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# Value Investor INSIGHT

The Leading Authority on Value Investing

# Quite Contrary

*The consensus certainly isn't always wrong, but it is wrong often enough for discerning contrarians like Robert Kleinschmidt to take consistent advantage.*

**INVESTOR INSIGHT**

**Robert Kleinschmidt**
Tocqueville Asset Management

A self-described "authority-resistant troublemaker,"Robert Kleinschmidt found the perfect home in joining Tocqueville Asset Management in 1991. The firm's philosophical heritage drew on the writings of Alexis de Tocqueville, who critiqued the U.S. in *Democracy in America* as unique in how "little independence of mind" its citizens exhibited.

Expecting today's volatile trading environment to continue, he's finding upside in such areas as timber, specialty insurance, glass containers and real estate. See page 10



## Inside this Issue

**FEATURES**



**INVESTMENT HIGHLIGHTS**

# Investor Insight: Robert Kleinschmidt

**Robert Kleinschmidt and Peter Shawn of Tocqueville Asset Management explain why the most obvious contrarian idea often isn't the best one, their current take on gold, why we should get used to high market volatility, why they value a sense of humor, and why they see unrecognized upside in Weyerhaeuser, Aflac, Owens-Illinois and CBRE Group.**

**Tocqueville bills itself as a contrarian value investor. Isn't that redundant?**

**Robert Kleinschmidt:** It is, but it actually captures separate aspects of our discipline. We're first contrarian, meaning we only pursue ideas in which we understand the consensus and where that consensus is either negative or indifferent. Once we can credibly articulate the anti-consensus view, we approach valuation as a private owner would, meaning we determine what we would be willing to pay for the expected cash flow stream from the business. If the share price is at a sufficient discount to that value, we're interested.

It may go without saying, but it's important to remember as a contrarian investor that the consensus is often right. My colleague François Sicart likes to say, "Just because everyone says it's raining outside is no reason not to take an umbrella." But because we believe the consensus is priced into any given investment, going along with that is a very hard place from which to make money.

**How do you figure out what the consensus is?**

**Peter Shawn:** We think of it as a marriage of the stock price chart and our read on investor sentiment. We're obviously looking at stocks that are down significantly in price, often at the very low end of historical price or valuation ranges. To gauge investor sentiment we use Wall Street research as a contrarian indicator, so we're attracted to names where analyst ratings have turned broadly negative and sell ratings are in the majority. We can also pick up a lot about how any particular company is currently being perceived through our day-to-day research of talking to company management, competitors, suppliers, industry experts and other investors.

**RK:** To give an example of how we tend to think, our initial entry point into Exxon Mobil [XOM] a couple years ago was when the stock starting falling out of favor after it made a big bet on natural gas in buying XTO Energy. Our feeling was that the company had a distinguished record of capital allocation and there was a very strong likelihood that it knew more about the long-term prospects for natural gas than the analysts who were so negative on the deal. If our valuation work supports it, that's the kind of bet we will often make.

**Is the impetus for a given idea typically bad news?**

**PS:** Or at least news that's perceived to be bad. We bought Ford [F] stock last summer when it fell sharply due to the market sell-off and to specific concerns about how a flagging economy would impact near-term U.S. car sales. We liked that it remained profitable at a lousy point in the cycle, and our work on the demographics of the U.S. market indicated – based on things like cars per household, the average age of the existing automobile stock and historical scrappage rates – that new-car sales were likely to come back further and faster than what was built into the share prices of companies like Ford. When its shares sold off, that gave us an excellent opportunity to buy.

**RK:** Which points up the fact that our thesis often is based on the passage of time. What makes a negative story negative may just be that the next three to six months – the time space in which Wall Street analysts live – don't look so great. Again, we try to look at companies as a private investor would. To that investor a company's near-term bad news is only instructive if it informs the long-term outlook. If it doesn't, why should we care?

Robert Kleinschmidt

## Making Connections

In pursuing his original goal to be an economics professor, Robert Kleinschmidt was exposed to a variety of teaching venues. The most unusual: teaching economics to executive-MBA students of Adelphi University while they commuted in and out of New York City. "We had dedicated cars on commuter trains and I'd stand up front with a microphone and a blackboard," he says. "It was only somewhat more civilized than it sounds."

