Note: Items in brackets [ ] are meant to be clarifying statements but are not part of the actual audio recording of the webcast. Please also see Important Disclosures at the end of this transcript and at the end of the webcast presentation.

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(00:00:00)

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It is now my pleasure to turn today’s program over to Kristina Surkova. Kristina, the floor is yours.

Kristina: Thank you. Good afternoon and thank you for joining us today. We would like to welcome you to FPA US Value's Second Half 2019 Webcast. My name is Kristina Surkova, and I support the Fund on the client service side. The audio, transcript, and visual replay of today's webcast will be made available on our website FPA.com.

In short order, you will be hearing from Gregory Nathan, the portfolio manager of the Fund. As a reminder, Greg took on the management of this fund on September 1, 2015.

As part of today's agenda, we will cover fund highlights, market commentary, performance and portfolio activity, and then open it up to question and answers. At this time, it is my pleasure to hand the call over to Gregory Nathan. Greg.

(00:01:51)

Gregory: [Please reference slide 2 and 3] Thank you for that introduction. I am proud to report that the Fund had a very successful year in 2019. It returned 34.16%, or 35.75% before fees and expenses. This compares favorably to the S&P 500's 31.49% total return. The Fund outperformed the index by 4.26% before fees and expenses, and by 2.67% after all fees and expenses. Additionally, within Morningstar's Large Blend category,

the Fund finished in the top sixth percentile out of 1387 funds. It outperformed the category average by 5.27%.[1]

To take a step back and in order to understand how we generated this outperformance, one should appreciate the journey we've been on these past four years. When we took over the Fund at the end of 2015, we came in with the mindset of putting together a portfolio solely through the lens of a senior analyst. For the first two years, the Fund was highly concentrated, averaging just 27 disclosed investments. We attempted to run the same playbook that worked for us for so long as a successful analyst; essentially mean reversion.

As an analyst, I focused on out-of-favor industries and companies, and believed that by focusing on average to above-average businesses, over time these companies' results would not be as bad as feared, leading to multiple expansion coupled with decent earnings growth. However, what we saw time and time again over the past few years was that these previously average to above-average businesses were more often than not continuing to miss expectations. As fundamentals eroded, so too did their stock prices. After two frustrating years in 2016 and 2017, we knew

[1] Source: Morningstar. https://www.morningstar.com/funds/xnas/fppfx/quote. Morningstar Percentile Rankings are based on the total return percentile rank within each Morningstar Category and do not account for a fund's sales charge (if applicable). Rankings will not be provided for periods less than one year. The highest (or most favorable) percentile rank is 1 and the lowest (or least favorable) percentile rank is 100. Historical percentile ranks are based on a snapshot of the funds as they were at the time of the calculation. Percentile ranks within categories are most useful in those groups that have a large number of funds. For small universes, funds will be ranked at the highest percentage possible. For instance, if there are only two specialty-utility funds with 10-year average total returns, Morningstar will assign a percentile rank of 1 to the top-performing fund, and the second fund will earn a percentile rank of 51 (indicating the fund underperformed 50% of the sample). FPA U.S. Value Fund, Inc. 5-year percentile ranking = 97. **Past performance is no guarantee, nor is it indicative, of future results.**

we had to be more diversified, since we were seeing many historically predictable businesses become increasingly unpredictable.

However, as we underperformed again in 2018, what we also understood was that not only was the vast majority of global growth over the past few years technology-related, but technology was also responsible for disrupting a lot of historically high-quality businesses we had an affinity for. We lacked a market-weighting of technology over the first three years because the multiples of so many of these companies were above average. Growing up as value investors, we learned to be distrustful of companies that had spectacular growth because most companies ultimately become ordinary due to basic economic principles, such as market saturation, competition, etc. As growth slows, multiples contract; thus we rarely invested in above-average multiple stocks.

However, what we finally realized was that we are in the early innings of several major growth trends tied to the internet, digital, and mobile revolutions. So towards the end of 2018, we took the opportunity to become more invested in technology companies and other companies we believe will be beneficiaries of technology for many years to come. Thus, for the first time since managing the Fund, we have finally had a market-weighting of information technology entering 2019, which partly explains why we were able to outperform meaningfully last year.

Our sector exposures heading into 2020 remain fairly similar to 2019. As a result, we believe the Fund is well-positioned to capitalize on

many of the key investor themes we will discuss later on in the presentation.

[Please reference slide 3] With all that being said, we believe the backdrop for investing in mid-to-large growing companies continues to be relatively attractive to other asset classes, but less so on an absolute basis, given how much valuations have risen over the past year. The 10-year US Treasury rate, at less than two percent, remains near all-time historical lows. The unemployment rate is low. The US economy is still growing slowly. However, if the US and China can resolve its trade issues, US economic growth could improve.

