is expensive and difficult to replicate. And, of course, as inflation over time is coming back it's even more so. Again, in Australia, they have a monopoly in South Australia and Victoria, which is more to my point.

So it depends on the nature of the asset and the business. So, for example, if you have a scarce asset as in the case of debt in fiber optic cables, in the case of Viterra with the grain handling network across the big grain producing provinces, as distinct from asset-like companies that own a slightly different scarce resource, intellectual property, the formula for Coke for example.

There are different kinds of things that can do very, very well in periods of inflation. Sometimes resource companies do quite well, as well, in addition. So there's a wide variety of things upon which the impact of inflation can happen.

Q: With resource companies — thinking of oil and gas companies — investors sometimes look to those companies also as in a way protection from inflation. What about the reinvestment? Isn't that a challenge for these companies in an inflationary environment?

A: Potentially, potentially. Let's take one example of a resource company which already has a reinvestment plan built in. Timber. Timber is a resource that grows. And, of course obviously, the reinvestment really is keeping your trees fertilized, pesticides, herbicides, that sort of stuff. But in general the reinvestment risk in, for example, something like a wire houser, for example, is somewhat low. Or someone that owns a very large stands. So along that line of reasoning, for example, we do **Weyerhaeuser** [WY]. We also own a Chilean company called **AntarChile** [Chile: ANTAR], which controls a company called **COPEC** [Chile: COPEC], which is one of the largest private land owners in Chile and they're a very large plantation of forests.

In the case of oil and gas companies, the question is what do you buy? Clearly oil is a depleting resource. There's no question about it. We have over time we've preferred companies with massive resource bases that are untapped. So there is clearly a reevaluation of assets in the resources in the ground. There's no question about it. But the ideal situation is one where there's only a minimal depletion on a year by year basis. That's the sort of preference I have.

Another area that's been of interest to us over the years has been agriculture in its many, many different forms. As you mentioned, we spoke earlier with an agriculture land company in Argentina, for example. Clearly that's an interesting thing, although it's probably not time for it just yet.

Other areas with agriculture related businesses; Viterra was one of those things. Alas, Viterra's probably no longer for this world so that's gone. But yes, inflation is something one does think about, one definitely things about. But yes, you're quite right, reinvestment is an issue but it depends on the nature of the business.

Q: You seek to invest in financially sound companies that are cheaply priced. What are some of the reasons some companies become cheap and which ones do you embrace as an investor and which ones are you more careful?

A: So people - there's a couple of things. There's actually a number of thoughts here. Financially sound is one of the slivers of a much broader aspect of being safe. When you talked about risk and risk aversion, the kind of risks you avoid is not just financially unsound companies. That's one of a number of things. For example, you'd worry about the governance aspects, you'd worry about things not just bad balance sheets, bad business models, a bad industry. Sometimes you avoid bad industries.

For example, a typically industry to avoid for me, for my preference, is an industry where there are limited barriers to entry. So we buy companies which are depressed, where industries are depressed, companies are having difficulties. And we're very patient investors. We're happy owning these things for a long period of time such that when times turn around these companies do really well. Now, when I say really well, they have a period where they own I'd say supernormal profits.

The problem with having a company which is depressed but in an industry where entry is easy, you will have very, very short periods with supernormal profits, which is one of the reasons you will see us as biased. Yes, why we're value investors. Yes, why we don't buy franchises. Yes, why we don't buy the sort of obvious brands and boats. Our companies do have some barriers to entry. That's an element of the safety I seek.

So financial soundness is one of those characteristics. How do financially sound companies become cheap? Well, here's the thing. We are long-term investors. We're shamelessly long-term. And I have no qualms about dropping anchor with a view that I'm going to own this thing for three to five years. My sort of approach to this and to my longer colleagues is if this is not something I'm going to go to bed with every night for the next five years I don't want to own it. It's just not worth it. What that does is it raises the bar in terms of soundness across all these different parameters.

Why do these things become cheap? Well, sometimes people are very fixated on earnings. Earnings, earnings disappointment, ROCs drop, sometimes adverse things happen. This presents an opportunity to us. For example, just to give you an example of a company that we used to own, we were the largest shareholder, an Australian agriculture company which Viterra actually wound up buying. The stupidest thing made it cheap. This company was a monopoly kind of like Viterra. Same business in southern Australia, it was a monopoly. And as a monopoly it was not a very clever monopoly. It was sort of a half-hearted monopoly. It was a half-hearted monopoly so you're the only supplier and all you have to show for being a monopoly is only 3% of your assets. That's not a very clever monopoly, right? So I'm presuming you can start slowly, gradually tweaking it higher and higher, but they were very slow about that so it was a very imperceptible improvement in the rate of return on capital.

So we reasoned, look, this is so cheap as a monopoly. And what made it cheap as a monopoly - it was a very financially sound company - was that they had a bad year weather-wise. There was a draught in

Australia. This I think probably goes back to the 2005-2006 period, December of 2005. We got very busy in December of 2005, early 2006. That was the Australian summer. Bad harvests. The thing about this company is earnings were very linked to the amount of grain grown in southern Australia. Because of the bad harvest, because there was a draught, there was a lower harvest. Less grain was handled. Less grain was handled, their revenues went down, their earnings went down, people freaked out, sold their stock. And that's how we became the largest shareholder of the company.

Now, I know that sounds stupid but that's the way it often works. People are very focused on the here and now. They have a very narrow way of using earnings as the basis of valuation. What they were completely ignoring was this company had this amazing infrastructure all the way from gathering grain grown by the farmers, storing, holding, grading it, transporting it to the terminals of the port where they had a monopoly yet again and sending it on. So I couldn't tell you when the rains were going to come but I could tell you the stock was cheap and the company had a good enough balance sheet to be a survivor. So people are often very focused on earnings, that's one thing.

Another thing that causes financially strong companies to be cheap is sometimes - I hate to say this because the industry we operate in is populated by some very bright, very intelligent people. Sometimes people get lazy. Sometimes people are not ready to lock themselves up in a room for one day and sit down with pencil and paper and add up the numbers. That actually produces interesting values for us.

