

THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

Investing in High-Quality, World-Class Businesses



MICHAEL GOLUB, Founder and CEO of the Golub Group, began his career in the securities industry in 1967. His 38 years in all different investment climates give him a depth of experience and perspective possessed by few in the industry today. His principal responsibility at the Golub Group is to direct the firm's activities and to serve as its Senior Portfolio Manager. Mr. Golub is a graduate of the University of Colorado at Boulder with a Bachelor of Science degree in Finance. He takes great joy in applying his experience as a portfolio manager and advisor for the benefit of his firm's clients and in his management and leadership of the Golub Group team.



COLIN HIGGINS, President and Portfolio Manager/Research Analyst at the Golub Group, brings over 10 years of investment analysis, equity research and portfolio management experience to the firm. As President, he directs all business and investment activities for the firm. Prior to the formation of the Golub Group, he served as a research analyst and portfolio manager with regional investment firms Branch Cabell, & Co. and Hofer and Arnett, Inc., where he worked closely with Michael Golub for over eight years. Mr. Higgins graduated from Washington and Lee University, where he was an All-American lacrosse player. He is a level II CFA Candidate. He is also an active member of the Renaissance Executive Forums.



KURT HOEFER, CFA, Portfolio Manager/Research Analyst at the Golub Group, brings over 17 years of investment analysis, equity research and portfolio management experience to the firm. Prior to joining the firm, he founded and built Hofer Capital Management, LLC, to counsel families and individuals on investment and financial matters. Previously, he was an investment banker with Thomas Weisel Partners and Banc of America Securities and an institutional stock analyst at Salomon Brothers. He received his MBA from the UCLA-Anderson School of Management and his Bachelor of Arts degree in Economics from Stanford University. In addition, he holds the Chartered Financial Analyst designation.



TIMOTHY RICH, Portfolio Manager/Research Analyst at the Golub Group, joined the firm in 2005 after earning his MBA from the UCLA-Anderson School of Management. As a Portfolio Manager and Research Analyst, he performs company and industry research, fundamental analysis and portfolio management. Previously, he was a Vice President in the Capital Markets Intelligence practice at Thomson Financial. He began his career in Washington, DC, as an analyst and lobbyist for the wireless telecommunications industry. He also holds a Bachelor of Arts degree with honors in Public Policy Studies and History from Duke University and is a Level III CFA Candidate.

This article does not include all of the purchase recommendations made by Golub Group. A copy of all Golub Group recommendations beginning 11/1/01 is available upon request. It should not be assumed that future recommendations will be profitable or will equal the performance of the securities in this article.

(ZBP502) TWST: Would you tell us about the Golub Group and the respective responsibilities of your team members there?

Mr. Golub: The Golub Group is what has grown from the securities practice that I started in 1967, so the Golub Group represents almost 40 years of experience. I am the CEO and Chairman of the company, and my primary responsibility is to help with the strategic planning and the overall management of the company. Colin Higgins serves as President of the company, and in addition to Colin, we have a team that is responsible for research and portfolio management. That team includes me, Colin, Tim Rich, Kurt Hofer and Ayse Pehlivan. In addition to our Investment Management research team,

approach is based, first and foremost, on protecting our clients' capital by addressing risk.

We don't ever want to lose the trust of any client who honors us by employing us. The way we do this is by investing strictly in high-quality businesses — almost exclusively multi-billion dollar world-class franchises, typically those that pay above average dividends. Not only do we stick with the biggest and the best business franchises in the world, but we also spend most of our time and effort on valuation, because if you pay too much, even for a wonderful business, you operate with too much risk and you limit your potential to realize a gain.

Golub: When we put together the fact that the biggest, the best and the most powerful blue chip companies are now selling at the cheapest prices since the early 1980s, that they are financially stronger than they have been since the early 1960s, with the probability that we're in for many years of high competition in this world characterized by low inflation and low interest rates, we get very excited.

we have a wonderful Client Services team headed by Joe Martin. Joe's team consists of six people who are dedicated to giving the best possible personal service to our clients.