The S&P 500 finished 2019 trading at approximately 18.3 times forward earnings estimates, up from 15.1 times a year ago. What you have seen is the index increase by about 30% while EPS is up approximately 10% year over year, and therefore around two-thirds of the index's return is from multiple expansion. A large part of this increase in valuation can be attributed to longer-term interest rates declining. The 10-year US Treasury yield declined from approximately 2.7% at the end of 2018 to approximately 1.9% at the end of 2019, and now sits close to 1.6%.

One of the biggest drivers of return differentials in the market is the valuation spreads we are continuing to see widen out between companies the market perceives as having structural, above-average long-term growth, i.e. current winners, versus companies who terminal values are

more in question, often due to technological disruption, i.e. potential losers. Therefore, it is imperative to avoid investing in potential losers whose fundamentals are eroding, and instead stick to high-quality companies we believe have sustainable competitive positions that should result in above-average organic growth over the long term.

Regarding today's agenda for the call—first we're going to walk through the Fund highlights. Then we'll touch on our investment philosophy and process. Following that, we will discuss some key investment themes which are helping shape the portfolio. After that, we will give an update on the Fund's performance and portfolio activity. Lastly, we will go through Q&A. If you are unable to participate in the live webcast and/or do not get your questions answered, please feel free to reach out to Kristina Surkova in client service to arrange a call with me.

[Please reference slide 4] Regarding the Fund highlights—the primary objective of the US Value Fund is growth of capital over the long term. Our goal is to outperform the S&P 500 over full market cycles, which we define as an approximate seven-year period.

[Please reference slide 5] Here is a summary of my professional background with approximately 18 years of professional industry experience. My interests are well-aligned with fellow shareholders. I have further increased my investment in the Fund in 2019 and have already begun to do so in 2020. I hope this gives you a sense of my confidence in the Fund.

[Please reference slide 6] Now we would like to walk you through our investment philosophy. The most important thing in investing is to avoid permanent capital impairment. Permanent capital impairment can result from: investing in a business whose profitability is structurally declining; paying too high of a multiple for a company; investing in a company with too much financial leverage that can't make it through a tough business cycle without having to restructure. Thus, we focus on finding quality companies in healthy, growing industries, at attractive valuations, with low financial leverage. We want the portfolio to have an appropriate level of diversification by number of investments and industry exposure.

We define quality as companies that have strong and enduring competitive positions—growing businesses within growing industries. A growing industry is key because without it, there will typically be poor earnings growth and investment returns. Lastly, we want our companies to have high returns on capital and a robust free cash flow generation.

We prefer companies with good management, which we define as those who make the right operational and capital allocation decisions to put the company in the best position to achieve sustainable, above-average revenue and earnings growth over the long run. However, one of the reasons good businesses are offered at attractive prices is because of poor management. Therefore, we will consider such companies, provided

there is not a structural impediment to replacing management, and there is a large enough discount to our estimate of intrinsic value.

Bottom line, the quality of the business followed by valuation are the most important investment criteria. A current example of this would be Boeing, which traded at a below-market multiple, based on normalized earnings power assuming the 737 MAX regains certification to fly again. Last month, Boeing announced that former CEO, Dennis Muilenburg, resigned, and the nearly appointed chairman, David Calhoun, would take over as CEO and president.

As is widely known, under Muilenburg's tenure, two 737 MAXes crashed and killed hundreds of people due to the faulty MCAS system. Muilenburg's approach to work with regulators, customers, and all other stakeholders was a failure. As the timeline for getting the 737 MAX back into service was delayed several times, for many more months than expected, and communicated to the public by Muilenburg, the board decided a change in leadership was necessary to restore confidence in the company. At the end of the day, Boeing operates largely as a duopoly, competing against Airbus, another portfolio company and approximately three times larger investment.

Global demand for air travel continues to grow at a mid-single-digit rate. We believe both companies have pricing power, as demand for their most popular planes outstrips their annual production supply. Additionally, the barriers to entry into this industry have likely never been higher.

[Please reference slide 7] Let me walk you through the key parameters as to how the portfolio is constructed. The Fund's multi-cap strategy affords us the ability to invest wherever the best opportunities arise. At least 80% of the portfolio will be invested in US companies. As of December 31, 2019, the portfolio is 88.1% invested in US companies. At the same time, we have the ability to make opportunistic foreign investments, which stands at 8.7% of the portfolio.

Appropriate diversification—individual positions will not exceed five percent of total assets at the time of purchase.

Generally fully invested—the reason for this is the portfolio is made up of what we believe are undervalued, high-quality companies that should compound in value over time, therefore cash will usually not exceed 10% of the portfolio. Cash and equivalents made up 3.2% of the Fund as of December 31.

[Please reference slide 8] The foundation of our portfolio construction process stems from our investment objective of seeking long-term growth of capital. At the same time, we have a goal of generating investment returns that exceed the S&P 500 over full market cycles, all while minimizing the risk of permanent capital impairment.