His first foray on Wall Street, at Irving Trust, wasn't much of an improvement. "I basically read Wall Street research and then recommended to portfolio managers what they should buy or sell," he says. "To my horror, they'd actually listen."

He found a more satisfying home at David J. Greene & Co., where he spent 13 years prior to joining Tocqueville in 1991. He credits his time there for instilling the importance of rigorous independent research and for making valuable contacts. Sitting to his right when he started was John Hathaway, now manager of the Tocqueville Gold Fund, and to his left was Dennis Delafield [*VII*, May 27, 2011], manager of the highly successful Delafield Fund, which Tocqueville acquired in 2009.

We try to use those situations as buying opportunities in stocks that we like.

**How do you try to distinguish between news that matters and news that doesn't?**

**PS:** We obviously don't always get it right. In 2008 we in certain cases let our contrarianism get the better of us and tried to catch falling knives – Fannie Mae and AIG come most painfully to mind – that in retrospect we clearly shouldn't have tried to catch.

One important lesson we've learned over time is to not focus our attention too narrowly when bad news is rampant. With financials, for example, we've sought out ways to benefit from the eventual healing of financial markets and potential increases in transactional activity without taking the leverage and business-model risk that comes along with, say, money-center banks. That's led us to companies like real estate broker CBRE Group [CBRE], title insurer Fidelity National Financial [FNF], and Lazard [LAZ], the boutique M&A advisory and asset management firm.

Another example: After the Gulf oil spill last year we spent time with litigation lawyers, including those involved in the cases being launched against companies like BP and Transocean. Our conclusion was that it was going to be too hard to jump in front of that train at that time in those companies, but that the collateral damage created buying opportunities in energy names we already knew well and owned, like Murphy Oil [MUR].

**We're curious how a utility company like NextEra [NEE] is a contrarian play.**

**PS:** Part of the story revolves around the company having one of the cleaner asset bases among its competitors. As the industry comes under a cloud due to potential environmental regulation and resulting rate pressures, we believe NextEra's generating assets in natural gas and alternatives might help them avoid some problems.

**RK:** This is the old Florida Power & Light and we also believe that despite the current economic hangover, baby boomers over time will continue to make their way to Florida in large numbers. We're intrigued by the utility industry, but you only want to be invested in areas where you're going to see ratebase growth – that's the only way these companies can really prosper.

**You make a distinction between your anti-consensus views in large versus small companies. Please explain.**

**RK:** It's much easier to find large-cap stocks that are out-of-favor – they're on the front page of *The Wall Street Journal* and the folks at CNBC are all over them. But in addition to looking for what others don't like, we also look for what is relatively neglected, which are almost always smaller to mid-cap names. In these cases our anti-consensus view is that the quality of the business and its prospects are just being missed by the market.

I'm quite interested in the natural gas industry, which I consider one area that could be a real positive for the U.S. economy if the expansion of domestic reserves ushers in an era of cheap energy. That doesn't mean natural gas prices are going to be high in the future, but we believe there's potential investment opportunity in companies involved both in extracting natural gas and in using it. One example is a smaller-cap name we own called Carbo Ceramics [CRR], which makes the ceramic proppants used in hydraulic fracturing methods that can access hard-to-extract gas and oil. Environmental concerns over what's commonly known as fracking may cause the stock to be volatile, but the company has a very strong secular tailwind that we don't believe the market adequately appreciates.

**ON MODELING:**

**It all comes down to the assumptions. If they're correct, a back-of-the-envelope calculation works perfectly well.**

**How do you think about valuation?**

**PS:** We use our own discounted cash flow model to calculate an intrinsic value estimate and then we want to be buying at a price at least 30% below that. We also look at how we believe that intrinsic value can grow and want to believe the value of the equity can double to our target price over the next three to five years.

**RK:** I'd add that while this is not true of everyone here, I'm still more back-of-the-envelope when it comes to valuation. To me it all comes down to the assumptions you're making. If they're correct, a back-of-the-envelope calculation works perfectly well. If they're not, sophisticated modeling isn't going to help.