Sometimes there's things that are sitting there, glaringly obvious to us, and I wonder what caused people to miss this. Things that are large enough in terms of capitalization, that are not obscure companies, things in developing markets which are very small - we focus on everything like Singapore. Sometimes structures in which these companies are embedded could be complex. People might not be willing to sort of do the leg work to pull apart the structure, do the valuation very carefully and do it. Sometimes it's diligence. There's a lot of stuff to do. People can be very distracted; people could also have very short-term horizons. Hard to tell.

Q: You distinguish between market risk and investing risk, seeking to take the former or limiting the latter. You touched on some of that already but could you give us an example that really highlights that?

A: Market risk is anytime you buy a stock your stock could go up, down, up and down or sideways. You are taking market risk. It's a fact of life. If you don't like market risk, buy T-bills. It's as simple as that. Now, it's a fact of life that's unavoidable so what is the investment risk that I avoid? Market risk I co-exist with. What is this investment risk that I strive to avoid? Investment risk is what I would expose myself to in terms of adverse developments at the company that I buy. Because of factors internal or external to the business. Basically it is anything internal or external to the company that could permanently damage the value of the business that you bought. It could be - very generic internal factors could be a poor balance sheet.

Poor balance sheets expose you to a lot of risk. Anytime you buy a company with a poor balance sheet you are effectively de facto taking on some very serious investment risk. What if the company cannot refinance? People always assume companies can refinance. Well, you have seen that happen again and again, again and again, where companies had difficulties refinancing and then go bust.

Bad management, well, right there, people doing stupid things with your money is not something you want to do. They could be dishonest, they could be stupid. You want to have neither. So think of what these people have done over the many years in the past. Separate emotional management from sort of nose to the grindstone, serious, hard working people.

Third risk internal to a company could be a bad business model. Let me give you an example of a bad business model, avoiding which has kept us out of so much trouble over the years. It's more about when companies because of their business have to access capital markets or financial institutions again and again to keep their business moving forward. I'm not out of companies that need to access capital markets in order to grow the business, to make an acquisition, but ones that need to for recurrent business needs go to capital markets again and again.

Now, examples of companies like that, which we obviously avoided because of a business model I'm very, very wary of, is businesses like investment banks that had big capital markets operations. Witness Lehman Brothers, witness Bear Stearns. Both of them needed credit rating. Credit rating agencies one morning freak out, that's the end of those businesses. That's not the kind of business I want to own. Obviously that's imperfect, it means eliminating businesses because this blunt instrument of eliminating a kind of business also eliminates the Goldman Sachses and Morgan Stanleys, which have so far been very successful companies and still surviving companies. So there are some business models we're very wary of.

What are external factors? Factors external to a business that we're wary about, obviously businesses or industries that are very sensitive to government meddling. Now, government meddling is a wild card, you never know what that is. Anytime you invest in certain countries you are probably taking on more business risk, more sort of government risk, regulatory risk than others. Investing in Russia comes with its own sort of issues. Although, let's not take it out on Russia. Let's take it out on other countries like New Zealand, for example.

Isn't New Zealand one of the cleanest governments in the world? Well, an example there was some years ago we used to own a company called **Telecom Corporation of New Zealand** [NZTCY]. Fine company, bought it because we believed that its competitors would die, which is exactly what happened. It turned into a duopoly in the fixed line business, a duopoly in the wireless business. The company was doing brilliantly, had lots of excess cash. Until, of course, the incumbent government in power, Helen Clark's government – let's name names here – decided, and she was very unpopular. She said, "One of the ways I'm going to bring my popularity back is, let's beat up on Telecom Corporation of New Zealand. The shareholders are foreigners, they don't vote in New Zealand. Let's break up Telecom Corporation of New Zealand. And let us also make sure that New Zealand telecom winds up getting farmers broadband access at the same rate they give people access in large, major sectors." Obviously a highly unprofitable venture, but supposedly very popular. She thought it was going to be very popular.

Now, imagine the impact of that on a company like Telecom Corporation of New Zealand. So the business purpose was being bent to support political ends. That does not work for people like us. As that news began to break we sold. It was a profitable investment. We thank God we've never had to look back at that as, of course, she was not reelected. Her policy was so ridiculous in any event. But that's an example of government policy changes can really blindside you. Handicapping governance is not easy. Some governments it's easier - Argentina, for example, is a very easy thing.

Or, for example, another sort of external risk that we worry about a lot is — and I alluded to that — is industry structure risk. There's some industries that I won't invest in. Industries which have, as I said, ease of entry, for example. Industries which have unusual competitive characteristics. Why bother? There is probably easier ways to make money.

Q: Now, you manage an international fund at Third Avenue. How does your approach to international investing differ, if at all, from that to investing in the U.S. as you have funds investing in the U.S. as well?

A: Sure. Now, in the old days people used to think the U.S. was sort of a risk free market, you didn't have to worry about things like political risk. Well, one thing you don't have to worry about is exchange rate risk. If you value things in U.S. dollars, well, it's going to be U.S. dollars here. There's a number of things.

First and foremost, U.S. investors have been spoon-fed lots of information over the years. Spoon-fed in a sense that there's a lot of information that's mandated and regulated to be disclosed, and that happens in the U.S. It's somewhat less than that outside the U.S. When I started investing professionally outside the U.S., that really goes back to the mid-1990s, there was a lot less disclosure available outside. You'd obviously invest in businesses you understand, where disclosure was adequate. But what you do, one thing you tended to do is not just rely upon mandated disclosure. You do a lot more digging, a lot more leg work, a lot more kicking the tires. You develop a lot more know who. There's a lot of other sources of information.

In the U.S. most investors very often just content themselves with the 10-Qs, the 10-Ks and that sort of stuff, the proxies and so forth. Well, you have much of that in countries like Canada. That is also sort of available outside more and more and more and more. It is available. So that has changed.

The other differences - there are many. In terms of takeover codes, for example, in some ways I find the takeover codes much more conducive in other parts of the world. In various Anglo-Saxon countries, for example, you can block hostile takeovers, you can block takeovers or takeunders with a 10% holding, and we have done that in the past successfully to good end. And so you have to be cognizant of the regulatory environment.