We are of the view that the world is dynamic, with change taking place seemingly faster than ever before. Therefore it is critical to have a diversified portfolio to mitigate unforeseen risks, namely disruption to business models. While we consider investing in all industries at any

given time, we will not invest in all industries if that means taking undue risk and/or negatively impacting long-term returns.

We deconstruct the S&P 500 whereby, in the famous words of Bing Crosby, we are trying to accentuate the positive, eliminate the negative, latch onto the affirmative, and don't mess with Mister In-between.

We start by eliminating or underweighting unfavorable sectors due to relative inferior quality, lack of above-average growth, and/or unattractive valuation. From the remaining sectors that meet our criteria, sector weights are based on long-term industry fundamentals, coupled with the relative attractiveness of various companies within those sectors, centered on business model sustainability, normalized long-term earnings growth, and valuation.

We consider select investments outside the US and/or S&P 500 that offer compelling risk-adjusted returns. The goal is to be as close to fully invested as possible, provided we can find the requisite high-quality companies at attractive valuations.

Cash is a byproduct of what is left over from having investments in the industries and companies we view attractive, at the relative position weightings we deem appropriate based on sector risks, coupled with our estimate of the companies' prospective returns over the long term.

It is important to note that the portfolio construction process changed in the fourth quarter of 2017. The current portfolio construction process is very different from the manner in which we constructed the US

Value Portfolio over the first nine quarters of operation. For the past nine quarters, we have operated using the portfolio construction process I just described.

Over the first nine quarters, the portfolio was constructed in a much more concentrated, purely bottoms-up manner by sector and company compared to the now more diversified manner which begins with a top-down view of the overall market and sectors within it. Specifically, we averaged 27 disclosed investments over the first nine quarters, compared to an average of 62 disclosed investments over the past nine quarters.

What is interesting to note is that many investors have the view that in order to outperform the market over time, you have to run with a concentrated portfolio. However, the numbers do not support that. For example, from 2016 through 2019, the S&P 500’s cumulative total return over those four years was 71.5%. The top 50 contributing stocks to the index’s performance had a median return of approximately 109%. The next biggest 50 contributing stocks to the index’s performance had a median return of approximately 131%. Additionally, the next largest 50 contributors had a median return of nearly 95%. The top 150 contributing stocks had a median return of approximately 112%. The top 250 contributing stocks had a median return of 102%. In theory, one could put together a highly diversified portfolio of 250 equally weighted stocks over the past four years and generated over 30% of alpha. However, the bottom 250 contributing stocks had a median return of 28%. The negative

alpha of the median bottom 250 was negative 43.5%. The bottom 100 stocks had a median return of negative 9.5%. This tells you it is just as important, if not more important, to avoid big losers compared to picking winners.

[Please reference slide 9] Another key point to make is that the top contributing stocks over these four years were in a variety of sectors, including information technology, communication services, consumer discretionary, healthcare, financials, and industrials. Moreover, the same is true about the greatest detractors. Therefore the main takeaway to me is that one can certainly outperform, and outperform meaningfully, with a diversified portfolio.

However, what it comes down to is a good batting average, i.e. having more of those stocks in your portfolio that are in the top 250 and as few as possible in the bottom 250.

Another crucial reason I concluded the portfolio needed more diversification was many companies which I have followed for years that seemed to have predictable business models were all of a sudden becoming unpredictable. Management would regularly give excuses and try to convince investors that these were short-term issues. Too often, I would listen and remain invested in these companies, only to be disappointed again.

However, what is continuing to happen is increasingly faster disruption across more industries. To better manage this risk, we needed

to operate with a sense of less conviction and more paranoia. As public investors, we can only know so much. Placing too much faith in management, who are human and are thus often wrong, is not the answer.

We have determined what is part of our solution is to have more positions and less conviction in our investment theses. Thus, when a company disappoints us, we are mentally free to sell and move on. I am only married to my wife, and certainly not to any company. Stocks are just stocks, and serve investors only one purpose: to generate good returns. When they cease to do that, they do not need to be in our portfolio. That is the beauty of the public markets. It gives us liquidity to freely buy and sell.

Moreover, we take advantage of that while trying to be tax-efficient. In 2019, over 90% of the Fund's return was unrealized. And since we generally believe our portfolio companies can continue to grow at above-average rates for many years to come, we typically have no need to sell other than to meet investor redemptions.

Another significant point I want to make is that over the first three years, the portfolio was significantly underweight in information technology due to above-average valuations relative to the index. Not only is this the largest sector in the S&P 500 but it is one of the highest-quality due to its consistent above-average revenue and earnings growth. This was a major reason for the Fund's underperformance over those first three years.

Now, the Fund has a more in-line weighting of information technology compared to the index, and we expect this will continue to benefit the Fund's performance going forward. This is certainly one of the core reasons for our meaningful outperformance in 2019 continuing into this January.