**You don't let a position get to more than 4-5% of the portfolio. Why?**

**RK:** It's a function of having seen the stocks of too many good companies fall off a cliff as a result of something out of left field. One example I like to use is when Merck announced it was pulling Vioxx off the market in 2004. You went to bed with the stock at $45 and woke up with it 25% lower. I'll give up some of the upside you might get from an outsized position in order to be better protected from a risk you couldn't possibly foresee.

**What's behind your view that the market volatility and high correlation among stocks we've been seeing is something we might have to live with for awhile.**

**RK:** The social safety nets built up over time in the U.S., Western Europe and Japan were in large part built on a demographic conceit, with a great big generation over here paying into the system and a relatively small generation over there taking out of it. The problem is that the baby-boom generation is now turning 65 and the promises made to them in the form of retirement and health benefits will prove impossible to keep without significant alteration either to the promises or the resources paid into the system.

Compounding that demographic-endgame problem is that we're seeing a resolute inability on the part of elected officials and society at large to deal with it. My view is that until that gets resolved, macro factors back and forth will continue to have a disproportionate influence on markets, meaning stocks are likely to move sharply and more or less together. The overhang of that demographic endgame playing out is just too large.

I say that, but will then tell you we continue to pick stocks one at a time on their individual merits. We do, however, believe the likely scenario is that politicians try to inflate the problem away, which will have the effect of deflating the promises that have been made. So as a backdrop to the bottom-up work we do, we're particularly sensitive to how our companies will behave in an inflationary environment. That means putting more emphasis than ever on pricing flexibility, which goes hand in hand with competitive advantage and some kind of moat.

**Is that also behind your continued affinity for gold?**

**RK:** Gold is a logical alternative for those worried about governments' ability to manage their finances. If western political leaders adopt practices which result in devalued currencies, large budget deficits and rising inflation, gold to us represents a pretty decent store of value relative to currency alternatives.

When we started the Tocqueville Gold Fund in 1998, the nadir of a 20-year bear market in gold, it was clear that was a contrarian move. Though it doesn't change what I just said, I'll acknowledge that it's also very clear that our view on gold is not so contrarian now.

**Why is Newmont Mining [NEM] the largest gold-related position in the portfolios you manage?**

**RK:** A good proxy for gold-company expenses is the price of oil, so during this long period of rising gold prices you've seen the cost of production go up even more. So while gold miners have certainly been decent investments, the expense drag on earnings has held them back.

It's started to happen already, but if gold prices stay somewhere around where they are today, we believe miners like Newmont could continue to see the revenue/cost equation turn more in their favor, resulting in some real earnings gains. That would be an added kicker to the stock, separate from any impact on the change in the metal's price.

**Is part of your thesis for Weyerhaeuser [WY] that it's an inflation hedge?**

**PS:** The core of the thesis is that if you look at long-term normalized production levels from timberlands like theirs and capitalize that production at a reasonable valuation multiple, the stock is extremely cheap. So it's first a question of waiting out the cycle, but there is also considerable appeal in the fact that timber has shown to be an excellent inflation hedge over time.

**After simplifying its business, describe the company's focus today.**

**PS:** After unloading its paper, corrugated-packaging and transportation businesses, it now operates in four primary business segments: timberlands, wood products, cellulose fibers (used in products like dia-

## INVESTMENT SNAPSHOT

**Weyerhaeuser**
(NYSE: WY)

**Business:** U.S. real estate investment trust operating in four primary businesses: wood products, timberlands, cellulose fibers and real estate development.

