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THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Combining Risk-Taking Assets and Risk-Mitigating Strategies Amid Potential Volatility

GREGG T. ABELLA is a Co-Principal and Portfolio Manager at Investment Partners Asset Management. After graduating from Bowdoin College in 1992 with degrees in both economics and Spanish, he began his professional career at Chubb & Son in the International Division of the Surety Credit Department handling Latin America and Europe. Mr. Abella subsequently held a number of positions with Chubb, ultimately establishing and managing the Guaranty Department for its subsidiary, Chubb do Brasil, in Sao Paulo, Brazil. His multinational experience and credit analysis skills bring a unique global perspective to the firm's clients. Mr. Abella has earned the Accredited Investment Fiduciary — AIF — professional designation from Fiduciary 360 and has received formal training in investment fiduciary responsibility. He joined Investment Partners in 1998.

SECTOR — GENERAL INVESTING

TWST: Could you tell me a little bit about the firm?

Mr. Abella: Sure. We are a regional investment management firm, specializing in investment planning for high net worth individuals and not-for-profits. Our focus is on diversified portfolios, but our particular expertise is investing in value and growth at a reasonable price.

TWST: Is there a unique investment philosophy at the firm?

Mr. Abella: We tend to focus, when we're picking individual stocks, on value and growth at a reasonable price. We also acknowledge that there are other styles that work, and when we're building out a broad, diversified portfolio, we stick to our knitting and invest in companies and funds within our wheelhouse of expertise. And then, we use confirmatory research in terms of model building to allocate assets to other styles, such as growth, international, small-cap international developed markets, high yield and other strategies where we rely on experts to fill those asset classes and those buckets.

TWST: Did you want to start by talking about one stock that you find interesting right now?

Mr. Abella: Sure. As value guys, we like when a stock is beaten down. That's when things start to look interesting, and after a year like 2018, there are many pebbles on the beach. But one in particular that we've owned and also are actively considering adding to is **AT&T** (NYSE:T), which, based on its 52-week high at one point, had a market cap of approximately $250 billion and more recently has corrected down to about a $200 billion market cap, down 20% off of its high.

TWST: What's going on with AT&T now that would be of interest to investors?

Mr. Abella: A couple of things. One of the reasons, and I think the largest reason for the correction, has to do with their acquisition of **Time Warner**, which went through in the late part of last year after a lot of controversy because it's going to require a lot of integration. It's going to diversify them into an area of business that they traditionally haven't operated, and I think that uncertainty, plus the debt that they've taken on to enact that strategy, has caused some investor consternation and thus the decrease in the price. But we believe that **AT&T** will ultimately be successful in integrating **Time Warner** and will emerge from this, hopefully, a more diversified company that can sustain and grow its dividend over time.

TWST: AT&T has changed over the years. It was the nation's phone company, then it was broken up, and then it went into unique businesses. It's sort of come back, being in areas where there's some opportunity. What do you think that AT&T is going to look like a couple years from now?

Mr. Abella: Great question. Anybody that has some time horizon looking backward at this stock has known that this is a company that has morphed many times over, as you just alluded to. Even though it's a very large company, it has successfully navigated a very rapidly changing landscape with respect to telecom and also media. I think, if they didn't make the more recent move, it would have really kept the company from staying agile and staying in front of the curve with respect to technology.

The wireless business has been a cash cow for them. It's their bread and butter. Some 10 years, 15 years, 20 years ago, it would have been the landline business, and that's really now anachronistic. The foray into cable or media and entertainment, I think, is going to pay off over the

long haul in a couple of different ways. First, they have to make a lot of investment in infrastructure to roll out their new high-speed 5G internet and data service for the wireless business.

But on the entertainment side, **DirecTV**, on which they were gaining subscribers up until a couple of years ago, has been losing some of its subscribers. So integrating **Time Warner** into the mix actually gives them a platform to create a new way to access their content, which they intend to call Osprey, which is a fully packaged **DirecTV** service to homes that can get access to it without having to have a satellite dish. They can either use the dish if they want to or not, and they can leverage off somebody else's cable broadband or possibly just the high-speed wireless and get access to sort of a basic package, the way you would with cable, a basic package with HBO content, which they now own, and then have sort of a premium package that can leverage off the **Turner** and **Time Warner** library.