[Please reference slide 10] Staying on this topic for another moment, I think it is important to explain in more detail why we have such large exposure to information technology and communications services. These are the two largest sector exposures that are both tech-related and combined, make up approximately 45% of our disclosed investments.

It is imperative to emphasize, we are value investors who seek to find high-quality companies that have the ability to organically grow revenue and earnings at above-average rates over the long run. In addition, we invest in these companies at what we believe are compelling valuations.

Over my 13-year professional career as an analyst from 2002 to 2015, I was able to generate investment ideas with market-beating returns by fishing for stocks trading at below-market multiples. That is because if you look at the chart on the left, global earnings across a multitude of sectors grew at similar rates as the tech sector did from 1985 to 2012. Therefore, if you fished in a global pond across industries and market caps and you focused on buying quality stocks trading at below-market multiples, you had good odds of outperforming the market over time.

However, beginning in 2012, this all changed. Technology earnings growth began to outpace non-tech earnings, and over the past few years, tech earnings growth has exploded while non-tech earnings have flatlined. Many companies that historically exhibited growth no longer were.

When I transitioned from a successful analyst to a portfolio manager, my portfolio construction process was simply to create a concentrated portfolio of my best ideas. Just as I was an analyst, I would be completely bottoms-up because historically, there was not any sector that exhibited significantly better growth than others did for sustained periods. And I would buy stocks at below-market multiples because you were generally not getting more value paying up for the higher-multiple stocks, as most could not sustain their above-average growth rates. This is why value or low-multiple stocks generally performed as well as higher-multiple growth stocks from 2003 through 2015, which you can see on the graph on the right.

Keep in mind, very few things last forever. Economic principles remain true even for tech companies, which are at risk of disruption by competitors over time. Just look at IBM and Oracle for example, which continue to lose market share and grow slower than its end markets. Thus, we are not advocating putting all of our eggs in one basket.

There are high-quality companies in non-tech sectors which we think have the ability to grow at above-average rates for several years. However, they are rare, and those that do exist often have expensive

valuations. As a result, about half of the disclosed portfolio is in non-tech sectors. Therefore, in total, about half of our disclosed investment portfolio is in tech-related sectors and half is in non-tech. Given where valuations are currently across industries, we are comfortable with this composition. However, we would probably be inclined to increase our exposure to tech on any market weakness because that is where most of the growth is, and that is where we believe most of it will likely be for the next number of years. Should that change, expect the portfolio's composition to as well. We want to invest wherever the growth is, at compelling valuations. We are mentally flexible and our portfolio will flex accordingly.

[Please reference slide 11] I want to take some time how the portfolio is positioned to benefit from of the largest forces driving global economic growth, namely the internet, digital, and mobile revolutions. We believe that approximately two-thirds of the portfolio should benefit from these multi-year sector trends including digital advertising, cloud computing, e-commerce, digital payments, mobile operating systems, digital media, digital banking, software-as-a-service, digital and mobile gaming, online travel booking, digital health, and autonomous vehicle software. As you can see, many of our portfolio companies are positioned to benefit from multiple secular growth trends.

Now we're going to go into a bit of a deep dive into some of these major secular growth trends, so you can better understand why the portfolio is positioned the way it is to benefit from them.

[Please reference slide 12] First, let's look at global digitalization. How people across the globe, communicate, access, and store information will continue to influence how the world conducts business. As you can see from the graph on the left, the number of global smartphones is expected to grow to 4.5 billion in 2022, or nearly 20% over four years. Equipment connected to the internet, including smartphones, smart watches, digital media devices like Roku, and digital assistants like Alexa, will nearly double to over 40 billion devices from 2018 to 2022, and the amount of global data we are consuming will nearly triple over this four-year period. Part of this will be made possible by 5G technology, which is expected to account for nearly half of all smartphone shipments by 2024.

[Please reference slide 13] This growth in global digitalization is impacting how companies manage its business across many different areas. Microsoft, which is one of the Fund's largest investments, operates across various verticals. From the 12 biggest technological drivers we showed you on slide ten, Microsoft is set to benefit from four of them. The company is in pole position to be among the winners, since it can provide customers with more integrated human solutions. For example, Microsoft is able to operate similar enterprise communication to called Teams, which competes against Slack. While fans of Slack might view the offering as superior to Teams, Teams is integrated within the Office 365 offering.

Currently, Microsoft has over 20 million daily active Teams users. The company said it saw more than a 50% increase in usage of its Teams

platform since July, when it announced that it had 13 million daily active users.

[Please reference slide 14] As more people around the world are habitually connected to the internet, the growth of e-commerce should continue for many years. E-commerce sales are expected to nearly double over the next four years to 2023. [Please reference slide 15] As global e-commerce grows, how the economic pie is split amongst the various supply chain participants will continue to evolve. This is one of the most important charts to understand, and really helps to put into context why we are so bullish on so many of our portfolio companies.