**Share Information**
(@12/27/11):

| | |
|---|---|
| **Price** | **18.36** |
| 52-Week Range | 14.82 – 25.33 |
| Dividend Yield | 3.7% |
| Market Cap | $9.88 billion |

**Financials** (TTM):

| | |
|---|---|
| Revenue | $6.72 billion |
| Operating Profit Margin | 7.5% |
| Net Profit Margin | 6.5% |

**Valuation Metrics**
(@12/27/11):

| | WY | S&P 500 |
|---|---|---|
| Trailing P/E | 22.7 | 14.5 |
| Forward P/E Est. | 41.7 | 12.6 |

**Largest Institutional Owners**
(@9/30/11):

| Company | % Owned |
|---|---|
| Capital World Inv | 9.4% |
| T. Rowe Price | 6.0% |
| Paulson & Co | 4.4% |
| Vanguard Group | 3.8% |
| State Street | 3.5% |

**Short Interest** (as of 11/30/11):

| | |
|---|---|
| Shares Short/Float | 3.9% |

**WY PRICE HISTORY**


**THE BOTTOM LINE**

Given ongoing concerns about the U.S. housing sector, the market is sharply undervaluing the company's productive and profitable timberland assets, says Peter Shawn. Separately valuing the timber business from other operating subsidiaries, he believes the stock over the next 12 to 18 months should be worth around $25 per share.

Sources: Company reports, other publicly available information

pers) and real estate. The company is structured as a real estate investment trust and isn't required to pay federal income taxes on timber-harvesting earnings. The other businesses are taxable.

One result of the restructuring is that the company is now more dependent than ever on the health of the housing market, which obviously has been a drag. Most of the timberlands Weyerhaeuser owns go to making softwood lumber, the U.S. consumption of which is maybe 50% of what it was in the mid-2000s. Wood products is still the largest division – accounting for about 35% of gross sales – and is struggling to get to cash breakeven after a multi-year process of cost cutting. That business has been highly profitable in the past, but won't be again without some return to normalcy in the housing market.

We see other factors working to enhance the value of the company's timberlands. One is the expected increased demand for Pacific Coast timber to make up for significant log-harvest declines in British Columbia due to devastation by the mountain pine beetle. Another is the fact that the Pacific Northwest is the only U.S. tree-growing region that can profitably serve China, where log demand has consistently outstripped domestic supply.

**How are you valuing Weyerhaeuser shares, trading recently at $18.35?**

**PS:** The majority of the value is in its more than six million acres of REIT-qualified timberlands, which have proven quite productive and profitable. Capitalizing our $660 million estimate of 2013 normalized earnings from those timberlands at a cap rate of 5% results in a value of around $13.2 billion. That's just over $2,000 per acre, which is quite reasonable in relation to transactions that have occurred in the industry.

For the taxable subsidiaries, we're putting a 5x multiple on estimated 2013 EBITDA of $700 million, resulting in a value for those businesses of $3.5 billion. Subtracting net debt and adjusting for recent asset sales, we arrive then at a per share value over the next 12 to 18 months of between $24 and $25 per share.

The wildcard, of course, is the pace at which housing starts recover in the U.S. We haven't come close to assuming a return to mid-2000s levels, but the upside here won't come without some pickup from today's depressed levels.

**What's your anti-consensus take on specialty insurer Aflac [AFL]?**

**PS:** Aflac sells cancer, supplementary health and various life insurance products for which the benefits payments are largely capped. A cancer policy, for example, might pay a lump sum of $5,000 upon diagnosis and $150 per day in hospital expenses up to a pre-defined limit. Approximately 75% of the business is in Japan, where the company uses a third-party distribution model and enjoys retention rates of around 95% per year. This business model drives consistent margins – in the mid- to high-teens on an operating basis – and strong returns on equity of better than 25% over time. Another manifestation of the strength of the franchise: the dividend rate has increased for 29 straight years.

Two items in particular have been weighing on the stock. The first is an issue that has been around but has flared up recently, which is a still relatively large

### INVESTMENT SNAPSHOT

**Aflac**
(NYSE: AFL)

**Business:** Marketing and sale of supplemental health and life insurance products in Japan and the U.S.; sold by independent distributors and directly through employers.

