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INVESTMENT STRATEGY OUTLOOK – ALL CAP EQUITY

March 31, 2016

The FMI All Cap portfolios returned approximately 4.5% in the March quarter, compared to the benchmark Russell 3000 Index return of 0.97%. Sectors that outperformed the benchmark included Producer Manufacturing, Retail Trade and Health Technology. On the negative side of the ledger, Energy Minerals, Utilities, Distribution and Consumer Services hurt relative performance. PACCAR, Dollar General and H.B. Fuller all contributed positively to the quarter, while Devon Energy, AmerisouceBergen and eBay lagged. Oil and a number of other commodities, whose prices have been collapsing over most of the past eighteen months, rebounded to varying degrees in the second half of the quarter. Growth stocks, which led the market advance over the past seven years, took a breather in the quarter; value stocks, including FMI portfolios, generally outperformed. Valuations started to become more interesting in January as markets came under pressure, but central banker's sugar once again lifted stocks in February and March. Unfortunately, fundamentals, as measured by revenue and earnings growth, remain quite weak. Standard & Poor's 500 Index (S&P 500) median GAAP[1] sales and earnings growth rates in 2015 were 0.8% and minus 0.8%, respectively. Goldman Sachs calculated final 2015 S&P 500 adjusted sales and earnings per share (EPS) growth, excluding financials and utilities, of minus 3.8% and minus 11.0%, respectively.

As measured by the Dow Jones Industrial Average, the current bull market, lasting over seven years without a 20% decline, is the third longest on record (see chart to the right). This market was starting to break apart last year and into January of this year, with energy, commodity and industrial-related stocks moving into bear territory. Smaller capitalization stocks, and even some of the big winners over the past cycle such as health care and biotech, were slipping. An intra-quarter drop of nearly 30% in the Nasdaq Biotech Index, as well as high profile stock declines from the likes of Valeant, Micron, LinkedIn and Twitter, seemed to indicate the bear was upon us, but soothing comments from the Fed and the European Central Bank (including negative interest rates) have, at least for now, put the bull back in charge.

Bull Markets In The Dow Jones Industrials: Distribution Of Gains By Year

	Annual Bull Market Price Gain (%)								Total
Bear Market Low	1 Yr.	2 Yrs.	3 Yrs.	4 Yrs.	5 Yrs.	6 Yrs.	7 Yrs.	8 Yrs.	Gain (%)
September 24, 1900	**Bull market lasted less than one year**								47.8
November 9, 1903	59.1	21.6							144.3
November 15, 1907	66.2	12.7							89.6
September 25, 1911	28.0								29.1
July 30, 1914*	84.5								110.5
December 19, 1917	24.9								81.4
August 24, 1921	56.0	-7.8	12.6	37.9	13.1	16.5	24.3	60.7	495.2
July 8, 1932	155.1	-7.6	26.1	27.5					371.6
March 31, 1938	**Bull market lasted less than one year**								60.1
April 28, 1942	44.4	1.5	51.3						128.7
June 13, 1949	40.1	10.4	7.4	-1.0	21.2	36.7			222.4
October 22, 1957	29.2	15.4	-7.7	22.2					75.1
June 26, 1962	32.3	17.2	2.8						85.7
October 7, 1966	24.8	3.0							32.4
May 26, 1970	43.6	7.2							66.6
December 6, 1974	41.8								75.7
February 28, 1978	9.0	5.6							38.0
August 12, 1982	52.2	3.0	7.9	39.7	45.4				250.4
October 19, 1987	22.9	25.5							72.5
October 11, 1990	26.2	5.1	14.6	7.9	22.1	26.1	34.8		294.8
August 31, 1998	43.6								55.5
October 9, 2002	32.9	3.9	2.4	15.2	19.5				94.4
March 9, 2009**	61.4	15.6	5.7	11.7	14.2	9.4	-5.5		*158.1*
# Observations	21	16	10	8	6	4	2	1	23
Median	41.8	6.4	7.7	18.7	20.4	21.3	24.3	60.7	85.7
Average	46.6	8.3	12.3	20.1	22.6	22.2	17.9	60.7	133.9