Companies that have the strongest direct relationships and brands providing the best overall customer experience are positioned to capture more of the pie over time. If you look at the chart, you can see that in this example of a $100 retail sale of running shoes, half of the economics is going to the brick and mortar retailers. Thus companies like Nike and Adidas are well-positioned to sell more of its products direct to consumer, or DTC, and capture a higher margin of those sales. Nike and Adidas have stated that online DTC sales are approximately two to three times more profitable than brick and mortar retail sales, and looking at this chart helps explain why.

[Please reference slide 16] As e-commerce grows, certain distribution expenses, store rent, and associated overhead, as well as traditional advertising expenses, are reduced, freeing up more spending

on effective customer acquisition. Therefore, performance marketing is not purely advertising. Rather, it is money spent effecting on acquiring customers, customer transactions. Essentially, it is the economic rent of e-commerce.

In an e-commerce-centric model, a sizable chunk of that $50 going to the retailer is freed up, and can be reallocated to find additional customers more cost-effectively. Evercore ISI estimates that in a $100 traditional physical retail sale that moves online, advertising spending for that sale increases by 125%. In our view, the market opportunity for the likes of Alphabet's Google properties and Facebook's social media platforms have often been defined too narrowly as advertising within a traditional framework based on a physical retail-centric model.

[Please reference slide 17] Given that people are spending an increasing amount of time using search and social media, companies are increasingly advertising more on Alphabet's and Facebook's platforms to reach targeted consumers cost-effectively. If you think about it, if a DTC sale for Nike and Adidas is two to three times more profitable than a retail sale of the same product, companies like Nike and Adidas are willing to spend an increasingly greater amount of money on digital advertising in order to get more customers to buy products directly through its app or website.

For example, on Adidas's first quarter 2019 conference call, it stated Instagram Checkout was the second biggest driver of its DTC

business, growing 40% year over year in the quarter. With over 1 billion active monthly users on Instagram, it is logical that Adidas should be willing to spend an increasing amount of money on that platform to drive those much higher margin DTC sales. Thus it stands to reason social media platforms like Facebook and Instagram will likely see its pricing rise nicely over time.

[Please reference slide 18] The king of e-commerce, Amazon.com, continues to grow its Prime customer base, which now stands at over 50% of US households. This increasing scale provides it with unique opportunities and competitive advantages.

[Please reference slide 19] Amazon is keeping its foot on the accelerator, so to speak, by offering one-day shipping on an increasing number of goods sold and fulfilled by Amazon. Again, referring back to the chart where half of the pie is going to the physical retailer in a traditional retail sale—because Amazon does not have a lot of those traditional physical retail expenses, it is able to reallocate resources toward one-day shipping, and utilizing the gross profit dollars from a growing number of sales to help pay for that costly expense.

Over the past few years, Amazon has been growing its data and fulfillment square footage at a 25% CAGR. Much of this growth is in smaller, local centers within urban areas where there is population density. This allows it to increase its total adjustable market by being able

to sell consumers various goods and services that are more time sensitive, such as groceries, meals, and health care.

[Please reference slide 20] As Amazon delivers an increasingly greater percentage of a growing e-commerce market, its cost per item delivered should decline over time, and result in an even greater competitive advantage. In my opinion, this is a virtuous cycle that will continue to distance Amazon from the competition. Amazon is willing to take the upfront hit to expenses by offering one-day shipping on a growing number of items.

As it continues to take more market share, its gross profit dollars from selling these items allow it to reinvest more into its delivery network. Companies like UPS and FedEx, which do not capture a piece of the gross profit dollars from sales of products, do not have those dollars to help invest in their offering in order to provide faster, cheaper delivery. So what you will likely see over time is Amazon continue to take share, utilize more of its own delivery network, and cause retailers and delivery companies to suffer the impact from fixed-costing leverage.

[Please reference slide 21] Additionally, both UPS and FedEx are at risk of being hurt by another major trend. As the world moves more towards an e-commerce-centric model, the market mix of shipments moves away from higher-density and higher-margin B2B volume toward lower-density and lower-margin B2C volume. Luckily for Amazon, it has a

growing market share of products and the associated gross profit dollars to offset the impact, but UPS and FedEx do not.

I also think it's important to remind shareholders that the Fund used to be invested in UPS and FedEx, because we thought they would be natural beneficiaries of a growing e-commerce market. But the work we're showing you here demonstrates how the world is a dynamic, changing place, moving at a seemingly faster place. This also demonstrates our mental flexibility to change our view. Our investment thesis on both companies was wrong, and thankfully we were able to exit with a profitable investment in UPS and manageable loss in FedEx.

[Please reference slide 22] Another key investment theme for the Fund is its investments in the cloud and enterprise software industry. Amazon Web Services, or AWS, data suggests that over 90% of compute spend is still on-premises, and less than five percent is in the cloud, which translates into a large market opportunity. [Please reference slide 23] Oppenheimer estimates that enterprises have only migrated only about 20% of workload to the cloud in the US, and worldwide enterprise cloud adoption is even less, which helps explain why this industry stands to have robust growth for many years to come.

