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THE WALL STREET TRANSCRIPT

Connecting Market Leaders with Investors

Managing Concentrated Portfolios of the Highest-Quality Businesses

DAMON FICKLIN is a Portfolio Manager and Analyst, and a Senior Partner at Polen Capital Management. Mr. Ficklin joined Polen Capital in 2003 and is the Co-Portfolio Manager of Polen Capital's flagship Large Cap Growth Portfolio. Prior to joining Polen Capital, Mr. Ficklin was an equity analyst at Morningstar and a tax consultant at Price Waterhouse. Mr. Ficklin graduated magna cum laude from the University of South Florida with a B.S. in accounting, earned an M.S. in accounting from Appalachian State University and earned an MBA with high honors from The University of Chicago Booth School of Business.

SECTOR — GENERAL INVESTING

TWST: Could you just start by telling us a bit about your firm and your role at the firm?

Mr. Ficklin: Polen Capital was founded by David Polen about 36 years ago, and our flagship product, which was launched 26 years ago, is our Large Cap Growth product. While we are excited to be launching our second product — a Global Growth product — in 2015, our flagship product has been our sole focus for the past 26 years. I'm a Portfolio Manager and a Senior Partner at the firm, and have been with Polen Capital for more than 11 years now. Dan Davidowitz, our CIO, and I co-manage our flagship product. Dan has been with the firm more than nine years, and Stan Moss, our CEO, has been with Polen Capital for more than 11 years.

TWST: What types of clients do you tend to serve, and what are your total assets under management?

Mr. Ficklin: Our total assets under management are almost $5.5 billion now, and we serve a diversified client base. Roughly half of our business is with institutional investors, including large state retirement systems, endowments, corporations and other like clients. The other half of our clients are high net worth clients obtained through intermediaries, such as registered investment advisers, trust companies, private banks and the wire houses.

TWST: What is your investment strategy as it pertains to your Large Cap Growth Fund?

Mr. Ficklin: Our investment strategy is fairly unique. I think we have several things that distinguish us from most of our peers. One, we manage a very concentrated portfolio. We typically own about 20 positions at any point in time, and we think this is a big advantage. Owning 5%, 6%, 7%-plus of your portfolio in a business that does very well over time really helps drive performance.

And by concentrating our investments in only the highest-quality businesses, we have been able to reduce risk. Our portfolio has been less volatile than the indices and the vast majority of our peers, and has gone down much less during down markets. We also have a very long-term focus. Our average holding period is almost five years, and in the 26 years that we've been managing our flagship product, we've only owned a little more than 100 companies in total.

Our strategy is not to generate returns through activity. We are not trying to buy low and sell high, and create returns through our activity. Rather, our construct is to own 20 great businesses for the next five-plus years and let the businesses drive the returns. The underlying earnings and free cash flow growth of the portfolio is what we believe drives long-term share prices and what has driven our returns over time. We have compounded at about 14% since inception 26 years ago, and our best estimate is that 12%-plus of that comes from underlying earnings per share, free cash flow growth. We had a small benefit from dividends and a little bit of multiple expansion, but it's really about the underlying earnings growth over the long term.

TWST: Can you walk us through your stock-selection process? How do you identify ideas and vet them for inclusion in your funds?

Mr. Ficklin: In terms of our process, we start with a pretty broad universe. We will consider any company that has a market cap of $4 billion to $5 billion or greater. We first do some quantitative screens, and what we're really looking for is franchises with sustainable, competitive advantages. The first cut is just looking for companies with return on equity of 20% or greater, typically high and improving margins, very little debt or leverage, and then better-than-average earnings and free cash flow growth. We are looking for at least double-digit earnings per share growth over time. So those quantitative screens knock a lot of companies out of the universe, and as you know, the 20% return on equity hurdle is a couple standard deviations above normal.

So that whittles down the universe considerably to, say, a few hundred companies. From there we eliminate or weed out companies that are highly cyclical. Some energy, materials or telecom companies might meet our return on equity and growth hurdles at a positive point in the cycle, but if you look at a full business cycle or five-plus-year horizon, most highly cyclical businesses do not sustainably deliver the type of results that we desire. So those companies typically fall out of our process.