One of the things that makes the Golub Group so special is that we try our very best to be something unique and meaningful in the lives of our clients, not only in terms of the quality of the job we do in creating wealth for them, but in the way we treat our clients and the kind of close, caring and responsive service we give them.

Mr. Higgins: As a result of this, we have experienced some tremendous success since we last spoke with you in October 2004. We've grown our assets under management from \$250 million to its current level of \$400 million, and our client base has grown from 210 clients to about 400 today. We've also added significantly to the team, nearly doubling the headcount of our firm to 11.

TWST: Is there an overall investment philosophy for all the customized portfolios or do you have a different strategy for each?

Mr. Golub: We manage all money the same way. We have different asset allocations, but regardless of the allocation, our philosophy and discipline is based on the idea that the best way to create wealth is to manage risk first. This was a lesson that Benjamin Graham gave the world and, of course, he was Warren Buffett's teacher. We take Mr. Graham's philosophy to heart. Our

So we want to buy a world-class business at a 20% or better discount to what we calculate to be its present intrinsic value. Furthermore, when a business in our clients' portfolios becomes too popular on Wall Street and, as a consequence, becomes overvalued, we have a strict set of rules, which requires that we take capital out of those businesses and find another business of equal quality that is undervalued. Doing this positions our clients over the long run so that their money is always being managed in a way that minimizes risk.

What we've learned over the years is that the better the job you do at minimizing risk, the higher your return will be. People often misunderstand this; they look at the way we manage money and say, "Oh gee, you are conservative." They don't understand that the reason we manage money the way we do is because we know this is the best way to make money. We don't do it to be conservative — we do it because it's sensible, and it's the most dependable way of achieving our goal for our clients, which is to create a lot of wealth for them over time.

TWST: What is the process by which you identify stocks that qualify for your portfolio?

Mr. Hofer: We have an investment committee, which includes Michael, Colin, Tim, Ayse and me. We meet weekly to review and make changes to our existing portfolio and to discuss new ideas. To

produce these ideas, we screen a broad universe of common stocks to find the few that meet our criteria. We are looking for businesses that have inherent competitive advantages, a proven management team, and great financial attributes. These attributes include high return on equity, strong balance sheets, strong free cash flow and a history of consistent and predictable profitability. These companies are then added to our focus list, and we establish our estimate of their intrinsic value. We perform independent, fundamental research on the companies, and once

There are so many of us who are getting on in age. I don't speak for Colin, Kurt or Tim, but I am 64. We baby boomers need places to put our money to support us in our retirement that are acceptable from a risk point of view. If we can't get an acceptable return the easy way from money market funds, CDs and Treasury securities, there is simply no other place to go except to big, trustworthy, blue chip stocks that pay above average dividends. The prospects are phenomenally good for this class of securities.

Golub: We have different asset allocations, but regardless of the allocation, our philosophy and discipline is based on the idea that the best way to create wealth is to manage risk first. The way we do this is by investing strictly in high-quality businesses — almost exclusively multi-billion dollar world-class franchises, typically those that pay above average dividends.

we have confidence that we are buying an exceptional business at an appropriate discount to our estimate of intrinsic value, we'll place it on the buy list. These are the stocks that end up in our clients' portfolios.

The further advantage that we have and that we employ in our process is that we have the services of some terrific advisors who include Manny Goldman, Kurt Wulff and Ralph Block. These gentlemen have developed deep industry knowledge over decades of experience on Wall Street. They offer us a valuable perspective when we are evaluating the companies and the industries that they cover. These industries include consumer products, oil and gas, and real estate.

Lastly, we are always trying to achieve diversification for our clients. We typically have structured portfolios with between 30 and 35 securities that represent a broad range of sectors in the economy. So we take roughly a 3% position and avoid concentration.

TWST: What is the outlook for your type of investing in these quality companies for 2006?

Mr. Golub: I won't comment specifically on the outlook for 2006, because we try not to focus on the short run. We always focus on the outlook over the next three to five years. The one word that characterizes the world we find ourselves in today is competition. We know the probability is high that in the next 10 or 20 years, we are going to be in a competitive, slow growth world with low interest rates — far lower than most people imagine. A low interest rate world favors large, blue chip stocks that pay handsome dividends and regularly raise those dividends.