The other thing, going back to disclosure, is the aupacity. Depending on the nature of the company you own and the country you own it, it could be controlled by other entities. So you obviously have to worry about things like related party dealings. Sometimes asset rich companies attract not-such-nice people. And that is obviously something we are totally paranoid about. To be quite candid about it, you worry about who is going to take money out of your pocket. We focus on companies with big balance sheets, very liquid balance sheets, often flush with cash. If, for example, the parent of this company is a highly leveraged company, the highly leveraged company might want to dip its hands into your pocket to extract that cash. So related party sometimes might be easier in other countries. So you approach a level of paranoia. But again, this is true in the U.S. as well, in issues of securities of related parties. But the reporting requirements are bigger and better in the U.S. and have a greater frequency.

But you do much the same sort of stuff. You approach things with a greater layer of concern, for example. In foreign countries, one of the factors that has sunk many investors over the years has been the idea of currency mismatches. I think people don't focus on it that much. For example, in other countries — I mean, it's true in the U.S. as well, but in other countries much, much more so — in a given company, revenue streams and costs could be different currencies, assets and liabilities are different currencies. That is particularly bad if your company has a leveraged balance sheet.

For example, over the years let's name a few of these wonderful crises that would have been great opportunities. The tequila crisis of the mid-1990s, you had the Asian crisis in 1998, you had Argentina blowing up in 2001. A common thread that ran through these things was, with a very different set of origins, was that the currency financial institutions had their liabilities denominated in, very often U.S. dollars, was different from the currency in which their assets were. So a repricing of assets caused by devaluation or unpegging, you had a massive asset liability mismatch and the banks blew up. But banks are a particular example because they're highly leveraged capital structures, and of course this is where currency mismatch is at its most acute in terms of its impact, but corporates similarly can blow up and have blown up. So there's that.

Another aspect about foreign markets versus U.S. markets — and again, this depends upon the history — in many developing companies before capital markets are really developed you typically used to have a company highly cash generative which was a source of capital for another company. That's how you developed what they call group structures or in Korea they call them chaebols, for example. So the thing about these things is you could have these octopus-like structures, you could have a lot of opacity or related-party dealings, you could have a lot of currency, you could have a lot of bad stuff going on. This is something that South Korea found out in a very, very big way during the Asian crisis in 1998, which is one of the reasons why the rules related to chaebols have been completely revised to diminish systemic risk in South Korea companies, the chaebols in particular.

There is that aspect to there are risks peculiar to each market so it's hard to generalize across markets. I will trade you a statement such as we had two years ago, in the very early years. The first fund I was managing, which continues to this very day, had to take recourse to the

Sri Lankan SEC about some mischief that was going on. And they responded faster than you could ever imagine the Japanese SEC responding. So it is not a matter of development or the degree of development or size of the capital market. It's very much on a market by market basis. Hard to generalize.

Q: Well, would you perhaps single out some of the markets that are more transparent, if we take Asia? What are some of the role models perhaps for some other countries to aspire to when it comes to regulating a financial market in a sense that's conducive to foreign capital and wealth creation on the long term? Who gets it? Hong Kong? Singapore?

A: Well, a funny thing is in 1996 I wrote a piece about this, emerging markets, that they would inexorably, because of their growth needs, therefore the capital needs, would have to become more transparent, would have to improve the regulatory environment so as to attract foreign capital. So where are we now? Well, many of these markets have actually leapt over and done that, have actually leapt over in fact it's not just the markets doing it but individual companies themselves doing it, improving the level of disclosure themselves such that they could even within the context of their own market attract foreign shareholders to buy their shares in those markets. A separate industry for the markets themselves.

Now, in terms of Singapore and Hong Kong, they're not bad. Are they the most transparent? Reasonably, but not quite. Singapore's quarterly reporting, Hong Kong still does not have quarterly reporting. In terms of markets themselves, it's a company by company thing. In terms of actual markets being watchful, Singapore will get very high marks in terms of actually being very watchful. Actually, little New Zealand and little Norway might, as well, get - it really will vary by market. It totally varies by markets. Some markets make exceptions. France. Well, for French companies sometimes exceptions happen. Clearly there are markets on the other end of the spectrum in countries in Europe which have always been a very sort of iffy, edgy place to invest in. Italy, for example.

We made our very first Italian investment after much hemming and hawing in November 2010, which worked out very, very well. But it took a lot of agonizing and worrying about what could go wrong. We did not, in that case, depend upon the market regulations to be protective of us. We expected a limited degree of protection.

Anglo-Saxon countries historically have been better in some ways. And I'm not talking of quality financial reporting, per se, but in terms of regulatory oversight. It really varies. This is as distinct from accounting principles. Continental European companies, in some ways, can have much more conservative account then, say, the UK for example, which has a little bit more book accounting, I'd say. On the other hand, the regulators in the UK would snap to attention much faster, in many cases, than some of the continental ones. So generalizations are very hard. Company specific situations will determine.

A lot depends upon the company itself, in terms of what they want to tell you, why they want to tell you that and so forth. It's hard to generalize.

Q: How do you generate investment ideas?

A: We're an opportunistic investment group. We look for things around the world. We're happy doing stuff from developing countries as well as developed countries. I'm doing this for 15 years, 16 years, or more than that actually. You have an accumulated knowledge base of companies really. Well, companies, people who've done what to people, so you know who to stay away from.

You also have learned a lot about the landscape in various countries. We've probably looked at pretty much every company in New Zealand, most companies in Norway. That sort of stuff, we spend a lot of time looking at individual companies. So that's an enormous body of accumulated knowledge in our group.

I'll give you an example of that. For example, we looked in Brazil for a number of years and it was just very difficult to find anything that was cheap and safe there for us. So we just did nothing. We did nothing in Brazil. We'd visit companies, companies would visit us here, we'd learn about them, we'd put our notes into our database and put them aside. Finally after all these years of no results in Brazil - well, bad things had been happening in Brazil in many emerging markets. Suddenly Brazilian stock started getting cheap. And, in fact, some of the companies that we thought were very interesting were among those companies so we could move fairly rapidly.