We also exclude anything that we don't believe has a sustainable competitive advantage. Some companies meet our criteria and are doing very well in the market, but it's because of a fad or a fashion or short-term favorable opportunity that they're seizing upon. But when we think three to five years out, we don't have a great degree of confidence that they'll continue to deliver that kind of growth and have the advantages to protect their franchise. So those companies kind of fall out of the process as well.

Once we get through that part of the process, we usually have 100 to 150 companies left, and that's really where the investment team spends the vast majority of our time, just trying to understand the businesses. Really our goal is to identify what we think are among the 20 best businesses in the world. Once we get comfortable with the idea that we have identified a quality franchise with sustainable competitive advantages and stronger than average growth over the long term, we try to determine if it is fairly valued and whether we should own it. And then, of course, when we do take a position in a company, we continue to follow it as intently as when we were digging in to understand the business in the first place.

Highlights

Damon Ficklin discusses Polen Capital Management's Large Cap Growth Portfolio and his investment philosophy. Mr. Ficklin maintains a concentrated portfolio and a long-term focus, generally holding about 20 positions at a time with an average holding period of five years. He looks to own the highest-quality companies at reasonable values. In addition, rather than generate returns through activity, Mr. Ficklin allows the businesses to drive returns. Due to the investment strategy, Mr. Ficklin feels patient investors with a long-term perspective are best suited for the fund.

Companies discussed: Allergan (AGN); Valeant Pharmaceuticals International (VRX); Actavis plc (ACT); Google (GOOG); Visa (V) and MasterCard Incorporated (MA).

What we liked about **Allergan** was its heavy investment in R&D and aggressive investment in the business, in sales and marketing, in infrastructure and development, beyond the R&D. They had spent aggressively for many years and really continued to do so through the five years that we owned the company. They have a well-balanced franchise.

BOTOX is their largest franchise. Most everyone is familiar with the aesthetic indication of BOTOX, which is administered to reduce wrinkles, but BOTOX is also a very big therapeutic franchise treating a lot of serious conditions, including chronic daily headache, overactive bladder and many others. Almost half of **Allergan's** business is in eye care pharmaceuticals — treatments for glaucoma, dry eye and other various areas in ophthalmology — and it's a very stable franchise with leading products that were strong growers in the U.S. and on a global basis.

And then, rounding out the rest of the business are other aesthetics and medical devices, like dermal fillers, breast implants and the like. So **Allergan** has grown aggressively for a very long time and management continued to invest heavily into the business to maintain strong growth for the long term. That has been the consistent story right up to this year.

As you know, early in the year, **Valeant Pharmaceuticals** (VRX) made a hostile buyout attempt on **Allergan**, which really put the company into play. The premium offered was roughly 60% of the unaffected share price of **Allergan** early in the year, but what **Allergan** management did in response to that offer was pretty impressive. They really unearthed a tremendous amount of earnings power and value on an organic basis, and have grown earnings about 50% over the course of the past year. So despite **Valeant's** buyout offer kind of pushing the share price higher, we felt that **Allergan** continued to be reasonably valued as a standalone business.

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TWST: Can you give us three stocks that are among your top holdings, and explain to us what attracted you to each name and what you like about it?

Mr. Ficklin: Our largest holding during this calendar year was **Allergan** (AGN). We just recently trimmed it back, but it was our largest weighting for most of the year and was roughly 10% of our portfolio prior to our recent trim. **Allergan** has had a lot of excitement around it during 2014.

We originally purchased **Allergan** in late-2008. As you'll recall, back at that time it was a very difficult environment, and everything was on sale. Some of the better, stronger growth franchises became more attractively valued at that point in time. So we were able to acquire **Allergan** for less than 15 times earnings back then, despite the fact that we thought it was a great growth franchise.

So we remained very big shareholders of the company. It was our largest position, as I mentioned, and we were able to do that because we felt comfortable with its value on a standalone basis, even if that deal fell apart. You, of course, know the rest of the story now. **Actavis** (ACT) came in and offered an even higher value about a month or so ago. Shortly after that, we cut our position in half because we feel that **Allergan** as a standalone company was pretty fairly valued at that point.

We still have a 5% position because we do believe it's still reasonably valued. We also believe that as we approach the deal close in the middle of next year, **Actavis'** shares are likely to float a little higher, which will in turn pull the deal price higher, and there is still a spread on the deal that will close as well. So we think **Allergan** is still reasonably valued on a standalone basis and that we can still earn a decent return between now and the deal close, but it no longer warrants a supersized position in our portfolio.