**Share Information**
(@12/27/11):

| | |
|---|---|
| **Price** | **43.30** |
| 52-Week Range | 31.25 – 59.54 |
| Dividend Yield | 3.1% |
| Market Cap | $20.21 billion |

**Financials** (TTM):

| | |
|---|---|
| Revenue | $21.52 billion |
| Operating Profit Margin | 14.2% |
| Net Profit Margin | 8.6% |

**Valuation Metrics**
(@12/27/11):

| | AFL | S&P 500 |
|---|---|---|
| Trailing P/E | 11.0 | 14.5 |
| Forward P/E Est. | 6.5 | 12.6 |

**Largest Institutional Owners**
(@9/30/11):

| Company | % Owned |
|---|---|
| Vanguard Group | 4.4% |
| State Street | 4.2% |
| BlackRock | 2.5% |
| Wellington Mgmt | 1.8% |
| Wells Fargo | 1.6% |

**Short Interest** (as of 11/30/11):

| | |
|---|---|
| Shares Short/Float | 2.0% |

**AFL PRICE HISTORY**


**THE BOTTOM LINE**

Peter Shawn believes the market is overreacting to concerns about the company's exposure to the European debt crisis and to potential increases in Japanese cancer rates. Once those concerns recede, he expects the stock to again earn at least its historical 10x earnings multiple, which on his 2011 estimate would result in a $63 share price.

Sources: Company reports, other publicly available information

exposure to European financial-institution debt in the company's investment portfolio. While some investors see that and run the other way, we believe we have a fairly good handle on the scope of the exposure and what the ultimate risk might be. In our view, while there still may be some mark-to-market losses to be taken on the European exposure, they are more or less at a level today that can be offset by unrealized gains in the rest of the investment portfolio.

The other issue concerning the market is the impact the nuclear-power disaster earlier this year in Japan might have on the incidence of cancer in the country. While this is a very difficult issue to analyze, we generally believe that over the long term any increase in cancer-related insurance payments in the country due to radiation fallout will result in rising insurance rates to compensate.

**Are there secular arguments to make for the sale of supplemental insurance?**

**PS:** There's an argument to be made that as the breadth of what's covered by traditional health policies shrinks – particularly with underfunded federal plans – and the co-payments required increase, that will create growth opportunity for sellers of supplemental insurance like Aflac. We haven't quantified that impact or built it into our assumptions, but we do believe long-term it can be a significant positive.

**From today's price of $43.30, what upside do you see in the shares?**

**PS:** We expect the company to earn more than $6.30 per share this year. After a slower-growth 2012 as the investment portfolio is turned over into lower-yielding securities, we expect EPS to grow in the high single-digits annually over the medium term, from pricing power, cost efficiencies and share buybacks.

But even if we assume this year's earnings is a conservative estimate of earnings power and put on those earnings a far more reasonable 10x multiple – the stock's average P/E over the past ten years – we arrive at a share value 45% above today's price. If investors get past their current concerns, the multiple would justifiably be higher.

**Owens-Illinois [OI] investors have certainly had a bad 2011. Why do you expect that to be short-lived?**

**PS:** The company is the world's largest global glass-bottle manufacturer, which by the nature of the business – capital intensive, high shipping costs, advantages of scale – is prone to more or less oligopolistic competition. It is #1 or #2 in all of the 20 or so markets it's in, with particularly strong positions throughout South America. It also has good exposure generally to emerging markets, where bottled beverage consumption is on the rise.

There's been no shortage of bad news here. The weak economy has arguably caused some beer drinkers to trade down to cans from bottles. Venezuela announced a year ago it was taking over Owens-Illinois' plants in that country. Earnings in the U.S. have been hit by what turned out to be poor production planning to meet an unexpected increase in customer demand. Input costs have been rising faster than revenues, squeezing margins. The company's asbestos liability remains a significant Achilles heel.

### INVESTMENT SNAPSHOT

**Owens-Illinois**
(NYSE: OI)

**Business:** Largest global manufacturer of glass bottles, used to package a wide variety of beer, wine, spirits, non-alcoholic beverages, condiments and packaged foods.