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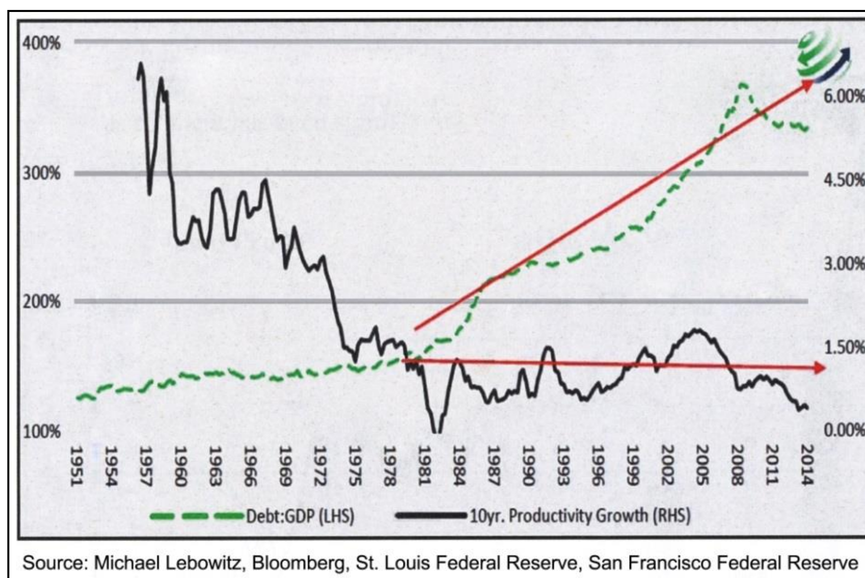
*Adjusted for closing of NYSE in second half of 1914.

**Year 7 gain is through March 4, 2016 (...assuming bull market is still intact).

[1] Generally accepted accounting principles

We would like to embrace easy monetary and fiscal policies, except for the small issue that they don't seem to work. How many years of well-below-par growth, despite unprecedented stimulus, do we need to reach this conclusion? Apparently a decade is not long enough. In a recent market commentary from Dr. Marc Faber, noted value investor and long-time Barron's round table participant, he used the chart to the right, which depicts the rising line, debt-to-GDP,[2] juxtaposed to the declining line, 10-year productivity growth, to show that we are pushing on a string.



Source: Michael Lebowitz, Bloomberg, St. Louis Federal Reserve, San Francisco Federal Reserve

Debt levels go up, growth comes down. GDP remains largely locked in a 0-2% channel. The textbooks say it's not supposed to happen, but rather than explore why this is so, our leaders come back year after year and say "We haven't done enough." Dr. Faber infers the psychological parallel between the academics running the Fed and college professors, by quoting the famous writer and German statesman Johan von Goethe (1749-1832), in a book by Johannes Eckermann (published in 1836), on why professors ignore alternative theories:

> *This is not to be wondered at; such people continue to error because they are indebted to it for their existence. They would have to learn everything over again, and that would be very inconvenient […] They do not prove the truth, nor is such the intention; the only point with these professors is to prove their own opinion.*

One alternative theory to the prevailing conventional wisdom is that unnaturally low interest rates distort economic agents' behavior. Companies, for example, buy back stock and engage in dubious merger and acquisition activity rather than expand their capital investments, research and development spending and hiring. Suppressed interest rates may thus retard, rather than enhance, economic growth. Governments generally believe spending generates economic expansion, but they fail to measure the true cost of this effort, which inevitably appears to exceed the headline benefit. Data across a large number of countries seems to support the notion that government spending is generally beneficial up to the level at which such spending constitutes roughly 15-18% of GDP. Spending on infrastructure, protection, and other public goods enhances overall economic growth up to a point, and then additional outlays appear to restrain growth as the bureaucracy expands. All government spending, including federal, state and local, has grown dramatically over the past fifteen years and is approximately 38% of GDP in the U.S. today. We have discussed these issues at length in previous letters so we won't dwell on them here, other than to observe that nobody is doing much to reduce the size of the government.