[Please reference slide 24] Globally, companies are in the early innings of cloud adoption across their enterprises. New use cases from the likes of the internet of things, artificial intelligence, and autonomous vehicles may help fuel industry growth. How quickly enterprises are willing

to embrace the cloud and all of its benefits may help determine who the winners are within their respective industries.

[Please reference slide 25] One of the Fund's largest investments is Amazon.com. Currently, Amazon's most profitable business is AWS, which is the largest and leading cloud computing platform. AWS began to both aid developers and improve efficiency of the company's own infrastructure, mainly compute power, storage, and database. As you can see in this chart, AWS is the industry leader with approximately three times the market share as the next closest competitor, Microsoft Azure.

[Please reference slide 26] AWS has helped grow the market by adding an increasing number of features and services each year. Additionally, it has continued to reduce pricing on these features and services in order to spur greater adoption of them. [Please reference slide 27] Despite continued price reductions over the years by AWS to help grow adoption of more features and services, its revenue and operating margin have grown nicely. Operating profit is expected to more than double of the next four years, while it continues its practice of annual price cuts.

[Please reference slide 28] While AWS is the clear leader, both Azure and Google's cloud platform, or GCP, have been gaining share over the past few years. Many of AWS's customers are cloud-native companies, such as Netflix, and were thus early adopters of the cloud. Many of Azure's and GCP's customers have a longer corporate history.

They are increasingly making the transition to the cloud and are often more interested in a hybrid solution, which Azure has embraced as part of its core offering.

[Please reference slide 29] Even though Azure and GCP are expected to gain further market share over the coming year, AWS is still expected to grow the most revenue. Companies such as Wal-Mart, Home Depot, Snap, Colgate, Disney, eBay, and Spotify that compete with Amazon's various businesses, all else equal, would prefer not to give its cloud business to AWS, which would help grow its cash flow that could be further invested into its other business that compete against the aforementioned competitors. We think it is a possible in the future that Amazon might spin off AWS as a separate public company to better position the business to compete with Azure and GCP for the long-term, which could also increase Amazon shareholder value.

[Please reference slide 30] Another key investment theme is software-as-a-service, or SaaS. As more software companies, such as Adobe, increasingly transition their business to a subscription-based model, profitability can increase dramatically. Looking at the graphs below, as the subscription revenue mixes from the high 70s to nearly 90% over the past three years, revenue has more than doubled while EBITDA margins have expanded by over 300 basis points, in large parts due to such high gross margins in the high 80s.

In a subscription-based model for software, the incremental costs to add a new subscriber onto the platform are relatively small. The winning software companies are those that have unique products and services, which continually reinvest in their offerings to provide more value to its customers. The cloud-based subscription model allows companies like Adobe to constantly upgrade its offerings through continual software updates. As customers see the increased value in this, more switch over to a subscription. And as that subscriber base grows, so does Adobe's ability to increase pricing over time. Adobe has leading market share in some of the most dynamic secular growth areas in software, including creative design, dynamic media, and marketing automation. With a move of its customers towards subscription nearly complete, its greatest long-term opportunities are capturing new users and garnering higher revenue per user through their adoption of more features and services.

[Please reference slide 31] Regarding the portfolio's holdings, we'd like to point out a few highlights.

We believe our companies operate within secularly growing industries. The aforementioned key investment themes are helping fuel above-average growth for many of the Fund's portfolio companies. In our view, the Fund's holdings have strong competitive positions due to advantages stemming from having large scale in a low-cost structure, superior products and services, and/or high-quality brands. A majority of these companies are among the top players in their respective industries.

[Please reference slide 32] I think it's worth understanding US Value's portfolio characteristics compared to the S&P 500. While US Value is reasonably diversified, with 64 investments, 59 of which are disclosed, we are more concentrated than the index 500. US Value has 33.9% of the disclosed portfolio in its top five holdings compared to 17.5% for the S&P 500. Our top 10 disclosed investments make up 50% of the portfolio compared to 22.7% for the index.

Another key differentiator is over nine percent of our portfolio is invested in foreign equities while the index has none. Today you can see that the median and weighted average market cap of our portfolio is considerably higher than the index. That is because some of the largest companies in the index, such as Apple, Microsoft, Alphabet, Amazon, and Facebook, are some of our largest positions. This also contributes a great deal to our portfolio's approximate 40% disclosed overlap with the index.

We believe these are some of the highest-quality businesses we have ever come across, and they share an ability to grow revenue and earnings at above-average rates for many years to come.