**Share Information**
(@12/27/11):

| | |
|---|---|
| **Price** | **18.65** |
| 52-Week Range | 13.43 – 33.32 |
| Dividend Yield | 0.0% |
| Market Cap | $3.06 billion |

**Financials** (TTM):

| | |
|---|---|
| Revenue | $7.27 billion |
| Operating Profit Margin | 10.6% |
| Net Profit Margin | (-2.1%) |

**Valuation Metrics**
(@12/27/11):

| | OI | S&P 500 |
|---|---|---|
| Trailing P/E | n/a | 14.5 |
| Forward P/E Est. | 6.6 | 12.6 |

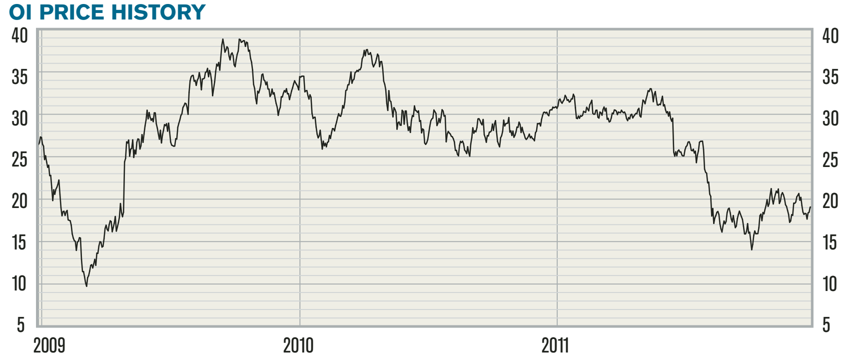
**Largest Institutional Owners**
(@9/30/11):

| Company | % Owned |
|---|---|
| Wellington Mgmt | 9.3% |
| Farallon Capital | 6.2% |
| Vanguard Group | 5.3% |
| Atlantic Inv Mgmt | 4.9% |
| Manning & Napier | 4.2% |

**Short Interest** (as of 11/30/11):

| | |
|---|---|
| Shares Short/Float | 2.5% |

**OI PRICE HISTORY**




**THE BOTTOM LINE**

The laundry list of bad news affecting the company's operations and share price are at varying stages of being worked out, says Peter Shawn. Assuming 2-3% annual revenue growth and a return to the 13% EBIT margins historically earned, his DCF model suggests a $29.25 intrinsic value for the company's stock, nearly 60% above today's price.

Sources: Company reports, other publicly available information

On top of all that, it certainly hasn't helped investor sentiment that 40% of annual revenues come from Europe.

**Your contrarian take on all that?**

**PS:** Over time the economy will improve enough for volumes to recover. The confiscation of the Venezuelan assets isn't positive, but not an insurmountable problem given that they accounted for less than 5% of the overall business. The operational problems in the U.S. are working themselves out, and were more a function of poor forecasting on the part of customers than an endemic flaw in Owens' processes. The margin squeeze will also recede, as contracts typically allow for cost increases to be passed through, but with a lag. It's hard to know what impact the European financial crisis will have on the actual economy, but the fact that the expenses and debt of the European operations are euro-denominated provides somewhat of a hedge against currency devaluation.

Then there's the asbestos liability, stemming from long-ago use of the material at its former Kaylo subsidiary. Asbestos-related payments reduced the company's free cash flow by approximately $170 million in 2011. Here we believe we have a good understanding of how this plays out, having spent an enormous amount of time to understand asbestos litigation and claims history, stemming from our experience as long-term shareholders of W.R. Grace. The reality is that as time passes most of the people who were truly hurt by asbestos have already been compensated and/or have died. While still large, the claims liability declined 7% this year, a rate that will accelerate.

**With the shares at $18.65, how are you looking at valuation?**

**PS:** One thing we've done is to look at the business without the asbestos liability, to get a sense of how the operating business is being valued. Absent asbestos payments, Owens generated $400 to $500 million in annual free cash flow over the last few years, translating at today's market cap to a free cash flow yield on the shares of 13-14%. That's extremely high for this type of business and illustrates the valuation upside as the market over time refocuses on the underlying business.

Our DCF model assumes 2-3% annual revenue increases, that EBIT margins recover to just over 13% – the typical level prior to this year – and that asbestos payments decline at 7% per year. With a weighted average cost of capital of just over 9%, that results in an estimated intrinsic value today of $29.25. If the earnings power gets to the $5 per share we believe is possible longer term, there's a good deal of upside beyond that.