The fact that we have low growth is about the only thing on which most people can agree. The rising level of angst and the emergence of populist firebrand politicians are not emblematic of an economy that is satisfying the masses. Unfortunately, this pattern is all too common around the world as global economic growth estimates continue to wane. It is particularly interesting to observe how the Chinese are handling a lack of

[2] Gross Domestic Product

growth in their economy. How are they keeping the masses from stirring? Like Putin's Russia, there is an old fashioned crackdown on dissent and a nationalistic surge. Additionally, the Chinese are plying stimulus maneuvers again, but the level of debt in that economy is already alarmingly high (190-340% of GDP, depending who is doing the measuring). The government tacitly admitted they have a problem as regulators tried recently to foster debt for equity swaps out of some $200 billion in bad bank debt. It is widely recognized that China's banking system is at least $34 trillion in size (up from approximately $3 trillion ten years ago) and it continues to grow rapidly ($525 billion in January) despite increasing bad debts and a slowing economy. Kyle Bass, a highly regarded hedge fund investor, believes that in the current cycle China will experience losses of $3.5 trillion, or roughly 10% of assets and 30% of GDP, which happens to be the same loss rate experienced in the 1998-2001 credit cycle. To put this into context, U.S. banks lost about $650 billion in the great financial crisis of 2007-2009.

It's no coincidence that the dramatic economic slowing China has experienced in the past eighteen months has had a significant drag on U.S. industrial and commodity businesses. Even though we saw the China problems coming, it affected some of our companies more than we thought. It's a further reminder of the degree to which global economies are intertwined. Unfortunately, and despite the recent sharp stock market rally, China may not have hit bottom yet, if Mr. Bass is correct. Until valuations are more attractive, we will stay cautious about having a significant percentage of investments in businesses exposed to the producer side of the Chinese economy. Longer-term, we remain optimistic about consumer growth, but we would not be surprised if even that side of the Chinese economy takes a breather.

Before turning to a couple of individual investments, we'd like to revisit the word *optimism*. We sometimes get chided for not being optimistic enough. From one perspective, however, it is irrelevant. How we feel isn't going to change what actually happens to individual stocks, the market or anything else. From another perspective, optimism, if already reflected in the stock price or the market, is actually a dangerous thing. For many, if not most stocks, that is the issue today. Generally speaking, we are going to be more optimistic if valuations are lower. If pro-growth fiscal and sensible monetary policies are increasing in prevalence, we will be more optimistic. That is not happening today. Finally, optimism is far less important in the investment business than realism or common sense. We have recently seen investors who have been highly optimistic about various stocks back up this sentiment by taking truly outsized positions that have subsequently collapsed. Our modus operandi has always been to take prudent risks, and be highly sensitive to what can go wrong before dreaming about what can go right.

Kirby Corporation (KEX)

(Analyst: Andy Ramer)

Description

Kirby has two business segments: Marine Transportation (77% of 2015 revenue) and Diesel Engine Services (23% of 2015 revenue). The Marine Transportation business operates the largest inland and coastal tank barge fleets in the United States. Diesel Engine Services is a nationwide service provider and distributor of diesel engines, transmissions, parts, and oilfield service equipment.

Good Business

- With approximately 25% of the inland and coastal tank barge markets, the resultant economies of scale position the company as a low-cost operator, and therefore raise the barriers to entry -- as does the Jones Act, which shields the business from foreign competition.
- The inland waterway system plays a vital role in the U.S. economy. Barges offer an efficient mode of transport for a wide range of cargoes.
- The company earns its cost of capital through a cycle.

- This is an easy business to understand.
- The balance sheet is solid, and Kirby generates a significant amount of cash.

Valuation

- The stock trades near the low end of its 10-year average valuation range on a price-to-earnings, price-to-book, price-to-sales, and price-to-cash flow basis.
- Kirby is valued at about a 30% discount to the replacement value of its fleet.

Management

- Chairman Joseph Pyne has been with Kirby for 38 years.
- David Grzebinksi has served as President and Chief Executive Officer since April of 2014, and prior to that was Kirby's Chief Financial Officer.
- Investment decisions are driven by return on capital. Compensation is based, in part, on the achievement of a return on total capital target.

Investment Thesis

Kirby has come under pressure due to the collapse in oil prices. This has resulted in barges that used to ship crude being converted to transport other products like petrochemicals, and has also led to a significant contraction in fracking equipment build and repair work. The percentage of industrywide inland barge capacity dedicated to crude, however, has fallen from 15% at the peak in mid-2014 to less than 5% today, and the industry has slowed new building activity and accelerated retirements, in an effort to balance supply with demand. Management has also restructured Diesel Engine Services such that the business is currently operating near break-even levels, which provides opportunity from here. Longer-term, the feedstock position of the U.S. should put the company's customers in a competitively advantaged situation globally. Kirby is poised to benefit from more than $100 billion of planned domestic petrochemical investments.