In terms of comparative quality, there are a few metrics you can look at to give you a sense but don't tell the entire story. The companies in our portfolio over the past two years have grown revenue and earnings faster than the index by approximately four and five percent respectively. At the same time, based on consensus estimates, over the next couple of years, expectations are for revenue and EPS to grow at a faster rate of

five percent. This is a material difference when compounded over many years.

Our companies also have about three percent higher return on equity and carry less financial leverage, meaning that on an unlevered basis, return on capital for our portfolio of companies is even higher.

As you can see, the 12-month forward P/E of our portfolio compared to the S&P 500 is at a bit of a premium. We would argue that this valuation premium is well-deserved, if not too small.

(00:17:53)

Probably one of the greatest differentiators for US Value is our willingness to eschew entire sectors of the market. To that point, US Value currently does not have any disclosed investments in 5 of the 11 sectors that, combined, make up 21.5% of the index. These sectors are materials, consumer staples, energy, real estate, and utilities. This goes back to the earlier point of trying to minimize exposure to inferior parts of the market where we do not see good value.

Many people would say value investing does not work anymore, however, to say that one must first define value. We define value as the relationship of business quality relative to the price you pay for it. Business quality means the ability to generate sustainable above-average earnings growth over the long term. We have found trying to find value by leading our quest looking for low-multiple stocks is not a good approach.

Instead, we focus on finding quality businesses within growing industries. From there, we estimate its long-term earnings growth—earnings power—and as a result, we can have a view as to what an appropriate multiple is for the company and therefore what a good purchase price is.

We believe we will be able to continue finding value by taking a long-term view and hopefully being right on those views much more than we are wrong. Moreover, by using this approach to construct a reasonably diversified portfolio, we are confident this will generate long-term growth of capital, with returns exceeding the S&P 500 over full market cycles.

[Please reference slide 33] Now here is the portfolio sector breakdown as of December 31. There are disclosed investments in 6 of the 11 sectors in the S&P 500. Combined, these six sectors, which make up 79.7% of the index, account for 94.7% of US Value's disclosed portfolio. Relative to the S&P 500, the portfolio is overweight in information technology, communications services, consumer discretionary and industrials, and has a generally in-line weighting in and financials. The Fund is underweight healthcare.

[Please reference slide 34] Lastly, and most importantly, let's discuss US Value's performance. We explained the manner in which we put together the portfolio over the first three years is entirely different than how we've been managing the Fund since the end of 2018. Those changes of being more diversified and invested in the right sectors is what has allowed us to deliver on our goals and our performance. In 2019, the

Fund returned 35.75% before fees and expenses, and 34.16% after fees and expenses. This compares favorably to the S&P 500's total return of 31.49%.

Within Morningstar's large blend category, the Fund finished [2019], in the top sixth percentile, and outperformed the category average by 5.27%. Over 90% of the Fund's gains were unrealized, and thus our return was tax-efficient. Furthermore, because we are invested in so many great companies that we believe can deliver above-average organic revenue and earnings growth for years to come, we can continue to hold those investments and deliver further tax-efficient returns.

Now, while it's early in the year, the Fund is off to a fantastic start. As of yesterday, January 27, year to date the Fund is up 2.24% after all fees and expenses, compared to 0.49% for the S&P 500's total return. We are confident that our mentally flexible approach is working to our advantage and will help us continue to deliver on our goal of continued growth of capital and outperformance. We look forward to delivering value for fellow shareholders over the coming years.

I would like to end this presentation with a quote from one of my heroes growing up: Kobe Bean Bryant, may he rest in peace with his daughter GiGi. "You guys know that if you do the work, you work hard enough, dreams come true. You know that; we all know that. But hopefully what you get from tonight is that those time when you get up early, and you work hard; those times when you stay up late, and you work hard;

those times when you don't feel like working—you're too tired, you don't want to push yourself, but you do it anyway. That is actually the dream. That's the dream. It's not the destination; it's the journey. And if you guys can understand that, what you will see happen is that you won't accomplish your dreams, your dreams won't come true—something greater will."

Thank you to my fellow shareholders who have taken this journey with me the past four years, and you look forward to continuing on your confidence and support mean the world to me. And thank you to those who have helped allow me to go on this journey and grow both professionally and personally. It is a dream come true.

Again, if you are unable to participate in the live webcast and/or do not get your questions answered, please feel free to reach out to Kristina Surkova in Client Services to arrange a call with me. Thank you for your confidence and continued support; we truly appreciate it. Now back to you, Kristina, to poll for questions.

(00:41:16)

Kristina: [Please reference slide 35] Thank you, Greg. And we want to thank those of you who submitted questions in advance. We will cover those first and then turn to questions that might be submitted during the presentation.

Number one is where are you finding value?

Gregory: I will refer you to slides 11 through 30 to help explain several of the driving forces behind approximately two-thirds of our portfolio; as well as slide 31, which discloses 59 of our 64 investments.

Simply put, positions in the portfolio are there because we believe they offer good value and will deliver good risk-adjusted returns over a full market cycle.