What causes it? This is the asset of being sort of aware and ready for opportunities but what causes opportunities to happen? Well, it could be a few things what gives us these chances. It could be company specific disaster; it could be an industry wide unpleasantness, downturn, cyclical depression of the industry. Or it could be economy wide or cross-economies. You could have some sort of capital market event that seems to be going on and on and on and on in Europe, providing different opportunities at different points, obviously. But so you have some degree of readiness but your ability to respond should be there.

Sometimes opportunities are fleeting; sometimes you have the luxury of time to build up your positions. But you have to have some degree of preparedness, some degree of knowledge, for example. For example, you could see looking back a couple of years, the sense was Romania was going to hit a brick wall. There wasn't a whole lot there in terms of investable stuff. The odd thing was the crisis that ensued and the IMF's prescriptions has generated an ever expanding list of potential securities. So from what was not even an investable place, there was not a whole lot to do there, there's development.

Or, for example - you keep your eyes on the world. You keep your eyes to what's out there, what could be out there, what isn't out there today, and learn about it. You have to be a curious person. So I tell my colleagues, "Look, if you're not hungry today looking around, you're definitely going to be hungry tomorrow. You won't have captured your meal."

Q: Now, just in that context, do you use screens much?

A: No. The problem with - there's a number of problems with screens. Everybody uses them. I'm usually the last person to get around to these things. Everybody uses screens for the same kinds of things - price to book, price to earnings, price to sales, price momentum, a whole bunch of similar kinds of things. So I'm not sure I have any value add in that.

Third, screens tend to rely on historic accounting information. Historic and accounting, there's a gap oftentimes between accounting values and economic values. Now, what we're interested in is finding this gap. That's what we're interested in. For example, just a very prosaic example, a very silly example, in zinc in the early 2000s it was going through a very bad - the metal zinc, base metal. By the time we got our act together to look at zinc it was 2004. And zinc was below the cost production for about 55-60% of the world's producers. They were still producing. Many of them had written down their assets to nothing. For example, gigantic mines had been written down to nothing. They had no accounting value but they had economic value.

Now, the screen would have captured a sort of premium price to book in the case of a mining company that had written down its accounting value, its value of the mine for accounting purposes. But lo and behold, three or four years later when the zinc prices turned around, this mine kicked on, came on stream and it was gushing cash. So screens can be misleading in that regard. Screens are very focused on accounting values.

There's yet a fourth reason why, which is a much more interesting reason from my perspective, because I like to look at industry structures and how they change. In the case of depressed industries what happens is sometimes industry structures change, consolidation happens, closure of capacity can happen, market shares change. So the profitability of a company historically is absolutely no indication of what happens in the future. So industry structure change can sow the seeds for very, very different industry dynamics and profitability. Screens are completely useless for that. So there is that aspect to it. So there's a lot of things, softer facts, harder facts that screens just don't capture. People like them, people are good with them. It's not a skill of mine.

Q: Looking at your portfolio, what sticks out is some holding companies, agriculture investments, real estate. Where do you see the biggest inefficiencies? And I know it's all company specific but are there any - for example, holding companies, is there a bit of a theme? Do you perhaps look for holding companies?

A: Not per se. However, it's been a fairly fertile hunting ground. Holding companies come in many, many different kinds of shapes and sizes and textures. I mean, let me sort of reject a few that are never going to be of interest to me. For example, again holding companies all have their own histories which would to some degree influence and determine their purpose. So, for example, a holding company that exists for the sole purpose of exerting control of another entity or a collection of entities, for the sole purpose of that and nothing else, is of no interest to me.

An example of that — and I'm not saying it's a good or bad thing — is **Peugeot**'s holding company **PSA** [Paris: UG]. And it's always been a discount. I think Peugeot is not a brilliantly managed company and it shows. All they do is buy Peugeot shares and the discount narrows, the discount widens and whatever it is, it is. That's of no interest to me. It's always at a discount, so mechanically it's a discount.

Second, holding companies where there's control exerted, it's very important from my perspective to see the nature of control that's exerted. So, for example, during the early stages of the global financial crisis in 2008 when Europe is beginning to get hit in early to mid 2008 we bought a Swedish holding company called **Lundbergs** [Stockholm: LUND B], which we don't own anymore. Lundbergs is a family that controlled a collection of different investments focused largely on real estate and financial services and some metal bender, the standard Swedish industrial companies. Again, here was a situation where the family had AB shares, the two-class share structure that controls the company through the class of super-voting shares. So you had to be super cautious there as to what their motivations are, how are they running the companies. And you have to be brutally honest with yourself and critical in terms of the nature of the engagement with each of these holdings that they have and how they've added value over time. And to our mind they've done a very, very good job, hence that Swedish holding company got into our portfolio because of that.

For example, **Handelsbanken** [Stockholm: SHB], which is one of the banks over which they exerted a certain degree of influence; Handelsbanken was the only Swedish bank which did not have to go through recapitalization. All the other ones did […] So watchfulness in terms of control in a constructive way is an important thing, so that's another aspect. Are they adding value? That's very important.

Third factor is in terms of holding costs. What does it cost to run this business? We don't want yet another layer. Of course, often times holding companies are a very efficient way to own a cluster of assets which are managed cheaply. Compare it to a mutual fund, for example.

Is it compelling? Is it 0.2% of assets that they're managing and overseeing? So that kind of stuff. This is exerting yet another layer of cost? Ideally not.

Fourth, what should be important is are the assets inside it cheap and are they interesting to own? So that's getting to the core of what you're really trying to do with owning a holding company. So you have cheap assets sitting inside, you have on top of that a further holding company discount reflecting hopefully it's a big one. These are cheap; I hope it's a big discount to boot. And of course, either you're getting - think of it as a leveraged way of owning investments. So those things go up in value, the NAV increases and the discount shrinks. That's another aspect to it.