TWST: Are there a couple more you want to talk about?

Mr. Ficklin: Google (GOOG) is another one of our largest positions. We've owned **Google** since 2008 as well. The original investment in **Google** was because of its dominance in search advertising and really the nascency of the business at that time. I believe time spent online was something like 7%, 8% of total media time back in 2008 and search advertising dollars still only accounted for maybe 3%, 4% of total advertising spending. We felt that time spent online would increase meaningfully over time, and that ad dollars would follow that time spent, if you will, and that clearly has happened.

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1-Year Daily Chart of Allergan

Chart provided by www.BigCharts.com

Today, I'd say, including mobile, more than 35% of time is spent online, and it's still climbing. Excluding mobile, online ad spending has largely closed the gap with time spent online, but time spent and ad revenues are still growing nicely, and we think there is tremendous growth potential in mobile. **Google** has continued to grow advertising revenues in totality at a nearly 20% rate. Even if you assume that that growth slows a little bit, say a midteens-type growth over the next five years, we think there's still meaningful growth, and we think there's tremendous value in **Google's** shares. Today, **Google** is trading for about 17 times forward earnings, and if you back out $60 billion of cash on their balance sheet, you're looking at a market multiple essentially for a company that clearly is a much-better-than-average company, with incredible positioning.

Mobile is exploding at this point, as you know. It's been happening for a couple of years now, and **Google** is benefiting from it because **Google's** share in mobile is even higher than its share in desktop search, which is impressive when you start with a 70%-plus share in desktop search. So they are benefiting from the volume growth and the explosion of mobile usage, and mobile monetization is still far below desktop search monetization as well. **Google** does not disclose their mobile revenues or mobile search revenues specifically, but by our best estimates, even if we're generous with where they are already at with mobile search, on a per-user basis, mobile monetization is probably not even a third of that of the core desktop search business.

So we think there's a tremendous opportunity for **Google** to increase monetization in mobile search over the long term, and that should drive tremendous growth in the coming years as well. So great franchise, clearly dominant, unbelievable set of assets and incredible positioning, and the core business, we believe, can still drive much better than average growth, despite the fact that **Google** is trading for what is essentially a market multiple.

On top of that, you have a lot of options. YouTube is becoming a very valuable and very big platform. Even things that seem more far-fetched, like the driverless car, are moving closer and closer to reality over time. That's a big wild-card opportunity. The Google Play Store is growing in importance.

It's unbelievable what they've done with the Android platform. They essentially have close to 70% share of mobile devices through Android. Now, that's skewed a little bit toward the lower end of the smartphone market, but that's the part of the market that's growing. So incredible platform, incredible positioning, and we think there's a tremendous opportunity for some of the other businesses that aren't quite as recognized yet as well.

1-Year Daily Chart of Google

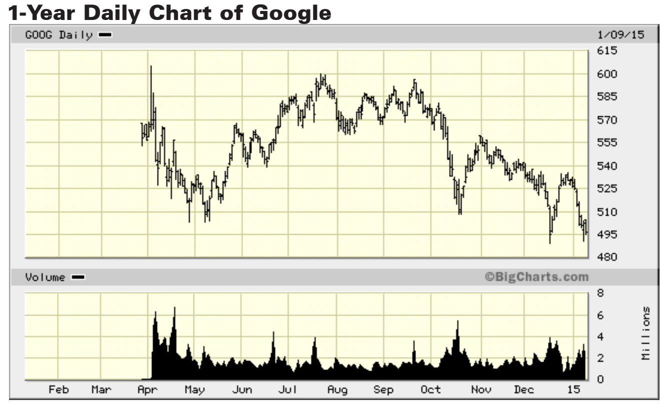

Chart provided by www.BigCharts.com

TWST: And a third one?

Mr. Ficklin: We own both **Visa** (V) and **MasterCard** (MA). I'll highlight **Visa**, but my comments will really largely apply to both. If you combine the weightings of the two companies, they make up one of our largest positions as well. We have about a 7%, almost 7.5% position in **Visa** and a 2% position in **MasterCard**. We had purchased **Visa** first, and we were looking to add further to the position, and we decided we would add **MasterCard** and think of them as a combined position.