**ON HUMOR:**

**In a deadly serious business, having a sense of the absurd eases tension and helps put things in perspective.**

**Describe what attracted you to real estate brokerage CBRE [CBG].**

**PS:** This was a case where we started looking at commercial REITs in the aftermath of the financial crisis, but more or less passed on the sector because of refinancing risk and lack of transparency with respect to asset values. What did interest us, however, was commercial real estate brokerage, where transactions had fallen off a cliff and we couldn't imagine things getting much worse. On top of that you had an enormous amount of commercial mortgage-backed securities [CMBS] on financial institutions' books that were underwater and would eventually need to be refinanced and/or sold off. We expected that process to result in a significant number of real estate transactions, from which the brokers would directly benefit.

The industry has consolidated in recent years, so that CBRE, Jones Lang LaSalle [JLL] and Cushman & Wakefield are the primary global players in the high end of the market, where most of the activity is today. What attracted us to CBRE was that it has diversified its revenue base so that some 50% of its business today is in recurring-revenue property and asset management, while the rest comes from leasing and sales brokerage. That gives it flexibility in riding out tough times, while still being levered to when the most cyclical part of the business – brokering sales – improves.

**The boom in transactions you expected as CMBS portfolios were restructured hasn't happened yet. Why?**

**PS:** By and large the banks holding this paper chose to "extend and pretend," by pushing out debt maturities rather than risk the chaos of seeing too much distressed real estate dumped on the market at such an economically precarious time. The problems haven't gone away, however, and this mountain of CMBS still has to be restructured. Prices will be lower than they were, but that process is still going to drive transaction volume, which is a great thing for CBRE.

**How is the rest of the business doing?**

**PS:** Property-management revenues have been growing 10%+ per year, as enterprises continue to increasingly outsource that function. The investment management business has held up well despite sharp declines in property values, and should see strong growth as commercial real estate prices bottom and as full-year results from the recent purchase of ING's comparable business flow through.

**At $15.30, how cheap are the shares?**

**PS:** The stock trades at about 8x estimated 2011 EBITDA on an enterprise value basis, at a time when commercial sales transactions are still 50% off their peak and when operating margins are pressured by the company maintaining much of its broker staff in anticipation of a recovery.

Without heroic assumptions about transaction volumes and margin improvement, we believe earnings over the next few years can get to a mid-cycle level of around $2 per share. With a reasonable mid-teens earnings multiple at that point in the cycle, the share price would be closer to $30.

**Have you ridden this position up and down since 2009?**

**PS:** We've done better than that, having sold some of our position as the stock went to $30 earlier this year and buying it back as the shares fell sharply with everything else over the summer. The long-term thesis is still very much intact.

**What's something you've sold recently and why?**

**PS:** Our long-term orientation doesn't mean we don't cycle out of names when the thesis is slow to develop and we have better opportunity elsewhere. We bought Briggs & Stratton [BGG], for example, betting on the delayed replacement cycle for its lawn and garden equipment finally picking up and on it possibly taking market share from Japanese competitors hurt by the earthquake and tsunami. As time went by we became less confident in the cycle turning in a timely fashion – when money's tight, it's not a big decision to keep the lawnmower for another year – and felt its business as a supplier to branded equipment manufacturers didn't have much pricing power. With better alternatives elsewhere, we moved on.

**You have shown more patience with Microsoft [MSFT]. Why?**

**PS:** The bear case is so well known, that Microsoft is a lumbering giant whose business is under threat because of the "cloud" and the rise of mobile computing. Our view is that Microsoft is actually well-positioned in the cloud with its Windows Azure platform and with its hosted software products that are tightly integrated with the desktop. We also generally believe desktop computers will dominate the enterprise environment for longer than the market seems to think and will have plenty of room for growth in developing markets where people won't be going straight to iPads.

