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THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Participating in Up Markets and Preserving Capital in Down Markets

LISA Z. RAMIREZ, CFA, is a Partner, Portfolio Manager and Analyst at Denver Investments. She is a graduate of the University of Colorado and has an MBA from Regis University. She is also a member of the CFA Institute and CFA Society Colorado. She has been President and Treasurer for the Latin American Educational Foundation. In 2015, she was named Businesswoman of the Year by the Hispanic Chamber of Commerce of Metro Denver.

SECTOR — GENERAL INVESTING

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

Ms. Ramirez: Denver Investments is a research-driven professional money manager. We were founded over 50 years ago. We are an employee-owned firm, and we manage $7.6 billion in assets. Denver Investments is the adviser to the Westcore family of mutual funds.

TWST: And could you talk a little bit about the strategy that you work on and if it has a specific philosophy?

Ms. Ramirez: Of course. The value investment team manages $1.5 billion in dividend-only value assets for retail and institutional clients, including the Small-Cap Value, Smid-Cap Value, and Mid-Cap Value Strategies. We believe our investment philosophy is unique and innovative with a focus on the long term. The four main tenets to our philosophy are that we focus on cash flow, not earnings or revenue growth; we invest in businesses that meet our quality criteria and pay a dividend; we strive to buy businesses on sale; and we are not a star system. We make team-based decisions on every stock.

TWST: And why does this approach make sense with the current market conditions?

Ms. Ramirez: Well, we think this approach makes sense in all market conditions. We believe investing in dividend-paying stocks is a smart way to invest. Dividend payers have historically outperformed the market, and they have done so with less risk. Within the small- and mid-cap universe, which is our primary focus, dividend payers have compounded money at a rate 480 basis points higher than nondividend payers, thus creating over four times the amount of dollar value.

Research shows that this dividend supremacy historically holds true from the smallest all the way up to the largest companies. In rising markets, these stocks have kept pace, while in falling markets, they have done a better job of preserving shareholder capital. Now some may think that the phenomenon of dividends outperforming comes from just a couple of high yielding sectors, but it doesn't. Our research shows that dividend payers have historically outperformed nondividend payers in all sectors and do so with less risk, as measured by standard deviation.

TWST: And also, the fact that they are dividend-paying stocks, they might be appealing for those people who are nearing retirement or are retired and looking for dividends in the retirement years.

Ms. Ramirez: Yes, it could be a good product for individuals interested in capital preservation and, to a lesser extent, yield. Since we prefer to own companies with a lower payout ratio who have the ability and intent to grow those dividends rather than own companies with high dividend yields, our yields have historically been modestly higher than the respective indices. Specifically, our Small-Cap Value strategy has a dividend yield 50 basis points higher than the Russell 2000 Value Index, and our Mid-Cap Value strategy has a dividend yield 20 basis points above the Russell Midcap Value Index before fees.

TWST: And did you want to mention a company that you find interesting?

Ms. Ramirez: Absolutely. One of our holdings we find very interesting is **InterDigital** (NASDAQ:IDCC). **InterDigital** is a technology licensing company that helps design and develop standards that enable and enhance wireless communications. Think of them as a mini-**Qualcomm** (NASDAQ:QCOM). They collect royalties for standards they helped pioneer, standards that allow all of us to use our wireless devices on 2G, 3G, 4G and soon-to-be 5G networks. This is a high-return-on-invested-capital business with a very shareholder-friendly management team.

Today, roughly half of the handset units sold globally are paying **InterDigital** for their intellectual property, which means that half are not, and this is the opportunity. This is changing for the positive, especially when it comes to China. China wants and needs to sell more of their products globally. In order to do so, we see them respecting intellectual property more than they ever have, and signing agreements with companies like **Qualcomm** and **InterDigital**. If half of the nonpayers convert to payers, we believe the stock price could approach $100.

And this doesn't even give them credit for what they are doing on the next-generation royalties for 5G and internet of things. Internet of things is where millions of connected devices feed data up for analysis, allowing you to remotely monitor data from things like refrigerators, washers or even a fleet of tractors. The possibilities with such a connected world are only starting to be defined.

The bottom line is, we think there is an enormous opportunity for **InterDigital** to continue to grow cash flow over time, and they are returning the cash flow to shareholders through dividend payments and stock buybacks. They have raised their dividend 100% over the past two years and by 23% since 2011 while reducing their share count. This is what we look for: Companies that do very shareholder-friendly things and have great long-term opportunities.

TWST: Did you want to mention a second company?

Ms. Ramirez: I'd love to. Another name we own is **Goodyear Tire** (NASDAQ:GT). **Goodyear** develops and manufactures tires and related products and services worldwide. This name hit our stock screen due to an attractive valuation and recent improvements in their return on invested capital. For every stock, when we begin our initial research, we utilize a discounted cash flow model, but we use it in reverse. We let the stock price tell us what the market is implying about revenue growth, cash flow margin, capital needs and risk.