Now, interestingly, because there has been so much worry for the last year or so, part of which is the natural consequence of coming out of one of the major bear markets in history, these businesses are sitting at bargain prices today. If you look at an analysis of the way blue chip, world-leading businesses are priced today in the stock market, and look at the interest rate environment we are in and the earnings per share that these companies are generating, they are the cheapest they have been priced since the early 1980s. They are true bargains. Not only are they priced at bargain levels, but they are also flush with cash. Large corporations today have stronger balance sheets than they have carried over the past 20 years.

You have to go back to the early 1960s to find a time when our large corporations had so much cash on hand and they had reduced debt as much as they have in the last few years.

So when we put together the fact that the biggest, the best and the most powerful blue chip companies are now selling at the cheapest prices since the early 1980s, that they are financially stronger than they have been since the early 1960s, with the probability that we're in for many years of high competition in this world characterized by low inflation and low interest rates, we get very excited. This will be the best opportunity in our lifetime probably, at least for those of us who are my age, to enter the stock market and invest in these kinds of businesses. These are the kind of businesses that we exclusively invest in for our clients' portfolios.

TWST: Do you have benchmarks for these portfolios?

Mr. Higgins: We typically compare ourselves to the S&P 500, which is representative of the majority of our equity holdings. Please keep in mind that many of our portfolios have a fixed income component to them, and our performance has still been excellent. If we look at all of our fee-based discretionary accounts, in the aggregate, over the 10-year period ending December 31, 2005, our accounts have returned 11.11%, versus the S&P 500 return of 9.07%. Over the past five years, which includes the very difficult 2001-2002 time frame, we have returned a positive 5.35% per year, versus 0.55% for the S&P. We are very happy about our three-year numbers,

”As that segment noted, the tar sands up in Canada have 175 billion barrels of proven oil reserves.

This is second only to Saudi Arabia, but interestingly, this number should increase as the production technology improves, which we believe it will, given that there are world-class companies that manage the resource, including **Exxon** (XOM), **Petro-Canada** (PCZ) and **ConocoPhillips** (COP). Also, the oil that is ultimately produced from these sands is high-quality crude that often trades at a premium on the world markets. With the increasing political troubles and geopolitical concerns that we have across the world, Alberta is about as safe a location to do business as anywhere in the world.

Rich: When we initiated the position in Canadian Oil Sands, it was trading at about \$30 per unit, and it is currently trading at about \$130 per unit. So not only has the capital appreciation really been impressive, but the business itself has performed to the extent where the management has recently doubled the dividend payout.

which averaged 18.02% per year, versus the S&P's 14.39%. Last year, all of our accounts returned an average of 10.05%, versus the S&P's total return of 4.92%.

Mr. Golub: This illustrates my point that we manage not just to be conservative, but because it creates superior returns and is much less risky than the market. Over the last several years, in each of the quarters where the market was down on a quarterly basis, we were either not down, or we were down far less than the market. So we can show statistically that our discipline is significantly less risky than the market as a whole.

TWST: Do you have any examples of the success of your investment discipline that you can tell us about and the reasons why those picks were successful?

Mr. Rich: **Canadian Oil Sands** (COS_UN:TSX) is our top holding, and it really is a perfect example of how our clients benefit from the access that we have with some of the best analysts on Wall Street. As Kurt Hofer discussed, we have a relationship with Kurt Wulff of McDep Associates. Mr. Wulff is a 30-year Wall Street veteran in the oil and gas industry, and he brought **Canadian Oil Sands** to our attention back in 2003 when, for the most part, the Alberta tar sands were an undiscovered investment opportunity. This resource is now getting a lot more attention including a recent piece on “60 Min-

When we initiated the position in **Canadian Oil Sands**, it was trading at about \$30 per unit, and it is currently trading at about \$130 per unit. So not only has the capital appreciation really been impressive, but the business itself has performed to the extent where the management has recently doubled the dividend payout and has given an indication that the dividends will continue to increase over time as production ramps up and their technology improves.