Highlights

Gregg T. Abella discusses Investment Partners Asset Management. Mr. Abella focuses on diversified portfolios. He notes that, when choosing stocks, the firm's expertise is in value and growth-at-a-reasonable-price investing. Mr. Abella then uses model building to allocate assets to other styles. When it comes to the value side, Mr. Abella likes stocks that are beaten down, and after 2018, he is seeing a lot of opportunities. He thinks volatility is probably here to stay in 2019. With this in mind, Mr. Abella is trying to combine risk-taking assets to get a return with risk-mitigating strategies.

Companies discussed: AT&T (NYSE:T); Netflix (NASDAQ:NFLX); Alphabet (NASDAQ:GOOG); Facebook (NASDAQ:FB); Oracle Corporation (NYSE:ORCL); Microsoft Corporation (NASDAQ:MSFT); Berkshire Hathaway (NYSE:BRK.A); SoftBank Group Corp. (OTCMKTS:SFTBF); Extra Space Storage (NYSE:EXR); Regency Centers Corp. (NASDAQ:REG); Sun Communities (NYSE:SUI) and Healthcare Trust of America (NYSE:HTA).

I think this will be a real boon for consumers that are looking for content for older movies that maybe are not on **Netflix** (NASDAQ:NFLX), they're not on **Hulu** or any other streaming service, but there are movies that they want to get access to. This is going to be a one-stop shop to get it. So I'm quite optimistic that this is the right move for them, and the metrics from a valuation standpoint are very compelling.

TWST: Do you think that eventually they might be more like some of the Silicon Valley and West Coast companies coming up with innovative products using their name to market those products, maybe something like a Google (NASDAQ:GOOG) or Facebook (NASDAQ:FB), or do you think they are going to stay where they are now?

Mr. Abella: You're taking the words right out of my mouth. This is another avenue for them, since they now have a platform because of the I.P. of the content that they now own, that they can leverage and do some things in terms of monitoring metrics and data — and advertising — that maybe they couldn't have before, and that's a very high-margin business. So I don't know if you're ever going to see **AT&T** with the same sort of growth multiples that you might see on a Silicon Valley stock. It's just more of a staid, reliable — more like a utility — but with a little bit of a growth kicker in there from these other avenues. I think, for sure over the long term, it has a lot of potential.

TWST: Did you want to mention another company?

Mr. Abella: Well, since we just mentioned Silicon Valley, another company that we find interesting in here is **Oracle** (NYSE:ORCL), which is the second-largest software company in the world behind **Microsoft** (NASDAQ:MSFT), trading at very reasonable multiples. When we're looking at investments in individual companies, we start with whether or not we like the business generally. And then, if we like the business, do we then like the valuation? If those two line up, then it's time to dig even deeper and see if this is the type of company that can grow over time. And this particular company seems to fit a lot of our criteria. So it's one that we've had more interest in over the past year.

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Looking forward, this is a company that's still going to do $185 billion in sales, projecting $60 billion in EBITDA. The company is trading at a very reasonable multiple of about 10 times earnings and 6.5 times enterprise value to EBITDA with 20% return on equity and 6.7% yield — not all bad. Personally, I like the stock in terms of buying it at a little lower level. I really liked it when it was in the higher $20. We've had a little bit of a run lately, but the average price target for the stock from the analyst community is in the mid-$30. So tactically, I think that this is one that you could sort of have a core position and even trade around, acquiring in the lower $20, maybe lightening up on it in the mid-$30, but maintaining a long-term core position because you're getting paid very handsomely to wait as the story unfolds.

TWST: What's going on with Oracle? I understand Berkshire Hathaway (NYSE:BRK.A) was interested in it.

Mr. Abella: Yes. They've taken a stake more recently, which is sometimes a blessing and a curse. Warren Buffett's track record, with respect to technology investing, has been, let's say, less than stellar. I think his timing hasn't necessarily been the best, but he tends to invest for a very long period of time, and in this case, I think it's one that will work out.

I don't blame him because the company has $60 billion in cash, approximately 1-to-1 cash to debt. The enterprise value to EBITDA is about 10 times, 14 times earnings on a non-GAAP basis, $40 billion in sales, over 75% gross profit margin and 10% net gross profit margin. All of the high notes are sort of hit with an investment like this regardless of the business that it's in. Also, they've been buying back stock at a nice aggressive clip. So these are all things that we like to see.

1-Year Daily Chart of AT&T

Chart provided by www.BigCharts.com

"One of the specialties of the house is closed-end funds. They're not like open-end funds where when you buy the shares of the funds the money goes into the fund. They are almost more like ETFs because they trade like stocks."