These are incredible franchises that are producing tremendous growth, and you're not paying a very aggressive multiple or price to own them. Both companies are growing earnings per share at about a 20% pace and trading for 23 or 24 times. We think that's a pretty attractive valuation for that type of secular growth.

If you think about what drives both of these businesses, underneath it is the personal consumption expenditures growth globally, and that's a pretty nice number. It's low- to mid-single-digit growth on a global basis. But on top of that kind of underlying growth that's happening, you have this huge secular shift from cash to other forms of payment: credit, debit, digital, mobile payments. And **Visa** and **MasterCard** are the beneficiaries of that.

If you look at, here in the U.S., cash penetration levels have been reduced down to about 50% or less. We're further along that curve in the

U.S., in terms of moving payments over to digital payments. If you look everywhere else in the world though, cash penetration rates are still exceptionally high; in Europe, north of 70% and Latin America close to 90%. And that's true in other emerging geographies as well. So there's tremendous opportunity for the secular story to continue to play out on a global basis, and **Visa** and **MasterCard**, they are just mopping it up.

If you listen to both of these companies talk, they're talking about the war on cash. Essentially, what they're saying is that they need to both focus on converting all the cash payments to credit, debit and electronic forms of payments that can drive growth. That is exactly what's happening. **Visa** and **MasterCard** are not out there trying to undercut each other on price. They're trying to go out and convert those cash transactions.

We think there's strong secular growth. Both companies are growing revenues at a low-double-digit pace. They have tremendous scale, which provides inherent leverage opportunities, and then, of course, they produce a ton of free cash flow, which can then be used to buy back shares to create additional earnings leverage. So we think 20%-type earnings per share growth is very doable for a long period of time, and again, the valuations are very reasonable.

TWST: What do you see as the biggest risks for growth investors at the moment, and how do you seek to minimize those risks for your clients?

Mr. Ficklin: The chief risk to a growth investor is not paying a little too much for a great growth company but paying too much for what seems like a good growth company but isn't. After a strong run in the market driven by a lot of stimulus for a very long period of time, I think that risk is probably very real today. If you step back, after the great financial crisis in late-2008, the Federal Reserve has essentially instituted a near-0% interest rate policy since then, for an unprecedented period of time. And we are not just talking about the U.S. A version of this has happened pretty much everywhere on a global basis.

So the last six years or so have been a very unique environment driven by a tremendous amount of stimulus. The near-0% interest rates have driven more risk taking and have likely made many companies appear stronger than would be the case in a more normal environment. Add to that the fact that share prices have risen faster than underlying earnings growth for many companies during the past few years. How do you protect yourself from that or deal with that? From our perspective, it's only owning great franchises that remain reasonably valued.

We have a very fundamentally driven investment strategy, so our portfolio has had a harder time keeping up, broadly speaking, during the past three to five years, given the backdrop that I have described. But we have managed to roughly keep pace, and if you look at the performance of our portfolio, the compounding of our portfolio returns has been completely supported by underlying fundamental earnings growth. That has not been the case for the indices. So we feel good that we own only the highest-quality businesses. We feel good that the share prices of the businesses we own have not detached from their underlying fundamentals.

Where we stand today, the businesses that we own still remain reasonably valued, and on a portfolio basis, we believe our portfolio is going to continue to grow earnings in the midteens. We're paying roughly 19 to 20 times forward earnings, which is a couple multiple points higher than the respective indices but with much better growth, much higher-quality companies, with values fully supported by earnings growth. So that's really the way we protect, and the way we always operate is to only own the highest-quality franchises at reasonable values.

TWST: Now that you've told us about your approach and what you do, what kinds of investors do you think would be most interested in Polen and your Large Cap Growth Fund?

Mr. Ficklin: We think we work well for a wide variety of investors, but I would say the best investor for us is a patient investor with a long-term perspective. That probably best fits in the bucket of institutional investor or a high net worth individual that really understands business and the value of being invested in a great business for the long term — not so much investors that have a short-term orientation or are looking for you to beat the indices every quarter and every year, year in, year out. We think an investor that understands what we are trying to do, which is to own great businesses and let the businesses drive returns over time, and that has a patient, long-term perspective is going to do very well with us.

TWST: Thank you. (MES)

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