Rob Forker, Chief Investment Officer

Big Shoes to Fill

We have much to thank the managers of 2006-2007. They accomplished much during their tenure. Their performance speaks for itself. All four funds performed well and they returned a cumulative 13.7% from April 1, 2006 to March 31, 2007 beating all benchmarks for that same period. Over that same time the S&P 500 returned 8.3% and the Russell 1000 returned 9.8%. The Assets under management for the club (as of June 18, 2007) have now grown to over $6.5 million dollars.

But their accomplishments were not limited to picking great stocks, but also great structural changes for the club as well. The addition of a fourth fund named the Cavalier Fund has allowed DCM to accommodate the growing interest by Darden students in the profession of investment management. Next, the ability to short stocks has further enhanced the professional development of managers. Last, DCM made a concerted effort to reach out to DCM alumni and we will continue along that path.

In conclusion, I would like to thank the 2006-2007 managers for setting a high bar. As the new Chief Investment Officer I have many goals and aspirations for the club. One of the most important is greater exposure for DCM. Steve Evans has been incredibly helpful in our cause. Look for more articles and more news from the club in the coming year. Another goal we have is to get corporate sponsorships. To that end, Greg McCullough and I have sent out corporate sponsorship proposals this past week. Patrick Garcia and Joyce Carman from Foundation Relations have been instrumental in our efforts. Other improvements include the website which has received an upgrade and will continue to be improved. (http://student.darden.virginia.edu/dcm/). Lastly, DCM will seek to increase the number of investment management firms that visit Darden to recruit. Jack Oakes from the Career Development Center has been a great help.

In summary, I believe that DCM is a great club that is well-known within the Darden community; but it is time to expand our reach. I will give updates on our progress in future additions of The Advisor. Thank you and it is an honor to lead such a great organization.

Please contact me at forkerl08@darden.virginia.edu if you would like to become more involved with DCM.

Greg McCullough, Director of Business Development

Calling All Alums

We are now in the heart of the summer and this year’s Portfolio Managers are spread across the country in a variety of internships. A few short weeks from now we will be returning to Charlottesville to begin our second year and will look to inject our funds with fresh ideas from our summer experiences. As Director of Business Development, I want to extend an invitation to all alumni and students to get involved as much as possible in DCM over the coming year. We hope to increase the educational opportunities available to students this year by increasing the number of guest speakers, expanding the content and frequency of The Advisor, investing in research and analytical tools, and creating a comprehensive DCM alumni directory. I am looking forward to enhancing the strong ties that DCM has with its alumni and to building upon what you all have created over the years. If you would like to participate in or contribute to any DCM activities, or if you have fresh ideas for the club, please contact me at McCul- loughG08@darden.virginia.edu.
Jonathan Chou
Meet the Manager

One of our goals this year is to more actively engage our strong alumni base in the field of investment management. To achieve that end, we are initiating a “Meet the Manager” interview to highlight one of our alums in the industry, which is presented in a Q&A format.

Q: Did you participate in DCM while at Darden?
A: Yes, we managed approximately $800,000 in two funds my first-year (Monticello and Darden). We did very well that year and grew our assets to $1MM, and a third fund was started my second-year (Jefferson). The structure was different back then. There were portfolio managers and analysts; there wasn’t a CIO. The funds didn’t have different investment styles like they do today, and we usually met all at once. I was an analyst my first-year and a portfolio manager my second-year.

Q: What do you value most from your Darden experience?
A: The Darden network. Darden and UVA have strong investment management networks. Throughout all of my experiences, I have always been able to call a Darden alum and at least get a meeting, which is all that you can ask for. I never would have been able to do some of the things that I’ve done without the Darden network.

Q: How did you end up in the investment advisory and Fund of Funds business?
A: Before joining CornerStone, I was the Chief Investment Officer for the Nature Conservancy. CornerStone was, and still is, the advisor for The Conservancy. I joined CornerStone because it blended my investment experience with the ability to advise a number of non-profit institutions, while also still remaining involved with The Conservancy. Generally, a Fund of Funds investment is just one component of a customer’s strategy, but CornerStone’s advisory service (80% of our total business) allows us to take a more holistic view. We develop deeper partnership relationships with our clients and their businesses. As a result, we can better match their investment goals with their respective operating and financial strategies.

Q: What advice would you give to Darden students about getting into investment management?
A: Get into the industry as soon as possible. Unlike many other industries, it is critical to get into investment management early in your career in order to start building a track record. Otherwise, I think that the toughest decision is whether to work at a large, established firm or a smaller, entrepreneurial firm. It’s difficult to balance the pros and cons of working at either type of firm, and there really isn’t a right answer.

For questions or comments, please contact Jonathan Chou at ChouJ08@darden.virginia.edu

Kevin Schuyler, CFA
Class of 1997
Firm: CornerStone Partners
Role: Director
AUM: $3 billion
Previous Employers: Louis Dreyfus, McKinsey, Birdwood Capital, and The Nature Conservancy
Fun Fact: When Kevin founded Birdwood Capital with fellow Darden alum Jack Benson (Darden 1997), he purchased the domain for Birdwood.com.
Brian Pratt, Class of 2007

DCM Goes to Hollywood – Value Investing Congress

Three second-year members of DCM (Glenn Miller, Ryan Murphy, Brian Pratt) attended the Value Investing Congress in Los Angeles in early May, in an effort to expand their investing skill sets and to learn from top-notch value investors.

