

# THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

## Investing Globally Across Industries and Market Caps



**BERNARD R. HORN JR.** is President and Portfolio Manager of Polaris Capital Management, LLC, a leading Boston-based global and international value equity firm. Mr. Horn founded Polaris in April 1995 to expand his existing client base dating to the early 1980s. Mr. Horn has been managing Polaris' global and international portfolios since the firm's inception. The Polaris team manages the Polaris Global Value Fund. Mr. Horn's pure global value philosophy combines a quantitative global valuation model and investment technology with traditional fundamental research. His 29-year track record exceeds most current competitors in length, and he has produced admirable risk-adjusted returns since the Fund's inception. Known as a forerunner in global and international investing, Mr. Horn has been profiled in *SmartMoney Magazine*, *Business Week*, *Financial Times*, *Forbes*, *Fortune*, *Investor's Business Daily*, *The New York Times*, *The Wall Street Journal*, *Washington Post* and many other national publications. He has appeared on PBS Nightly Business Report, PBS' Consuelo Mack WealthTrack, CNBC, CNN and Bloomberg TV to discuss global market trends. In addition, Mr. Horn has served as a guest lecturer at various investor events, including the Value Investing Congress, Bloomberg Portfolio Manager Mash-Up and the Morningstar Investment Conference. His recently written works have included "International Diversification: Why it Still Makes Sense," published in the *American Association of Individual Investors Journal* (2010).

### SECTOR — GENERAL INVESTING

**TWST: What are some of the advantages of global investing?**

**Mr. Horn:** I started investing globally in the early 1980s, and at the time, it was an unpopular investment strategy because of foreign market risk and less globalization. Yet even then there were some inherent advantages that endure today — diversification, flexibility and opportunity. If you have money spread around in 10 or 20 different countries, you can achieve better diversification with less risk than putting all your money in a single country. Today, the Polaris Global Value Fund has holdings in at least 15 different countries and industry groups.

We can focus on finding the most undervalued companies in the world, regardless of country, industry or market capitalization. We also have the flexibility to invest in emerging markets, providing an additional avenue for exposure to some of the world's fastest-growing economies. We frequently identify opportunities in a particular sector or country that don't exist in other countries. For example, the Fund holds China-based **Guangdong Investment** (0270.HK), a water company that supplies all the drinking water to Hong Kong. If you want to invest in the steady stream of cash flow from supplying water in Hong Kong, you couldn't possibly make that investment by buying any other company.

We seek opportunities across all market caps, acknowledging that many of the new ideas, innovations and disruptive technologies stem from small and midcap companies. If you want to invest in the growth of the world, one way would be to pinpoint newly formed companies or parts of the world that are growing a little bit faster than one's home country.

**TWST: Would you tell us about the investment philosophy for the Polaris Global Value Fund (PGVFX)?**

**Mr. Horn:** Global markets have proven generally efficient over time, but investor behavior creates volatility that leads to inefficiency somewhere in the world. During these periods, the stock price may not reflect a company's long-term fundamental valuation and/or future cash flows. We seek to buy such undervalued companies worldwide.

Sticking to our pure value philosophy, we focus on companies that generate strong sustainable free cash flow and conservative balance sheets. We analyze streams of cash flow to determine which are trading at the highest expected return, as we consider this to be companies' contribution to shareholders. A company is a good candidate if its market value relative to the cash flow generation, on a pretty conservative outlook, is mismatched, and if it's priced to give us a return that exceeds the expected return on stocks generally.

Typically, companies with strong free cash flow are capable of growing stronger in difficult economic times, while performing admirably in growth cycles, too.

An unwavering commitment to pure value investing — time-tested over nearly three decades — has been the key to the Fund's strong long-term returns for investors. As managers of the Fund, Polaris Capital Management has one of the longest global and international track records of any firm presently in operation, and continuously managed by the same individuals.

**TWST: How do you narrow down your screens to ultimately determine Fund holdings?**

**Mr. Horn:** Our investment team regularly screens a database of more than 35,000 companies, many of which are small- to mid-cap, to produce a list of approximately 500 to 2,000 companies worldwide that we view to be the most undervalued. Our screening criteria include the valuation of a company's sustainable free cash flow, financial strength, market capitalization, liquidity and margins.

Then we do a fair amount of fundamental detailed analysis on the company to try to understand why it might be undervalued and what pessimistic investors might be missing. We make three-/five-year company projections, and if our analysis

appears different from expected future prices, the company may become a portfolio candidate.