In the case of **Goodyear**, the market was pricing in negative revenue growth, no margin improvement, a high level of capital spending and a high discount rate. Through our research, we believe that the company is at an inflection point, and the market isn't appreciating the enormous cash generation that is ahead of them. They have recently completed significant investments in their core business to improve the product mix toward higher-margin value-added tires, and they have just finished paying $3 billion toward their underfunded pension plan. With these payments behind them, we believe there should be significant cash available to pay down debt and grow the dividend.

At the same time, their business has changed. After achieving key labor concessions, their cost structure is lower and more variable in nature, reducing the negative impact of down cycles. Layer on the mix shift toward higher-margin tires, lower raw-material prices and a demand tailwind coming from a strong cycle of new-car sales and you have a very nice outlook for margin improvement.

TWST: And is it partly because people are keeping their cars longer, putting more miles on their cars?

Ms. Ramirez: Yes, miles driven have increased over the past couple of years as a result of low gas prices. Historically, this has helped drive replacement tires, which are 70% to 80% of **Goodyear's** mix. What I was referring to was the strong new-car sales cycle that began after the financial crisis. This has resulted in more registered vehicles that are in or near the sweet spot of needing replacement tires. Basically, we see pent-up demand in the market, which should be a good tailwind for **Goodyear**.

TWST: And did you want to mention another company?

Ms. Ramirez: I am going to mention our largest holding, **Dean Foods** (NYSE:DF). They are a processor and distributor of milk and other dairy products. We believe **Dean Foods** is on the right path for sustainable cash flows and return-on-invested-capital improvements due to internal initiatives that we identified as being unappreciated by the market. They have shown initial financial improvements driven by more profitable volume growth. The profitability improvements have come from logistical cost reductions and layering new products across their national distribution infrastructure. An example of this is the rollout of DairyPure, their antibiotic-free, non-growth-hormone, high-protein-content milk at a much lower cost to organic options.

Highlights

Lisa Z. Ramirez discusses Denver Investments as well as the Small-Cap Value, Smid-Cap Value, and Mid-Cap Value Strategies. Ms. Ramirez's investment philosophy is based on four tenets: focusing on cash flow, rather than earnings or revenue growth; investing in quality businesses that pay a dividend; buying businesses on sale; and making team-based decisions. According to Ms. Ramirez, this approach makes sense in all market conditions because dividend-paying stocks have historically outperformed the market and done so with less risk. In addition, Ms. Ramirez expects to participate in up markets and preserve capital in down markets because she invests in companies with a lower payout ratio that can grow their dividends over time.

Companies discussed: InterDigital (NASDAQ:IDCC); Qualcomm (NASDAQ:QCOM); Goodyear Tire & Rubber Co. (NASDAQ:GT) and Dean Foods Co. (NYSE:DF).

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TWST: And there is increased demand now for healthier kinds of milk among consumers?

Ms. Ramirez: Yes. There is an increased demand for healthier food products overall. We can see that from the higher growth rates of organic products in general compared to conventional food products. The consumption of private-label milk has not grown over the last few years, but the branded and health-conscious side is definitely growing. We are also seeing the recent increase in birth rates, cereal category stabilization and slowing growth of alternative beverages help drive an improvement in milk consumption.

TWST: And they seem to be diversified, owning different types of companies.

Ms. Ramirez: They are diversified in terms of the products they offer. They not only produce private-label and branded milk, but they also produce juice, tea, ice cream and other dairy-based products.

TWST: I understand that they bought Friendly's restaurants recently.

Ms. Ramirez: Yes. While this was a small acquisition for them, it increases their exposure to the more profitable ice cream business, taking it to roughly 15% of their sales from 12%, and adds another point of distribution — again, growing higher-margin branded products and leveraging their infrastructure.

TWST: And as you talk with clients this year, what are some of their concerns about the market in 2016 and as we look forward to 2017?

1-Year Daily Chart of InterDigital

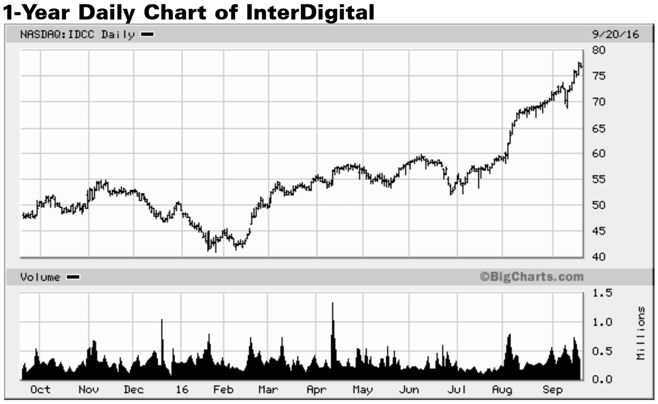

Chart provided by www.BigCharts.com

1-Year Daily Chart of Goodyear Tire & Rubber Co.