With the stock [at a recent $26] trading at less than 8x earnings ex-cash and at a trailing free cash flow yield of 11%, few people seem focused on how well the company has executed in recent years or on what could actually go right. Windows 8, out next year, could establish itself as highly relevant in today's world of tablets, app stores and touch interfaces. The Windows mobile operating system could be a solid competitor to Apple's iOS and Google's Android. The shares are priced for almost everything to go wrong and our view is that that's unlikely to be the case.

**You've spoken about the virtues of having fun at work. What's up with that?**

**RK:** Humor is an important part of Tocqueville's culture. That's not to say we're cutting up all the time or that we're even that funny, but in a deadly serious business like ours if you can't find humor in what you're doing, it's going to kill you. Having a sense of the absurd eases tension and puts things in perspective. Without that, people burn out or tend in their desperation to roll the dice. That's the last thing we want to do. VII

## INVESTMENT SNAPSHOT

**CBRE Group**
(NYSE: CBG)

**Business:** Provider of commercial real estate services worldwide, including transaction brokerage, property and facility management and investment management.

**Share Information**
(@12/27/11):

| | |
|---|---|
| **Price** | **15.30** |
| 52-Week Range | 12.30 – 29.88 |
| Dividend Yield | 0.0% |
| Market Cap | $4.88 billion |

**Financials** (TTM):

| | |
|---|---|
| Revenue | $5.79 billion |
| Operating Profit Margin | 9.5% |
| Net Profit Margin | 4.4% |

**Valuation Metrics**
(@12/27/11):

| | CBG | S&P 500 |
|---|---|---|
| Trailing P/E | 19.4 | 14.5 |
| Forward P/E Est. | 11.9 | 12.6 |

**Largest Institutional Owners**
(@9/30/11):

| Company | % Owned |
|---|---|
| Goldman Sachs | 8.2% |
| Blum Capital | 7.4% |
| T. Rowe Price | 6.1% |
| Fidelity Mgmt & Research | 5.3% |
| Vanguard Group | 5.3% |

**Short Interest** (as of 11/30/11):

| | |
|---|---|
| Shares Short/Float | 4.0% |

**CBG PRICE HISTORY**


**THE BOTTOM LINE**

The company has successfully diversified its revenue base, says Peter Shawn, but is still strongly levered to what he considers an inevitable rebound in depressed commercial real estate sales transactions. At 15x his $2 per share estimate of mid-cycle earnings, he believes the stock price can double within the next few years.

Sources: Company reports, other publicly available information

*This reprint is furnished for general information purposes in order to provide some of the thought processes and techniques that Tocqueville Asset Management uses to make investment decisions for its Multi-Cap Equity strategy, including the Tocqueville Fund (the "Fund"). It is provided for illustrative purposes only. This material is not intended to be a formal research report and should not be construed as an offer or recommendation to buy or sell any security, nor should information contained herein be relied upon as investment advice. Opinions and information provided are as of the date indicated.*

*Mutual fund investing involves risk. Principal loss is possible. The Tocqueville Fund's investment objectives, risks, charges and expenses should be considered carefully before investing. The Fund's prospectus contains this and other important information about the Fund. The prospectus may be obtained by calling 1-800-697-3863 or visiting www.tocqueville.com/mutual-funds. Read it carefully before investing.*

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*Fund holdings are subject to change at any time. As of December 31, 2011, the Fund's top ten holdings were:*

| ***Top Ten Holdings (as of 12/31/2011)*** | ***% of assets*** |
|---|---|
| *Pfizer, Inc.* | *4.39%* |
| *General Electric Co.* | *3.63%* |
| *Microsoft Corp.* | *3.51%* |
| *Exxon Mobil Corp.* | *3.44%* |
| *NextEra Energy, Inc.* | *3.29%* |
| *Newmont Mining Corp.* | *3.24%* |
| *E. I. du Pont de Nemours & Co.* | *3.09%* |
| *Mastercard, Inc.* | *3.02%* |
| *Johnson & Johnson* | *2.66%* |
| *Intel Corp.* | *2.62%* |

*The Fund discloses its top ten holdings on the Tocqueville website no earlier than 15 calendar days after the end of each month. References to other mutual funds should not be interpreted as an offer of those securities.*

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