Now, what I do not like is the mechanically looking at discounts - this is a 40% discount which is better than this 24% discount. The stuff that could be contained in the company at a 40% discount could be expensive such whereas the one that is at a 24% discount could own severely depressed securities. So, clearly, the one at 24%. So you don't blindly follow discounts.

You won't have to own the stuff sitting inside it, and this is another layer of discount. Obviously governance, that you alluded to, is a very important thing. It's very, very, very important. And also an important thing is in terms of thinking. And like you think about corporate you have to think - there are two sets of thoughts you have to think through. The underlying corporate entities, are they of interest to you? And the sort of overlay of the holder, the owner, the control party, is their orientation aligned with yours? So are they communities of interest or are they going to rip you off? Are they going to screw you? You have to worry about that. If you worry about that at the level of the companies you have to worry about that additionally at the level of the control parties. So the usual paranoia applies.

There's one last thing. So - and this is something really, really highlighted by the global financial crisis. So there's a collection of holding companies and in those days a number of them were in France, and still are, that used to do some private equity type investing. There's a bunch of those. There's all kinds of holding companies out there in this world. So the argument that they would lay out is that, "We're doing these buyouts, we own equity in these companies which we control, we oversee them. And the leverage is at the operating company. We upstairs, the holding company, have a clean balance sheet or a cashed up balance sheet. So we have no net debt that we're talking about." All true, all factual. And the debt at the level of the operating company is non-recourse to the holding company. Also true, very good. And, of course, the debt is at the operating company so there's matching cash in and cash out to support the debt. All good.

So what's wrong with this picture? Well, what's wrong with this picture is the following. You own these holding companies. You, Mister Holding Company, own the leveraged companies. And the problem is the global financial crisis did some nasty stuff to some of the businesses. Leveraged businesses found they couldn't refinance stuff. Leveraged businesses found that they weren't making much money and that it'd be even harder for them to service their debt. So, effectively, what was non-recourse, the gun to the holding company's head was if you don't stick in equity capital you are going to lose all your equity in this business.

So was it really non-recourse? Yes, it was a non-recourse operation but it was very much recourse. So you have to separate the leveraging. So in general, we do not like A, leverage of the holding company. And, B, we do not like a lot of leveraging down below either. We do not like too much leveraging going on down below either. So that is very important for us. So that's sort of how we think of holding companies.

Q: Now, there's a lot of noise around Europe and some would say there could be naturally some dislocations, inefficiencies there. How do you make sense of it? What opportunities do you see arising from this European crisis?

A: Europe has been evolving opportunities. From the early stages of the global financial crisis in 2008, early 2009, we saw options in northern Europe. Two kinds of opportunities. We saw opportunities in some German financial institutions - insurance companies, not banks. We saw opportunities in manufacturing companies in Austria, in the holding company I mentioned earlier on in Sweden. We also saw opportunities in French operating manufacturing companies. So that opportunity set existed.

[…] The opportunity set seems to have moved further south, so gingerly, gingerly we approach the south. South being the exciting part of Europe, which is Italy, Spain, Portugal, Greece, all of those, all of those countries. So we made our first Italian investment in 2010, November. The company was the object of a takeover bid in early 2011, which is extremely irritating. It was very profitable. We thought we could have made a lot more money over time, compounding it over time. So, of course, we had to look for more ideas.

We own a Greek cement company [**Titan Cement Company**] [Athens: TITP]. Before I get into the details, think of what we're trying to do. We want to buy businesses cheaply that are going to be around for a while. So going back to the discussion about business models, about not needing recurring financing, you make the first important assumption that the capital markets are going to close down. You, company in Greece or company in Italy or company in Spain, are not going to have access because your banks are bust. And nobody wants to write a check for a Spanish company or an Italian company.

So you should have the ability to survive on your own for a reasonable period of time, a year or two years, without having recourse of external financing. Because otherwise you might be in the position that if you don't get your bank financing in place you might have to engage a terrible idea. Equity financing, for example, there's always somebody willing to write a check at a price. If I'm your investor I don't want to tie me down to financing, too, and reduce the value of my holdings. So you've got to be able to survive the near term assuming the closure of capital markets or socio-external financing.

The second thing, which is very peculiar to the situation, now everybody threatens to throw everybody else out of the Euro. So Germany's going to throw Greece out, Germany's going to throw Italy out and Spain out. There's this sort of angst-ridden drama that's unfolding. So Euros are fine. We saw Argentina unpeg itself so we can assume the drachma might unpeg itself from the Euro or the peseta unpeg itself or the lira to unpeg itself. And yes, you will have this new currency. So you ask the question.

Now, suppose the drachma will come back, would our Greek cement company survive? It was an obvious question for us to ask when we bought our Italian investment of **Parmalat** [Milan: PLT], would Parmalat survive if the lira came back. And the short answer was of course it would. Parmalat had two issues. It had 1.6 billion Euros of cash and was making money around the world - excess cash. So capital markets are not an issue. Second, Parmalat, yes it was listed in Milan, traded in Italy. It was an Italian company but the Canadian business was bigger than the Italian business, the Australian business was bigger than the Italian business. And they did stuff in the rest of the world. So Italy was a part of its business but it was not a deal killer for us. So that's why Parmalat made sense to us.

So what about a cement company in Greece? Well, we own the cement company in Greece because it is listed in Greece but does a lot more outside Greece than it does inside Greece. And I suppose it could be a comforting fact, at some point in the future like it had been in years past, that Greece is a duopoly. It's a duopoly which has always been oversupplied with cement. And most of the cement is exported.

Because cement is exported the reintroduction of a drachma, I suppose, is probably good for that company. But this company also has operations in Turkey, in Egypt, in many of the Balkan countries. It also is a reasonable sized player in southern Atlantic states in the United States - it's actually quite big in Florida, it's a big player in Florida. And maybe the Florida market will revive before the Greek market. Who knows? And it doesn't need financing. So that's how we own that.