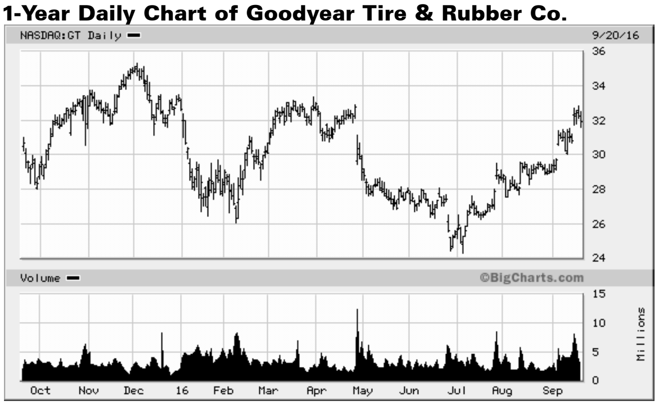

Chart provided by www.BigCharts.com

Ms. Ramirez: We have been asked about the valuation of dividend payers and what we might expect in a rising interest rate environment or in a down market. It is true that high yielding dividend payers are trading at a historical premium today and appear susceptible to a pullback. In addition, research has shown that high yielding dividend payers typically underperform during rising rate or inflationary environments.

The good news for us and our clients is that our dividend strategy is not focused on high yielding stocks but rather companies that have a lower payout ratio and can grow their dividends over time as a result of strong and increasing cash flows. And these types of stocks, dividend growers, have historically outperformed in rising rate environments as well as in down markets. So we feel well-positioned if rates rise or if the market takes a downturn.

TWST: Do some of the clients you talk to have concerns that the market is pretty high right now and there could be a correction?

Ms. Ramirez: We do have clients with that concern. While our clients find comfort in the historical market data for dividend growth stocks, we've also educated them so they understand how our specific strategy should perform in up and down markets, participating in up markets and preserving capital in down markets. We have 17 years of history managing small-cap value dividend-only assets for institutional clients and 12 years for retail clients. Over those 17 years, our upside capture rate averages 90% to 95%, while our downside capture rate is roughly 80%. This preservation of capital combined with the participation in up markets results in a strategy that has outperformed the index over a market cycle and has done so with lower risk.

We also talk to clients about the risk controls embedded in our strategy, which are one of the keys to producing risk-adjusted returns above the benchmark. Beyond the focus on dividends, we seek to control risk by buying stocks on sale. Our goal is to buy dollars for $.70 or less where management is increasing the value of those dollars through smart capital-allocation decisions. We strive to use conservative assumptions in our models, maintain tight bands around sector weights, keep position sizes below 5% and maintain a fully invested portfolio. Finally, we vigorously monitor our holdings using a proprietary screen to help flag stocks that are at risk of future underperformance.

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TWST: Do you get a feeling that some investors are concerned about investments overseas, especially if there is an increase in protectionism in the United States depending on who is elected President?

Ms. Ramirez: We do talk about the exposure our companies have to international markets, and we do analyze these exposures as we review every stock. Even recently, when we had the volatility around Brexit, we reviewed our entire portfolio stock by stock. We looked at the stock reactions to the news that the U.K. would leave the EU, and we compared that to the actual exposure that each of our stocks had to that market. We took advantage of market dislocations that we felt were unreasonable by adding to names that were overly punished and trimming or selling names that were near our price target. If we get volatility into the election or around the outcome of the election, we will be ready to research and take advantage of any opportunities that arise.

TWST: And do you think more investors might be looking at domestic investors given that there could be some issues coming on international trade?

Ms. Ramirez: I do think investors will be looking at domestic opportunities, especially if we have increased volatility and continued macro concerns in international markets.

TWST: You said you work with both retail and institutional clients.

Ms. Ramirez: We do. We have institutional clients as well as retail clients who invest in our Westcore Funds.

TWST: And what are their concerns as they look toward the next few years? Are they different from the concerns of retail clients?

Ms. Ramirez: I wouldn't say they're all that different. I think right now the main question is similar to what you asked earlier: how to find value in a market that has moved higher. We reassure our clients that we are still finding attractive opportunities in almost every sector. It's a little more difficult to find value in the utility and REIT sectors. The valuations are stretched because of their defensiveness and the low interest rate environment, but even in these areas, we have found unique ideas. But in our other sectors, we're finding very attractively valued names and increased volatility lends itself to that.

As I mentioned earlier, we look for those market dislocations, and we seek to capitalize on them. The bottom line is, we believe there is power to our approach of investing, and it comes from buying dividend-paying, cash-flow-generating businesses at great prices, and our talented team has a long history of using this approach to help our clients reach their investment goals.

TWST: Thank you. (ES)