1-Year Daily Chart of Oracle Corporation

Chart provided by www.BigCharts.com

In terms of ownership though, it's nice to see **Berkshire Hathaway** invested, but beyond that, most of the larger investors just appear to be index funds. I would be happier seeing sort of a technology-oriented company like a **SoftBank** (OTCMKTS:SFTBF) or even a technology-oriented activist get involved in a company like this because of the ownership outside of the institutions. About a third of the company, in terms of stock in options, is still held by Larry Ellison, and he's been there since the beginning obviously. And he's done very well, but I also think that it somewhat represents a bit of an overhang because it's a large position of stock, and the company keeps rewarding inside management with more and more stock. I think that somebody from the outside who could kind of shake things up could maybe help the company prioritize its shareholders even more with maybe an increased dividend and other things that could be value enhancers over time.

TWST: Is there anything on the horizon for them in the coming year or two?

Mr. Abella: Only that I think they're in the right space. They're basically in the enterprise resource planning software business, which is a very sticky business. They go into large corporations and basically integrate their business processes, supply chain management, data analytics and create a customized software platform for running the company. It takes a long time to integrate that, and once **Oracle** is in a company, the switching costs are so high that they tend to stay in for a long, long period of time.

So it's really a good business. Then, if you look at the trends of the enterprise software business, it's expected to grow at about an 8% clip per year over the next foreseeable coming years. I think it's the right place. It's a decent business. It's very sticky, recurring revenue. I like it a lot.

TWST: Have they mostly grown organically, or have they had some acquisitions?

Mr. Abella: They've had an acquisition here or there. This is one of the reasons that I think it would be good if they had an outside investor who's also in the software-as-a-service and cloud-computing space because it could help them identify bolt-on acquisitions to help growth. Otherwise, it's a company that is certainly growing, but it's growing at a modest clip, and I think they are probably going to have to continue to acquire to get growth rates above single digits.

TWST: Did you want to mention another company?

Mr. Abella: Sure. This one is not really a company as much as it is a fund. One of the specialties of the house is closed-end funds. They're not like open-end funds where when you buy the shares of the funds the money goes into the fund. They are almost more like ETFs because they trade like stocks, but unlike ETFs, the stock of a closed-end fund is issued once, at the time it goes public, and then it trades in the open market on an exchange, and sometimes it trades at the NAV of the underlying assets in the fund, and sometimes it trades at a discount to those assets.

One fund in particular that we've been interested in is called CBRE Clarion Global Real Estate fund. The symbol's IGR. It is a fund that basically invests in REITs, and REITs as an asset class, last year, like many asset classes, had a negative return. I think the North American REIT Index was down about 5%, and the global index for REITs was down almost double that.

When you have an asset class that hasn't worked very well, sometimes in the closed-end fund space, the gap between net asset value and share price gets even more out of whack. So toward the end of the year, on top of the fact that the asset class wasn't popular, you had tax selling and a couple of other events all coming together at once, and at one point, this fund traded at a 19% discount to its underlying assets. And

since it is an asset class that tends to pay dividends, this fund in particular was paying out a distribution rate that's between dividends and return of capital on a monthly basis — at an annualized rate of 9%.

So it kind of checks a couple of boxes for us. You're getting assets at a discount; you're getting paid a coupon while you wait. It's an asset class that, over the long haul, with respect to inflation, real estate tends to do pretty well. It's had a little bit of a run more recently, as a lot of things have in this past couple of weeks. So I'd be looking more toward times when there's more volatility to have the discount to asset value sort of blow out a little bit because those are the best times to buy. I wouldn't necessarily chase this investment, but opportunistically, at times where the asset value discount is wider than it traditionally is, those are times that we're going to be looking at it and potentially buying it.

TWST: What kind of real estate holdings are in the fund? I assume a lot of it is commercial real estate.

Mr. Abella: It is a global fund, but for the most part, it's concentrated about half in the U.S., and the rest is spread out among developed countries outside the U.S. Internationally, it holds investments in Japan, Hong Kong, the U.K., France, Australia, Germany, Singapore, but it doesn't have, really, any holdings in the emerging markets. So you're really dealing with developed-market real estate, with half of it in the U.S.

TWST: Would that include things like office buildings and warehouses?

Mr. Abella: It's commercial real estate. Examples of the holdings are: **Extra Space Storage** (NYSE:EXR). It's basically well-known, for the most part, REITs. **Regency Centers Corporation** (NASDAQ:REG) is one of their holdings. **Sun Communities** (NYSE:SUI) is in there. **Healthcare Trust of America** (NYSE:HTA) is in there as of the last filing. If you follow REITs, it's sort of the larger household-name kind of investments, and there are, as of the last filing, 82 different holdings in their portfolio. So it's pretty well-diversified.