(00:41:57)

Kristina: Thank you, Greg. Another question: have you changed metrics for the definition of value?

Gregory: Absolutely not. At the end of the day, when you invest, you are trying to get the greatest amount of future cash flow relative to your upfront investment. I will refer you back to slide ten.

Historically, by and large, it did not make sense to pay higher multiples for certain industries, and most companies within them, because very few could sustain above-average growth rates. So it made sense to start an investment search looking at below-average multiple stocks and from there try to identify average to above-average businesses. If you had a good batting average when it came to business analysis, then the majority of the investments' return would be from earnings growth and multiple expansion due to mean reversion.

However, what has been happening more recently over the past few years is that outside of technology, there is very little global economic growth. And technology is benefiting certain already-established winners

like Nike and Adidas for example, and as the same time is breaking down the barriers to entry for a lot of sectors and companies within them that historically enjoyed good returns.

So to put this into context—in 1997, when I was still in high school, if I wanted to make a phone call at school, I had to use a pay phone. I actually remember a phone call I had with Steven Romick back then from school. If you had the opportunity to invest in a payphone business back then at let's say a ten percent free cash flow yield, it would have been a disastrous investment. That industry had already begun to be disrupted by carphones and cellphones, and within a few years, it was game over.

At the same time, there was a little-known company that went public in May 1997 called Amazon.com. My first experience with Amazon was ordering a book to help me study for my AP Art History exam. Boy do I wish I invested in that company back then. Books and music were just the first retail categories Amazon was disrupting.

In 1997, Amazon generated $147.8 million in revenue, and it had an operating loss of $31 million. So there was no free cash flow yield back then. The company was in heavy investment mode, and still is to this day. Twenty years later, in 2017, it generated nearly $178 billion in revenue, and over $3 billion in net income. So in hindsight, it is obvious that Amazon.com was a phenomenal value and that payphone companies were short.

Now what is interesting to note is that Amazon is in heavy investment mode currently, both in trying to offer one-day delivery on more goods and services, as well as trying to offer more tools and services within AWS. These investments, which depress earnings over the short term, can help explain why the stock has been a significant underperformer over the past 13 months.

But what fellow shareholders are paying US Value to do is use our brains to try to figure out where industries and certain companies within them are going in the future. So while Amazon.com might not look like a cheap stock on current earnings, we believe its competitive advantages are increasing at a rapid rate, and that larger addressable markets are opening up for them as well. We believe that this combination will ultimately lead to much bigger revenue and earnings in the future. So at the end of the day, the business analysis is the most important thing to help determine what value is, and what a value trap is. That has never changed, and our definition of value has never changed.

What has changed is our process by which we are trying to uncover value. It now starts with industry and company analysis as opposed to begin our quest by looking at statistically cheap stocks.

(00:45:19)

Kristina: Thank you, Greg. There are no other questions at this time. We want to thank you all for listening to FPA US Value's Second Half 2019 Webcast.

We now turn it over to the system moderator for closing comments and disclosures.

Moderator: Thank you for your participation in today's webcast. We invite you, your colleagues, and shareholders to listen to the playback of this recording and view the presentation slides that will be available on our website within a few days at FPA.com. We urge you to visit the website for additional information on the Fund such as complete portfolio holdings, historical returns, and after-tax returns.

Following today's webcast, you will have the opportunity to provide your feedback and submit any comments or suggestions. We encourage you to complete this portion of the webcast. We know your time is valuable, and we do appreciate and review all of your comments.

Please visit FPA.com for future webcast information, including replays. We will post the date and the time of the prospective calls to forward to end of each current quarter, and expect the calls to be held three to four weeks following each quarter end.

If you did not receive an invitation via email for today's webcast and would like to receive them, please email us at crm@fpa.com.

We hope that our quarterly commentaries, webcasts and special commentaries will continue to keep you appropriately informed on the strategy.

We do want to make sure that you understand that the views expressed on this call are as of today and are subject to change based on

market and other conditions. These views may differ from other portfolio managers and analysts of the firm as a whole and are not intended to be a forecast of future events, a guarantee of future results, or investment advice.

(00:47:21)

Any mention of individual securities or sectors should not be construed as a recommendation to purchase or sell such securities. **Past performance isn't a guarantee of future results.**

Any statistics have been obtained from sources believed to be reliable, but the accuracy and completeness cannot be guaranteed.

You should consider the Fund's investment objectives, risks, charges, and expenses carefully before you visit. The prospectus details the Fund's objectives and policies, charges and other matters of interest to the prospective investor. Please read the prospectus carefully before investing. The prospectus may be obtained by visiting the website at www.fpa.com, by email at crm@fpa.com, tollfree by calling 1-800-982-4372, or by contacting the Fund in writing.

FPA Funds are offered by UMB Distribution Services, LLC.

This concludes today's call. Thank you and enjoy the rest of your day.

(00:48:34)

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