Twenty-First Century Fox, Inc. (FOX) – Voting B Shares

(Analyst: Dan Sievers)

Description

21st Century Fox, Inc. ("Fox") is a global media company. For 2016, Fox will report in three principle segments: Cable Network Programming, Filmed Entertainment, and Television. Cable Network Programming generated $13.8 billion in 2015 revenue led by (top six properties) Fox Regional Sports Networks, Fox International Channels, Fox News, FX, Star India, and Fox Sports 1. Filmed Entertainment generated $5.7 billion in 2015 revenue from films, home video, and television production and syndication. Television generated $4.9 billion in 2015 revenue from the Fox Broadcast Network as well as 28 owned and operated stations, including 17 Fox affiliates (13 of the top 15 designated market areas). Fox also owns 39% of SKY-GB, 33% of HULU, 50% of Endemol-Shine, 30% of Tata Sky, and other non-consolidated assets.

Good Business

- Fox's domestic cable network value resides mainly in four properties (Fox News, Fox Regional Sports Networks, FX, and Fox Sports 1). Each channel has unique content and brand equity for which its viewers are willing to pay (even directly). Establishing investments in Fox Sports 1 have been lossmaking, with first profits expected in 2016-2017. Advertising dependence is relatively low. Recurring revenue is high.
- The company has spent decades building networks that occupy coveted channel slots in international Pay TV systems, where subscriber growth is strong. For example, "Fox Sports" is often said to be "the ESPN" of Latin America.

- Star India has approximately 25% of Indian viewership share (much higher in sports) in a large and growing roughly 150 million-household Pay TV system, though recent heavy sports investment left Star India lossmaking in 2015. This asset alone could contribute $1 billion in [incremental] EBITDA[3] within 5-7 years.
- Fox Broadcast's ratings share fell dramatically with the decline in popularity of American Idol that began in 2011. Recently, Fox Broadcast network lost money, even after receiving reverse retransmission fees from affiliates. Fox's owned and operated stations are nicely profitable. Retransmission fees are growing rapidly, and a minor recovery in ratings share could result in significant earnings additions. Fox's spectrum assets have been mostly ignored, but have value.
- The company's library of owned content is rising in value, thanks to streaming video-on-demand services.

Valuation

- When reasonable adjustments are made for major non-consolidated stakes in SKY, HULU, Endemol Shine, and Tata Sky (ignoring smaller stakes), Fox appears to trade for 10.1 times EPS, 9.0 times enterprise value-to-EBIT[4] and an attractive 1.99 times EV/Sales vs. a 22.1% EBIT margin expected in fiscal year 2016.
- On a sum-of-the-parts basis, we believe the stock is worth over $40 per share, offering over 50% upside.

Management

- The Murdoch family directly controls approximately 40% of the voting interest in Fox. James Murdoch (42) is Chief Executive Officer. Rupert Murdoch (84) and Lachlan Murdoch (44) are both listed as Executive Chairmen. Chase Carey (61) is Executive Vice Chairman. An activist investor, ValueAct, controls 6% of the vote and holds a board seat.
- While Rupert Murdoch has occasionally acquired trophy assets, Fox should also be credited for the creation of an impressive global portfolio of media assets. James Murdoch may prove less imperious than Rupert.

Investment Thesis

Valuation aside, it would be difficult to identify a finer portfolio of global media assets than those owned by Fox. Its operating income margins are very likely to increase over the next several years -- something that cannot be said for many traditional peer companies. Having fallen 30% from December 2014 highs amidst domestic Pay TV pessimism (and foreign exchange headwinds), we feel that Fox's shares present an excellent entry point for long-term contrarian investors, as the market is failing to assign value to a variety of the company's assets that generated temporary losses in 2015, as well as assets that are unconsolidated and do not contribute operating earnings at present.

Thank you for your confidence in Fiduciary Management, Inc.