TWST: Changing direction a little bit, you mentioned that you work a lot with high net worth individuals and some not-for-profits. What's on their minds after the correction in the stock market we had late last year?

Mr. Abella: Well, I think it gives everybody a gut check that no asset class or market tends to move in one direction forever without some sort of correction. But what sort of surprised us and a number of folks is that 2018 was sort of a year without a Santa Claus. There wasn't an asset class — with the exception of only one or two short-duration bonds and cash and similar sort of extremely low-risk investments — you weren't rewarded for taking risk in virtually any part of the market. There wasn't a sector you could hide in. There wasn't a part of the world. There wasn't really almost any particular strategy that worked, and that doesn't tend to happen all the time.

You tend to see, in a broadly diversified portfolio, that you have lower levels of correlation, at least in some asset classes. The classic one is that if bonds are down, then stocks might be up or vice versa. Outside of sort of the shorter duration, you really didn't have an asset class that worked counter to your traditional core equity markets. When you're building client portfolios, clients are always concerned that, well, is this market going to come back? Am I going to be back on the trajectory of having a net-positive return?

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I think that over the long haul, diversification works, and that's a strategy that we're going to continue to employ, but it's certainly on everyone's mind whether or not we're going to have more correlation than we expect and whether or not a broad, diversified portfolio is going to have a net-positive return over the coming year. It's hard to know inside of a short period time whether your strategy is going to work. Over the longer haul, statistics bear out that you should do fine with a diversified portfolio and covering lots of different asset classes in different parts of the world. So that's what we intend to do and how we intend to work through what's potentially going to be another volatile year.

TWST: In terms of the not-for-profit and high net worth individuals — what the Federal Reserve does with interest rates and the need for trade agreements — do those impact their investments, and are they concerned about those things?

Mr. Abella: Well, they impact us all. One of the things that I don't know if this administration really took into account is that a trade war works both ways, and we're sort of seeing that with some of the larger corporations saying that trade sanctions in China don't necessarily just hurt China, they hurt large multinational companies. If you hurt the Chinese economy, and you have a large-cap company that relies on its growth in emerging markets, you're going to be impacted. So I think that, yes, certainly for sure the Fed action and trade agreements all factor in. So we're trying to simultaneously have risk-taking assets to get a return and also use risk-mitigating strategies to get current income and act as, to some degree, shock absorbers in case we continue to have more of this volatility through 2019.

TWST: Especially with high net worth individuals, are they thinking about what they might be able to pass on to their heirs? And at some point, there's going to be a big transfer of wealth — the money going from the Baby Boomers to that next generation. What is that next generation doing about investments and planning for investments?

Mr. Abella: Well, the Baby Boomers I think have sort of had a mixed bag. You have some Baby Boomers, and I'm not talking about our clients, but just broadly, who have sort of stuck their head in the sand and not maybe saved as much as they should have for retirement. And on the other end of the spectrum, you have folks — fortunately, folks like our clients — who have planned and have larger nest eggs to pass on. The changes in the inheritance tax have sort of made it a lot easier to pass that wealth on to the next generation.

And the next generation, maybe being Gen X and Millennials, now look at investing in a very different way than maybe their parents did with respect to what sorts of investments they're interested in, what sort of portfolios they want to have, whether or not companies that are legacy holdings that might be in an older person's account meet certain social characteristics that maybe Gen X and Millennials value. So it's going to be an interesting landscape in managing through that because the new portfolio strategies are more technologically advanced and also have a higher sort of focus on social awareness than they did in the past. So that's a challenge for advisers.

TWST: Is there anything we didn't talk about you care to bring up, either about the firm or some trends out there?

Mr. Abella: Just that our own thinking is — this volatility is probably here to stay. The things that brought it on are not the types of issues that are going to get off the front page any time soon. Perhaps we'll strike some sort of trade deal in China, but the undercurrent is still that we're going to be dealing with trade issues with China for a long, long time. And as a matter of fact, the numbers came out earlier today that show the trade deficit has never been bigger than it is now with China. So I don't know what sort of deal we're going to be able to cut, but this is not something that is going to go away overnight and nor is the Fed.

If we have inflation, the Fed is not going to sit idly and do nothing in the face of potential inflation. And that would make investors, I think, really consider what interest expense is going to mean for corporations and their underlying holdings in their portfolios. So we're not out of the woods. I think this is going to be a year marked by more traditional peaks and valleys rather than the slow churn higher over the last five years to 10 years with very low levels of volatility.

TWST: Thank you. (ES)

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