Basically, bottom-up fundamental research comprises the vast majority of time we spend in the investment process. Fundamental research covers financial analyses of companies, including in-depth review of financial statements, research on suppliers, customers and competitors, and meetings with company management. Our analysts travel the world, assessing industry conditions, competitive advantages, profitability, operating and financial leverage, and the quality of management — in an effort to identify new companies that may enhance the performance of the Fund.

At a macro level, we do understand what is going on in the respective countries and industries in which we invest because we talk to hundreds of companies a year, and we understand their business conditions and how respective economies impact these companies. But, at the end of the day, we rely on a bottom-up process to find individual companies that we consider grossly undervalued.

**TWST: What is your sell discipline?**

**Mr. Horn:** We attempt to buy companies that are priced to give us above-average returns. Historically, global equities have earned investors about 6% after

inflation. When we look for an investable company, we must believe that it has the potential to earn a few percentage points above inflation, our alpha.

The decision to sell is primarily based on a company's common stock valuation and the expected return on the stock. We sell when a stock appreciates to its price target. On the other end of that spectrum, when the valuation of the stock no longer is priced to include inflation plus alpha, it becomes a potential sell target. If Polaris' investment analyses, financial models, and assumptions change over time, the buy and sell prices are altered to conform to actual company results, and the company value is reassessed. Sometimes there is fundamental deterioration in a company; other times, industry or country conditions impinge on the stock's ability to achieve alpha. At that point, we will sell the stock and replace it with another company on our watch list.

**TWST: As of June 30, one of your top holdings was Greencore Group. Would you tell us a little bit about that company?**

**Mr. Horn:** Greencore (GNC.L) is an example of a portfolio company that has relatively lower volatility. At Polaris, we aim to hedge against downside risks and to improve the risk/re-

### Highlights

*Bernard Horn Jr. of Polaris Capital Management discusses the advantages of global investing and how his outlook has evolved over recent decades. The Polaris Global Value Fund has holdings in at least 15 different countries and industry groups across market caps, and Mr. Horn explains where he sees additional opportunities. He also walks through the stock selection process and names key holdings. Companies include: Guangdong Investment (0270.HK); Greencore Group plc (GNC.L) and Methanex (MEOH).*

turn profile of the Fund. **Greencore** makes chilled foods, ready-to-eat meals and sandwich products that are primarily sold to large retail grocery stores in the U.K., like **Tesco** (TSCO.L), **Marks & Spencer's** (MKS.L) and **Asda**.

In the U.K., store brand goods comprise a high percentage of grocery store sales; in the U.S., such sales are still much less. Retailers who operate in Europe and the U.S. have sought to convince **Greencore** to enter the U.S. market to increase the percentage of sales dedicated to store brands. **Greencore** made a couple of acquisitions over the last year or two that gave them an entry into **Starbucks** (SBUX) and **7-Eleven** accounts. This is a company that may expect to continue its dominance on the U.K., while growing its business in the U.S.

**TWST: What about Methanex? Tell us about that company.**

**Mr. Horn:** **Methanex** (MEOH) is the largest producer of methanol in the world. Methanol is produced from natural gas, which is itself a pretty clean fuel. When you produce methanol from it, it's a much cleaner fuel. Methanol is a precursor to adhesives and other chemical products, and is also used as a fuel additive and substitute. China is one of the fastest-growing users of methanol as a fuel substitute, as the country seeks to enhance environmental conditions. Methanol prices have tended to trend closely with oil prices, which have stayed stubbornly high.

**Methanex** builds methanol facilities where the low-cost natural gas is in some way stranded or cannot be used in the local economy. They have done that in Canada, Chile, New Zealand, and they have plants in Egypt, Trinidad and Tobago. At these plants, methanol is converted to a liquid form that then can be shipped to regions that want cleaner sources of fuel. They arbitrage the difference between low-cost natural gas as a feedstock, and ultimately something that trades a lot closer to oil prices. Any company that can conduct physical arbitrage between a very low price product and a very high price product is likely to make money. The Fund has had a position in **Methanex** for years, aware of its business model, customer base, strong management team and healthy assets.