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[3] Earnings before interest, taxes, depreciation and amortization
[4] Enterprise value-to-earnings before interest and taxes

Fiduciary Management Inc.
All Cap Equity Composite
12/31/2007 - 12/31/2015

Year	Total Return Gross of Fees %	Total Return Net of Fees %	*Benchmark Return %	Number of Portfolios	Dispersion %	Three Year Ex-Post Standard Deviation		Total Composite Assets End of Period ($ millions)	Total Firm Assets End of Period ($ millions)	Percentage of Firm Assets %
						Composite	*Benchmark			
2008	-26.65	-27.18	-37.31	12	0.60	n/a	n/a	$ 56.9	$ 4,062.5	1.40%
2009	30.19	29.35	28.34	18	0.23	n/a	n/a	$ 86.9	$ 7,008.9	1.24%
2010	18.20	17.41	16.93	18	0.26	n/a	n/a	$ 103.3	$ 9,816.0	1.05%
2011	3.85	3.14	1.03	23	0.41	19.57%	19.35%	$ 127.4	$ 12,273.6	1.04%
2012	16.06	15.34	16.42	30	0.27	14.87%	15.73%	$ 168.5	$ 15,253.5	1.10%
2013	29.61	28.70	33.55	35	0.69	11.72%	12.53%	$ 211.6	$ 19,705.3	1.07%
2014	12.65	11.91	12.56	41	0.31	8.43%	9.29%	$ 268.0	$ 21,001.1	1.28%
2015	-0.14	-0.82	0.48	42	0.45	9.70%	10.58%	$ 263.7	$ 21,042.9	1.25%

*Benchmark: Russell 3000 Index®

Returns reflect the reinvestment of dividends and other earnings.
The above table reflects past performance. Past performance does not guarantee future results. A client's investment return may be lower or higher than the performance shown above. Clients may suffer an investment loss.

Fiduciary Management, Incorporated (FMI) claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. FMI has been independently verified for the periods 12/31/1993 - 12/31/2015. Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The All Cap Equity composite has been examined for the periods 12/31/2007 - 12/31/2015. The verification and performance examination reports are available upon request. Benchmark returns are not covered by the report of independent verifiers.

FMI was founded in 1980 and is an independent investment counseling firm registered with the SEC and the State of Wisconsin. The firm manages over $21.0 billion in assets of pension and profit sharing trusts, mutual funds, Taft-Hartley funds, insurance company portfolios, endowments and personal trusts. The firm includes both institutional and mutual fund business. Although the firm has participated in wrap programs, it is a separate and distinct business, and is excluded from firm-wide assets.

The FMI All Cap Equity Composite was created in December 2007. These accounts primarily invest in small, medium and large capitalization US equities.

The FMI All Cap Equity Composite reflects time-weighted and asset-weighted returns for all discretionary accounts. From December 31, 2007 all accounts were managed for at least one month. All returns are calculated using United States Dollars and are based on monthly valuations using trade date accounting. All accounts in this composite are fee paying. Gross of fees returns are calculated gross of management fees and custodial fees and net of transaction costs. Net of fees returns are calculated net of actual management fees and transaction costs and gross of custodial fees and withholding taxes.
Dispersion is calculated using the equal weighted standard deviation of all accounts in the composite for the entire period. As of 12/31/2011, the trailing three year annualized ex-post standard deviation for the Composite and Benchmark are required to be stated per GIPS®.

Currently, the advisory fee structure for the FMI All Cap Equity Composite portfolios is as follows:

Up to $25,000,000	0.75%
$25,000,001-$50,000,000	0.65%
$50,000,001-$100,000,000	0.60%
$100,000,001 and above	0.55%

The firm generally requires a minimum of $3 million in assets to establish a discretionary account. High Net Worth individuals may establish an account with a minimum of $1,000,000, however, the firm reserves the right to charge a minimum dollar fee for High Net Worth individuals depending on the client servicing involved. The minimum account sizes do not apply to new accounts for which there is a corporate, family, or other substantial relationship to existing accounts. In addition, the firm reserves the right to waive the minimum account size and minimum annual fee under certain circumstances. A complete list and description of all firm composites is available upon request.
Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The Russell 3000 Index® measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market. The All Cap Equity composite uses the Russell 3000 Index® as its primary index comparison.