ACADEMY
CAPITAL MANAGEMENT

January 31, 2019

Enclosed is your statement for the fourth quarter of 2018.

As we have discussed in the past, volatility is the investor's friend. During the past quarter, we were able to add to our existing stock positions and purchase new positions. Further, we were able to take advantage of the volatility to work on reducing taxes created by sizeable gains we realized early in the year.

In the fourth quarter of 2014 we stated, "Our long-standing fourth quarter tradition had been to discuss the investments which generated the best and worst results for the year. Over time, we came to believe that this exercise had a fundamental flaw – the time horizon was much too short. More often than not, we simply ended up discussing our most volatile positions, not those with the most impact. Instead, we instituted the practice of discussing stocks we have sold." Our preferred stock holding period is "forever"- as long as the underlying company is preserving or increasing its competitive advantage. We prefer extremely low turnover in our portfolios. However, high prices caused the sale of three portfolio companies during the past year.

In March, we sold our position in Aflac (AFL). Despite our aversion to owning life insurance companies, we had researched AFL for years, impressed that a company from Columbus, Georgia was Japan's largest life insurer. We designated it in our riskiest Tier III category (limiting the initial buy to 1.5%). For years, AFL stock price traded at a premium. In 2013, AFL's stock price dropped on regulatory concerns in the Japanese medical insurance market. We believed that AFL's management culture was focused on Japan, could navigate the changes and emerge as a winner in the market. The good news was that we were correct; the bad news is that we did not get subsequent opportunities to purchase the stock at lower prices. In 2018, the stock price surged and we sold in light of the elevated risks of a large bond portfolio accompanied by mature Japanese and US results. While we wanted a larger position, we were pleased with our results as the stock nearly doubled in price while we were paid a dividend. In addition, the investment results outpaced our benchmark S&P 500.

Then, in July, we sold our final position in Microsoft (MSFT). We had owned MSFT before as our first foray into the technology area as a Tier III, purchasing it in January 2001 and selling it in July 2002 for a tidy profit. Then in April 2006, we purchased a sizeable position as a Tier II (initial buy limited to 3%). Due to MSFT's balance sheet and monopolistic Windows and Office franchises, we were comfortable raising MSFT to a Tier II – another first to rate a technology stock above a Tier III. In the fall of 2007, we

sold half of our position for a 50% gain. The following year, as the Great Recession unfolded, we were able to reinvest to 3% in October and then to 4.5% in November 2008. Then with the stock up 50%, we trimmed in 2013. Then, again in 2014, with the stock up 50% again, we trimmed. Finally, with the stock more than doubling, we sold our entire position in July at an extraordinary price.

A book could be written about MSFT on the transition from Windows to the Cloud, but for us there are several “takeaways” from this investment journey. One is that we moved into a new area for us (technology), not by purchasing the cheapest, but by purchasing the “best” company. Second, as we gained comfort, we reevaluated our Tiering structure. This provided the opportunity to increase our result. Third, we used the most significant financial crisis of our lives to expand positions (and had raised the cash to do so). Fourth, we gritted our teeth and held our low-priced stock during a period of unreformed management by Steve Ballmer. Part of the reason we were able to acquire the stock at low prices was his insistence on putting clunky Windows into mobile phones. Fifth, when the company gained new leadership with Satya Nadella, we viewed our earlier trims as “taking our money off the table” and let the stock run to pricing levels that were extraordinary. It was a very successful investment result on which we also received a sizeable dividend while significantly outpacing our benchmark S&P 500.

In June, we sold our position in Zoetis (ZTS), an animal health company, specializing in livestock and companion animals. We purchased the stock as it was spun off from Pfizer. We have had a long history in pharmaceutical investments and grew leery of “patent cliffs” despite our attraction to the drug industry. ZTS represented an ideal opportunity for us because there were fewer generic products in the animal health area as well as a greater recognition of brand names. To us, ZTS combined the durable characteristics of consumer brands (an area we favor) as well as the superior margins of pharmaceuticals. However, the ZTS spin-off was accompanied by a debt level that exceeded our standards and a nose-bleed P/E ratio. As a result, we determined ZTS was a Tier III. In retrospect, we wish it had been labeled a Tier I. We purchased a 1.5% position in ZTS in March 2014 and sold it nearly four years later, nearly tripling our investment while receiving a dividend and significantly outpacing our benchmark S&P 500.

From these discussions, we hope to provide you a deeper look at our investment process. It is worth pointing out that critical to the execution of these ideas is our excellent operations department, led by Derek Richards and supported by the careful work of Joyce Bell, Sara Johnson and Kari Siler.

If you’re new to Academy, past quarterly letters may be useful and may be obtained through your financial advisor or Joyce Bell at our office. Government regulations also require us to send the enclosed copy of Academy's Privacy Notice and to make available to you a copy of our updated Form ADV - Part II (our regulatory filing with the SEC). If you would like one, please contact Joyce Bell at our office.

As always, we appreciate the stewardship responsibilities you entrust to us and your patience with our investment process.

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