Mr. Golub: This move from \$30 to \$130 has taken place in just under two years. Again, this is an example of our approach, which cares most about limiting risk, yet still offers the opportunity to make very large gains.

Mr. Higgins: I'll give you an example of a recent purchase that we feel emphasizes this approach, and it is **Cisco Systems** (CSCO). It is our belief that **Cisco** has become a victim of its own success and that Wall Street has placed too much emphasis on the company's growth expectations and not enough emphasis on **Cisco's** attractive valuation, market position and tremendous cash flow. While **Cisco** is clearly no longer a high growth company, it is still a growth company, and it's a cash-generating machine that produces nearly \$7 billion in annual free cash flow. We think it is going to benefit significantly from the record \$1.4 trillion in cash that is sitting on corporate balance sheets. **Cisco** obviously dominates the

enterprise market, and as companies put this capital to work, we feel that IT departments are going to be rewarded with increased spending budgets. What we often hear from IT managers in charge of spending and capital allocation is that, “You won’t get fired for buying **Cisco** products.”

As a result, we expect **Cisco** to grow its earnings 10% to 12% annually over the next five years. At its current valuation of just 14.5 times fiscal year 2007 earnings, which is a July fiscal year, it trades roughly at par with its growth rate and at a discount to the S&P 500. We think it’s a cheap stock.

Mr. Hoefler: Another company that we have recently purchased is **American International Group (AIG)**. We think **AIG** presents a situation where our approach can create some real opportunity for clients. The controversy around Hank Greenberg’s alleged improprieties received a lot of press and sent investors racing for the exits. Wall Street’s reporting, which offered, in our opinion, far more heat than light, masked the fact that the financial restatements that were required by regulators had very limited economic substance.

AIG remains a juggernaut, with incredible financial strength, significant competitive advantages and very attractive economics. But now the stock is on sale and it remains cheap today. Shares currently trade at less than 12 times the Street’s estimate for

company that is largely out of favor on Wall Street right now. But, given the economics of its business, this negative posture presents us with an opportunity. We believe **Wal-Mart**’s scale should give it a sustainable advantage for years to come. Its distribution network, inventory management systems and expense controls are unmatched, and the company is improving its merchandising, which should boost margins. Many investors feel for various reasons that there will be an imminent and pronounced slowdown in consumer spending. We simply don’t agree with that. For one, **Wal-Mart** has done an excellent job of attracting the higher income consumer, but has also been careful not to alienate its core customer in the process. Shares of **Wal-Mart** are trading at 15 times this coming year’s earnings, just under a market multiple, which we believe reflects very low expectations for a company like **Wal-Mart**. We believe the shares should ultimately trade quite a bit higher than where they are now.

TWST: What is the approximate turnover of your portfolios?

Mr. Higgins: We have relatively low turnover. On average, we turn the portfolio over around 20% to 25% per year, which implies that when we buy a stock, we intend on holding it for an average of four to five years, and hopefully longer.

Higgins: While Cisco is clearly no longer a high growth company, it is still a growth company, and it’s a cash-generating machine that produces nearly \$7 billion in annual free cash flow. We think it is going to benefit significantly from the record \$1.4 trillion in cash that is sitting on corporate balance sheets.

2006 and, in our opinion, **AIG** is worth far more than that. We also think that in the wake of Katrina and the other major natural catastrophes of 2005, the insurers with deep pockets like **AIG** will enjoy a very benign competitive environment for at least a year or two. The new CEO, Martin Sullivan, may not have the formidable presence of his predecessor, but he is an extremely competent manager, and one who has earned the trust of Wall Street and the regulators. So we are willing to invest our clients’ capital with him and with that company.

Mr. Rich: We also wanted to point out our recent addition to our position in **Wal-Mart (WMT)**. As we see it, **Wal-Mart** is a

TWST: What are some of your long-term holdings?