Now, the problem with buying in these markets, mechanically you can see cheapness. The problem is how did the banks and how did everybody get so crazy and leveraged? Well, the banks lent a lot. So companies borrowed a lot. And witnessing the stuff that's been going on, a lot of these companies in Spain went out and acquired stuff in Latin America. Witness **Repsol**'s [Madrid: REP] newest adventures. Repsol's adventures in Argentina, for example. Repsol's busy. Expansion oil companies have to look outside Spain for oil and resources, and they did - legitimately and reasonably. So of course they went outside Spain. So finding companies that are cheap, meet our criteria obviously in terms of safety - safety from a capital markets perspective, from a perspective of governance, that's quite important both sometimes by the company's control and sometimes by the high end leveraged owners above. So, of course, the temptation is to do stuff which may or may not be good for you.

For example, you can talk about **Endesa** [Madrid: ELE]. Endesa's a big Spanish utility. Now, the problem is sitting on top of it is, **Enel** [Milan: ENEL], which owns 90% of Endesa. Enel is a highly leveraged Italian utility. So, we know who's going to finance whom. So that's the sort of problem you've got to worry about. What are the owners like? What are their motivations? Will they strip cash out of you and leave you with nothing? It's not as easy as it sounds.

Q: When we look at your portfolio, however, currently you have little to no investments in companies headquartered in what's labeled as peripheral Europe. So is that a reflection of you just haven't found the opportunities yet? Or is there more to it?

A: It's not been for lack of trying. I will say that, I will admit that. We do have something in Greece; we did have something in Italy which was taken over. You may well see stuff there; you may well see stuff there. I will never say never in that regard, but it may look deceptively easy if you look at valuations. The numbers, valuation wise, in some ways look cheap. Unfortunately each of these companies comes with issues. We have balance sheet issues, we have currency mismatch issues, we have governance issues. There's always something that's been the deal breaker for us there. So I will not say no that there won't be stuff in the future. We may see stuff in Italy and Spain in the future, respectively. I will not forecast that. Again, we are usually out there responding to opportunities. We do have ideas. Pricing may not be right.

Q: Let's move onto another market that a lot of value investors actually are shunning, but you've been there for some times and have large holdings in Japan. How do you approach Japan? What is different about your approach and why do you see value in Japan? And then where do you see it in Japan?

A: Now, a couple of things. Japan, if you were focused on safe and cheap and forgot about everything else your portfolio would have nothing but Japan in it. It is very, very cheap. Numerically it's very cheap. And companies are often flush with cash. It is neglected, it is disliked, it meets many of these criterias that draw people - some would say suckers - like us. There's a whole collection of value investors there gnashing their teeth and wondering what is it that we do and have done?

First, before last year, before 2011, disproportionally to my mind value existed in the domestic companies. Disproportionally by a big margin. Exporters were battle hardened. Locally Japanese companies have been coceted, coddled, and the local companies tend to operate quite differently.

So our focus was on domestic companies. They all met the safe and cheap criteria. Now, the question of course you ask is after some years of requisite impatience and nothing happening, how are we going to make money here? That's the question everybody asks. So having been worried about that same question some years ago earlier, having watched - you must understand, my history with Japan goes back to the early to mid 1990s. And Japan has been a place where you invest and you wait and wait and wait and suddenly make money, lots of it and very fast. It's always been this sort of hockey stick phenomenon. It's like watching paint dry.

Now, this time may be different. I don't know, I can't tell you. But the way I've approached this is you buy things, you put yourself in the path of some kind of change, change which may come from the companies themselves doing the right sort of thing. So we don't buy perfect companies. Let me be very clear about this. Are these great capital allocators? Often not.

Let me give you an example of one of our holdings which we have, which has done everything right except for one of the most important things. **Mitsui Fudosan** [Tokyo: 8801] is a magnificent real estate company, almost near trophy real estate. A great balance sheet, growing the top rapidly. It's building. They're building buildings; they're doing all the right sorts of things. However, what's the rub? The rub is the following. You're building buildings there with cap rates of 5% when you can repurchase shares at high single digits like 9-10%. To my mind it's not a very big leap of imagination that gets you there. Yet, for the last number of years they visited us here, for the last number of years we asked them, "Why do you not do that?" They said, "No, no, no, we have to grow the business."

So the business is growing. It is cheap. And it may stay cheap for a while. However, value is building. We are waiting for the lightning bolt to hit there.

Q: So what do you say to people who when you tell them about your approach to Japan and then they say, "Well, yes, I get what you're saying but how do you get over this corporate governance?"

A: Please. You have terrible corporate governance in other places, too. Japan's been, I think, singled out. Japan has been pushed into a crisis. They will change. They will change. Japan's response to the tsunami and Fukushima was shockingly slow. You're actually seeing change, I think, flowing from that now. I'm a patient investor. Again, we don't have a huge amount in Japan. Some people are very Japan sensitive so they won't buy it if you have an index rating. Again, we bought what we could buy which was interesting to us. We are very patient. We are seeing industries reconfigure, restructure themselves. We are seeing gradually eke out more and more and more.

The response of Japanese companies has not been entirely irrational. For example, for companies to hang on to cash in a period of deflation is a very rational response. It's a logical safety blanket. Logical, completely logical. Because it enhances the probabilities of survival. And they did that. They have very conservatively figured balance sheets to cope with this kind of deflation, the spiral the country went through. They also worked hard on their costs. There's a lot of good that's gone on in the process.

The arguments against Japan revolve around the lack of M&A market. Because if there was a very active M&A market you would seriously start to see a change happen in terms of valuations being recognized.

Q: So this argument about corporate governance then in your view does not reflect the specific opportunities that often pose exceptions to that overall negative view?

A: Oh yeah, I mean there's lots of reasons to avoid Japan. Lots of reasons, heavens. The graphics, the slow responses to crises, the civic economics. Maybe civic economics. A lot of stuff that they could do. A lot of the damage is self inflicted, quite clearly. The lack of active M&A market. But by the same token the steps are slow - baby steps, evolutionary steps is a culture not characterized by a lot of people wish to be outliers in their conduct.