**TWST: Are there any international trends or developments that are impacting your investment ideas?**

**Mr. Horn:** In the 1970s, 1980s and 1990s, the global market was relatively static, with an investment universe of 10,000 to 15,000 companies from the developed world. In the mid-to-late 1990s, countries like China, Russia and India transformed their economies into market economies. As a result, we went from having about 15,000 companies in our universe to about 35,000 companies. That is extraordinary growth in the number of investable companies around the world. Interestingly, most of this growth occurred in companies with market capitalization of \$1 billion to \$2 billion or below.

Currently, we are finding a wealth of potentially undervalued companies in the U.S. Over the past 12 months to 18 months, we have been adding more U.S. investments to the portfolio. If you look at the next group of countries that represent good value, it is primarily Japan, China, Taiwan, Korea, Indonesia and India. We have dedicated more resources/travels to those countries to meet with the companies. As European economies continue to struggle, regional companies are experiencing restricted cash flows. We are keeping a keen eye on European markets, expecting opportunities to arise when markets recover.

**TWST: What has changed to make the U.S. more attractive?**

**Mr. Horn:** The U.S. economy is improving at a faster rate than its international counterparts. For instance, the U.S. banking sector suffered a credit crisis in the 2008-2009 period. U.S. banks took an aggressive stance to fix the problems, although recovery took nearly five years. We are starting to see some loan growth in the U.S. banking market, as the housing market recovers. It has been uneven, but it does appear to be taking hold in certain areas of the country, and that is helping a little bit at the margin.

Additionally, energy discoveries in oil and gas have kept energy prices a little bit lower here than in the rest of the world, and that has tipped the balance of competitiveness in favor of the U.S. in certain industries.

**TWST: Why should one invest in the Polaris Global Value Fund?**

**Mr. Horn:** According to modern portfolio theory, an optimal portfolio should include assets proportional in the market index. From my perspective, a market portfolio is not just the S&P 500 Index, it's the entire world, because that's when you find companies that have low correlation with one's home country. If there is an investor who wants to achieve diversification in equities, this Fund is a good opportunity. If an investor wants to achieve growth above inflation, investments in global companies may be an appropriate avenue. We have been steadfast in our belief that a global investment strategy can achieve strong risk-adjusted returns. The proof is in our long-term performance.

**TWST: Thank you. (LMR)**

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**Polaris Global Value Fund**  
**Important Information Concerning the Attached**  
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**Before investing you should carefully consider the Fund's investment objectives, risks, charges and expenses. This and other information is in the Fund's prospectus, a copy of which may be obtained by calling (888) 263-5594 or visiting the Fund's website at [www.polarisfunds.com](http://www.polarisfunds.com). Please read the prospectus carefully before you invest.**

The Fund invests in securities of foreign issuers, including issuers located in countries with emerging capital markets. Investments in such securities entail certain risks not associated with investments in domestic securities, such as volatility of currency exchange rates, and in some cases, political and economic instability and relatively illiquid markets. Option trading involves risk and is not suitable for all investors.

As of 9/30/2013, the Fund's top 10 equity holdings were: Greencore Group PLC (2.83%); Methanex Corp. (2.24%); Christian Dior SA (1.93%); Kone Oyj, Class B (1.80%); Symrise AG (1.75%); Ameris Bancorp (1.74%); Svenska Handelsbanken AB, Class A (1.71%); KDDI Corp. (1.70%); GTECH SpA (1.67%); Independent Bank Corp. (1.66%).

On June 1, 1998, a limited partnership managed by the adviser reorganized into the Fund. The predecessor limited partnership maintained an investment objective and investment policies that were, in all material respects, equivalent to those of the Fund. The Fund's performance for the periods before June 1, 1998 is that of the limited partnership and includes the expenses of the limited partnership. If the limited partnership's performance had been readjusted to reflect the second year expenses of the Fund, the Fund's performance for all the periods would have been lower. The limited partnership was not registered under the Investment Company Act of 1940 ("1940 Act") and was not subject to certain investment limitations, diversification requirements, and other restrictions imposed by the 1940 Act and the Internal Revenue Code, which, if applicable, may have adversely affected its performance.

*The views in this reprint were those of the Fund's portfolio manager as of the article's publication date and may not reflect his views on the date this reprint is first published or anytime thereafter. These views are intended to assist readers in understanding the Fund's investment methodology and do not constitute investment advice. This reprint should not be considered as an offer to sell or a solicitation of an offer to buy shares of any securities mentioned herein.*

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*The disclosure page must precede the August 2013 Wall Street Transcript article.*