Mr. Higgins: Some of our long-term holdings also happen to be some of our top 10 holdings. We own businesses like **AMB Property (AMB)**, which is an industrial real estate investment trust headquartered here in San Francisco, **Citigroup (C)**, which is the world’s most profitable bank, **Generic Electric (GE)** and **McDonald’s (MCD)**. These are examples, again, of businesses that we bought when they were significantly out of favor with Wall Street. We bought them at a deep discount to what we thought they were worth, and we continue to own and buy them because we feel that they remain undervalued.

Mr. Golub: We will hold a business forever if it continues to trade at a reasonable relationship to its intrinsic value. If it goes up in price over time, roughly in proportion to the additional value created by the operations of its business each year, and Wall Street never gets carried away with it, we'll never sell it. We will just let wealth continue to be created by the company, which ultimately is always reflected in the price of the stock.

TWST: What is the sell process? What would trigger an exit from the portfolio?

Mr. Higgins: We will sell a business when there is a fundamental deterioration in the economics of the business. We will also sell a position if it exceeds our estimate of intrinsic value. We won't sell as it approaches intrinsic value, because, as Michael pointed out,

Hoefler: AIG remains a juggernaut, with incredible financial strength, significant competitive advantages, and very attractive economics. But now the stock is on sale, and it remains cheap today. Shares currently trade at less than 12 times the Street's estimate for 2006 and, in our opinion, AIG is worth far more than that.

these businesses are creating and increasing wealth for us as shareholders. We will also sell a business when it becomes too large a percentage of the portfolio. We get uncomfortable if a business becomes 6%, 7% or 8% of a portfolio. So we will take money off of the table and reallocate it.

TWST: What distinguishes the investment approach of Golub's growth from that of other firms? What are you bringing to the table that others might not?

Mr. Golub: I think it's the combination of the personal service that we give and the success we have had in creating wealth for our clients. Our service is characterized by integrity — truly caring for our clients and rigorously trying to give better, quicker and more accurate attention than is available elsewhere. If you were, for example, a Rockefeller and you were responsible for your family's money, you would go out and try to hire your own team of dedicated, well educated, experienced and committed human beings who would be involved in managing your family's money. That is what you get when you hire the Golub Group. And amazingly, you get the Golub Group for no more than the cost of a no-load mutual fund. Most people just don't realize that they can have what the Golub Group offers for that price.

TWST: Do you do all the research internally? Do you also use Wall Street research for your investments?

Mr. Higgins: We do the majority of our research internally, but as Kurt mentioned, we have a team of outside research analysts who are on our team. We review Wall Street research, but quite frankly, we use it more as an informational source, as opposed to something that will drive an investment decision. We've got a great team here, so most of our research is done in-house.

TWST: Do you still have a partnership with Charles Schwab or other firms?

Mr. Higgins: We do. Charles Schwab remains our primary custodian and we have had a phenomenal relationship with them over the last several years.

1-Year Daily Chart of AIG



Chart provided by www.BigCharts.com

Mr. Golub: We have 11 Charles Schwab offices south of San Francisco, from San Mateo to San Jose. The Schwab professionals bring us their clients who are looking for professional money management. So this is a very valuable relationship we have with Schwab, and we are extremely grateful to Schwab for this trust that they continue to place in us, and for all the wonderful people they continue to bring to us.

TWST: Is there anything else that we should touch on?

Mr. Higgins: One thing that we do when we're describing our approach is to use the analogy of an airline pilot. You do not want the pilot of your plane to be daring or heroic, but someone who is consistent, predictable and disciplined enough to get you to your destination. These are the same traits that you should be looking for in a money manager, and I think we do a great job of this.

Mr. Golub: I would just repeat that I sincerely believe that the current time represents one of the best opportunities most of us will have in our lifetimes to enter the stock market where you are willing to stick with the large, multinational, world-leading companies, which pay above average dividends, and where you are willing to be an investor, not a short-term trader. If you are willing to enter with the expectation that you will be an investor, and that means that you will let time do its work over at least three to five years, you will be handsomely rewarded.

TWST: Thank you.

Note: Opinions and recommendations are as of 2/6/06.

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