Let me tell you yet another worry I have. Japanese companies being increasingly seized by the fear that Japan is so permanently ex-growth given the fact that there are too many of these cash balances, given the fact that there are fewer and fewer growth opportunities in Japan, we start making crazy acquisitions outside Japan at very high prices. That is, for me, a much more scary thing than the other ones you mentioned so far. That scares me because Japanese companies historically have not been the stingiest of acquirers. They have not been willing to engage in some knock them out, drag them out, got to fight to save the last nickel. They just have not. They don't have it in them. They prefer to be viewed as friendly. Friendly takeovers sometimes are expensive takeovers, unfortunately.

Q: Now, some people would also say that if they can get over the corporate governance then often would cite it as but it's bad, there are graphics and the economy. How do you perhaps realizing that that doesn't present a hurdle for you, how does that perhaps filter down to the selection of the specific companies? So I'm thinking are there any themes in terms of more export-oriented companies, more certain sectors? How does that enter if at all?

A: Well, the hurdle of getting into Japan is overcome by looking at two times earnings for companies. I'd rather be two times earnings for companies. Insurance companies, I used to certainly love the idea of owning insurance companies at fractions of book value, fractions of embedded value, as opposed to buying them at multiples and multiples of book value in China because China had growth, this had none. So that's one hurdle. I have a much bigger hurdle to deal with in the case of these growth markets, or at least once growth markets. They are repricing, too, as they should.

I wouldn't say export companies have particularly been a theme for us. The most recent purchase of ours - actually two of them - would be **Daiwa Securities** [Tokyo: 8601] which was largely domestic. In fact, unlike Nomura, they have so much smaller global ambitions so they're not going to do silly things like buy Lehman Brothers and then find out everybody runs away after they buy them and stuff like that, all that stuff. They're much more local, they're much more focused on things like their asset management business locally. That gives me a source of comfort.

So companies that have really narrowed their focus, where they're very good and very big players, is of some interest to us. A company we bought, **Otsuka** [Tokyo: 4768]. Otsuka trades a very modest model of operating earnings, which it has grown over the years. This is a company which is a systems integrator. It's a company which is kind of like Ingro Micro in the U.S., for example. They're very big, very big. And Japan has been itself a slow innovator in terms of its installed computer base. It's much, much, much slower. They're very good at what they do. It's a company which was set up by a Ricoh copier repair guy who basically got into these and saw this huge opportunity to help automate, modernize small to medium enterprises in Japan which were very, very slow. They've actually been growing and growing very rapidly at the expense of the mom and pops. And even in this horrible market they've been growing rapidly.

The surprise - what will and should and probably will surprise people more is the rate of earnings growth happening in Japan. That's not what we focused on. We focused on cheapness, bought our stocks and what happens, happens. I'm incapable of forecasting the future.

Q: What is the single biggest mistake that keeps investors from reaching their goals?

A: Straying from the discipline, believing that they're smarter than they are. So there's a number of things. I mean, one, it depends on what kind of investor you are. Let's talk of investing as opposed to the business of investing. There are different kinds of things. The difference determines success. There are overlaps but there are things specific to the business, specific things to the actual act of investing. Each of us - again, we all come with our package of beliefs. We all come with our intellectual constraints. We all come with our history. That conditions how we think, that conditions situations that we're better adapted to analyze, think about, constructively and creatively. Overreaching beyond that is a dangerous thing.

Some people, sometimes in the belief that they know more than they do, some people have the mistaken belief in numbers. Numbers, there's an exaggerated perception of numbers as opposed to what causes the numbers. One of the things Marty always says, "Forget what the numbers are. What do they say? What's behind those numbers?"

So people could take numbers too literally or people could overreach in other ways, overreach in terms of somehow people take on levels of risk that they probably shouldn't in expectations of greater glory. And, of course, they have their heads handed to them as a result. Do what you know. And be very, very risk averse because there's new ways of losing money being invented every day. Try to avoid being one of those people. I mean, it's so easy to do.

Q: How do you improve your investment process over time? Specifically your judgment of investments. Have you tweaked anything as a result of the crisis? Some value investors will say that they have tweaked something because of the more emphasis on the macro. What about you?

A: Well, my first watershed event in investing was the Asian crisis. That's when I started investing, was in '96. The last quarter of '96 or the first quarter. Then '97 went headlong into the Asian crisis. The operating principles have always been the same. The whole focus on survivability. I mean, safe and cheap has taken me through the Asian crisis. So the learning that happened then, even before the Asian crisis - because I had spent a number of years working with Marty by that point in time. So the focus on survivability has always been a very big part because when I started here we went headlong into - in 1990 there was a big financial crisis which was when Drexel went and blew up, the high index market blew up, a number of life insurance companies were going to blow up. In fact, the entire life insurance sector was going to blow up. In fact, property casualty companies got in trouble because this was a commercial real estate crisis which also insurance companies had. So there were multiples of interlocking financial things. That was the beginning of my investment education, was here.

So going into my own way of investing I go headlong into the Asian crisis. So okay, we have our own crisis to deal with now. So it was actually very simple. You just avoid companies which have — the valuations you're being presented with in those short periods is so ridiculously stupid. Companies are just swimming in cash, no reason to borrow. And you get an operating business for free. Now, that sounds good. You could do that. I could live with that. And, of course, those companies were multi-baggers after that.

But importantly though, what particularly colored me was how capital markets can close down. It didn't really happen in 1990. The high index market sort of imploded and closed down. But here the visual experience of watching people line up, pull their money out of Thai finance companies in 1990, July, is a rich experience. It's one that continues.

So if you're a company looking to run your business, and arguably in those days nobody really thought that would ever happen there, and of course a lot of people caught flak for it. So, that tells you what you have to do and what you don't have to do. You don't want to be in companies that need to borrow to keep their business going forward, or access capital markets. So that's always been a cornerstone.

Second, the other thing about that financial crisis, the other learning aspect which is also true for subsequent such events is you can buy stock very cheap and it gets cheaper. You value very conservative, value for worst case scenarios, and then start your buying. And assume that it's going to get cheaper. When people are in the middle of this mad panic value has nothing to do with them. They just want to extract the cash and separate themselves from that piece of paper that keeps going down to the next tic. And, of course, I'm there buying it and it goes down to the next tic anyway. So I keep buying some more.

A favorite example of mine was a Japanese securities brokerage company. I was buying during the heat and goings on in those days. There's a few of these things. The stock had a book value of 750 yen per share. I started buying at 260, had a completely clean balance sheet, had never lost money. This is '98. The Japanese bear market began in 1990. I had spent odds and ends of money and the stock had declined. I thought, "265, I'm brilliant at buying this thing." I bought a little bit, it went down. I bought a little more, it went down. It got to - I think it got to 145 and I thought, "Lord, I'm mad or somebody else is mad." So I bought some more. And the company announced a buyback of 10% of the company. I said, "That's going to put a floor under the stock." And they bought back 10% in one trade that day and the thing went to 120. I said, "This is pretty scary stuff."

So that was August 1998. And about a year later the thing had gone to 800 something yen per share. I was beside myself, exultant, sold my shares and it went to 1,700 after that. So brace yourself for terrible things to happen, but obviously all of the while making sure that this company has survivability. And the company is still around today. It's still very much around today. And very much a survivor. So not a whole lot of tweaking has happened.

Survivability has always been a part of it but the important thing also has been to look for - be very careful often. Situations where something that's cheap on an individual company level where you're buying conservatively, and then you get steam rolled by the macro, there's no predicting that and there will be no predicting that. But the way to defend yourself, at least partially, against that is the internal solvency and viability of the business in the absence of capital markets as well as being very, very, very conservative in your evaluations, that is very important. It's paramount. A value of being a very, very stingy person in terms of valuing securities has protected us so much against so many adverse developments. It hasn't eliminated the fact of things where you start buying at 265 and it goes to 120, but it reduces the pain relative to buying at 700.

Q: Now, you have the benefit of working alongside one of the investment greats, Marty Whitman. For those of us who don't have that opportunity, what are some of the resources, some of the books that you would recommend to young people starting out, to anybody who's really interested in improving their investment acumen.

A: A few things. Look, my path was the following. I encountered Marty's first book in 1979 when it was published. And I lucked into encountering Marty's work in the early '80s and wound up working with him in the '90s and thereafter. It was very lucky. Clearly, it was very lucky. And equally I was lucky to have survived it. Marty's a taskmaster. He's brilliant but he doesn't suffer fools.

Now, value investing is a much broader discipline than Third Avenue's approach to value. It is important that anybody who goes down this path be aware of a few things. Know yourself. There's certain kinds of things that value investors do which are not fun. Fun in terms of patience, fun in terms of due diligence. This is grunt work, this is hard work, it's very unglamorous. I would tell you growth investors have a far more glamorous life. That's the fun end of the business. Their companies are always growing, they always look good, they have high ROEs. It's always wonderful. We're at the other end of the spectrum. We do the unpleasant stuff, we deal with these terrible companies, terrible countries, companies facing difficulties, companies which may need recapitalized. There's all sorts of stuff. So know what you want to do. Value investing may or may not be for you. That's item number one.

But notwithstanding that, you really think value investing is for you, there's a lot of stuff that's been written about value. Books that come to mind - again, this is in no particular order - obviously Marty's first book, his original copy of *The Aggressive Conservative Investor* was, to me, a great book. As I said before and I will say without being bashful, the book's a damn turgent read. It's a deadly read but it's a very bright book. It's full of a lot of ideas. Then, of course, are the other books that he's written, namely *Value Investing, A Balanced Approach*. Those will get you going. And then, of course, is Seth Klarman's book, *The Margin of Safety* which also came out, I believe it was in the early '80s, if I recall. Seth's book was a fabulous book, a great book. It's a much more user friendly book, so there is that.

Then, of course, if you enjoy special situation investing, there's Joel Greenblatt's book. His book is *Anybody Can Be a Stock Market Genius* or something like that. It's got a very odd title. It's actually a very bright book; I think it's a very clever book. Again, I'm not a fan of mechanical investment formula. If that's what you do Joel has another book about that. Most recently there's Howard Marks' book. Howard Marks is a great writer. The book is a very nice, easy summary of what we do, what he does. There's no question there's lots of wisdom encapsulated in Howard Marks' book, which is a really worthy read…

So if you made it through all that stuff and you actually read Graham and Dodd's book, you really want to pursue it, the only way to do it is by doing it. Doing it is, I believe, a process of some degree of apprenticeship with somebody who is going to actually teach you. You can learn generalities. There's an art of recognizing these things. There's an art of not being freaked out by these things and these auctions where they're staring you in the face. There's an art of recognizing things that are sometimes very subtle, things that could hurt you. That's very important. You can only learn that by doing and you do it by ideally working with an experienced person. I mean, it's obviously easier said than done, finding the right person who's actually looking for somebody, or the right temperament to be a mentor. But that's probably the way to do it.

There's a lot you can do by yourself. Some of my personal values about investing and investments were formed before I came to work at Third Avenue. In part, they were based upon the books that I read. Obviously I read Seth's book well before I came here, Graham and Dodd, Benjamin Graham's *Intelligent Investor* as well as Marty's first book. So a lot of that was done.

Read, for example letters written by investors. I would recommend, obviously, the **Berkshire** [Hathaway] [BRK] letters. Obviously, obviously. They're a must read. I would recommend to you the letters written by the folks of **Leucadia** [LUK]. I think they're absolutely brilliant investors. I'd love to become like them when I grow up, if there's anybody I want to grow up to be. There's Cummings and Steinberg. Certainly the letters of Third Avenue Funds. I realize that's a plug, so I'm not an objective party. But we talk about a lot in the letters. We talk about the stuff that moves us, stuff that causes us to invest in things. The letters are a serious source of education.

At Third Avenue, we are some old guys, mentors to the young people. One of the thing our younger colleagues have taught us is a big part of their leaning experience is not just Marty's book but also the letters. So we would sort of commend you the letters. Again, I quote what they say. I would find it difficult to be able to bear reading those letters that we've written yet again. But I think they are apparently quite educational. They capture a moment in time as to how we've invested in specific investments and what we are thinking. So that's one way to do it.

Q: Amit, thank you so much for your time and all the insights you've shared with us.