On May 7, the students attended a pre-Congress workshop led by Whitney Tilson and Glenn Tongue of T2 Partners. Workshop attendees went through over a dozen case studies, which illustrated, among other things, the differences between value opportunities and value traps, how to assess company management, and the importance of understanding behavioral finance. It was interesting to note that several of the companies in the case studies overlapped with recent holdings of the DCM funds.

During the Congress, over 350 attendees listened to presentations from over a dozen successful value investors. In addition to discussing their favorite current ideas, these investors also went through several frameworks they use to assess securities. For example, Mohnish Pabrai discussed the importance of having an exit strategy before entering an investment and the attractiveness of high-uncertainty, low-risk situations. Robert Hagstrom emphasized the importance of being careful to accurately describe the attributes of the company in question. Further, Hagstrom, a growth fund manager, discussed the application of traditional "value" tools for assessing growth stocks, and the largely artificial distinction between growth and value. Michael McConnell, a Darden graduate and activist investor, discussed the importance of accountability and strong corporate governance in investments. These were but a few of the frameworks learned that attendees can apply to make better investment decisions.

“In addition to being a source for interesting new ideas, the Congress was also a great opportunity to network with investment management professionals,” said Ryan Murphy. Glenn Miller said the Congress “serves as a great networking event and signal to potential employers that you are serious about a career in asset management. Additionally, it offers a superb introduction to the key principles of value investing and to the ‘Who’s Who’ in the field.”

For the three graduating students, all of whom will work in the investment management industry after graduation, the Congress served as a capstone for the Darden MBA experience, and provided a good transition for their return to the professional world.

Note: Darden is a supporting organization for the 3rd Annual Value Investing Congress this November in NYC!
Jeff Sutton, Darden Fund Senior PM
Weekend at Woodstock – Berkshire Annual Meeting

During the first weekend in May, while most Darden students were celebrating the end of classes, sleeping off their hangovers, and procrastinating from studying for exams, seven members of DCM traveled to Omaha, NE to take in the wisdom and wit of the “Oracle” Warren Buffett and his chief disciple, Charlie Munger, at the Berkshire Hathaway annual meeting. The festivities began with a lunch on Friday, May 4, hosted by Bruce Lauritzen, Darden School Foundation Trustee (Class of 1967), and Chairman of First National Bank of Omaha, an organization with over $16 billion in assets. Mr. Lauritzen hosts this pilgrimage every year for a small group of DCM members. Following lunch, the DCM crew was invited by Duncan Burn’s (Class of 2007) father to meet David Sokol, Chairman and CEO of MidAmerican Energy Holdings, a Berkshire company. It is widely speculated that Mr. Sokol will fill Mr. Buffett’s shoes as CEO of Berkshire. When asked what advice he could offer us about investing, Mr. Sokol reiterated, “what Warren says.” According to Mr. Sokol, Warren Buffett believes you should look for management teams that have “integrity, intelligence, and passion.” However, Mr. Sokol cautioned that without the first of these traits, you might as well not worry about the other two. He also pointed out that no business will ever run as well as the spreadsheet says.

On the morning of Saturday, May 5, the doors to the annual meeting opened at 7:00 am, and thousands of shareholders rushed in to the Qwest Conference Center to claim their seats, which are all selected on a first-come-first-serve basis. Since over 27,000 people attended the event this year, it was imperative to arrive early if you wanted to sit close enough to see Mr. Buffett and Mr. Munger without the help of the 25-foot-tall video screens that hung from the ceiling. Each year the meeting begins at 8:30 am with the Berkshire movie, which is part parody/part info-mercial for each of the Berkshire companies. In short, it tells the story of all that Berkshire encompasses, and it allows Mr. Buffett and Mr. Munger to laugh at each other and the cult-like following that they have created with their annual meeting, otherwise known as the “Woodstock for Capitalism.” Shortly before the movie began, Neil Kansari and I had the pleasure of seeing Mr. Buffett up close and personal, as he promptly walked down the center aisle of the conference center and sat down just two rows behind us about fifteen seats over. He remained there for the next hour until the movie concluded.

The next six hours of the meeting consisted of random questions from the audience to Mr. Buffett and Mr. Munger. During the meeting, any shareholder is entitled to walk up to one of twelve microphones strategically placed around the arena, and when notified, the shareholder may ask any question he chooses. Mr. Buffett and Mr. Munger then proceed to patiently answer each and every question, completely unscripted. This year’s questions ranged from topics such as the potential side-effects from the increased use of financial derivatives over the last five years, to questions about good books to read, and included several protest-like demonstrations intended to influence Berkshire’s involvement with several of its investments that have either impacted the fishing industry in the Pacific Northwest or pertain to China’s involvement in Darfur. Some of the more memorable responses came from Mr. Munger and include, “It’s important to remember that heroes don’t have to be living” (obviously referring to Benjamin Franklin, who Munger claims to have modeled his life after), and my personal favorite, “You’d have to be some sort of pot-smoking journalism student to worry about global warming.”

The weekend was a tremendous success and a great way to highlight the end of the school-year for all of the DCM members. I’d like to reiterate that we are hugely grateful to Mr. Lauritzen for hosting us in Omaha, and for all the support he gives to Darden. After meeting with him, we all agreed that his personal contact with us has a much more meaningful impact to us, as students, rather than simply supporting Darden through financial donations (which of course, are important too!). I think we should all hope to someday repay Darden in a similar manner.

DARDEN ATTENDEES
Class of 2007: Will Cohen, Charles Seidman
Jay Gundy – VP of Development, Darden School Foundation, also attended the lunch with Bruce Lauritzen
Cris Stone – Class of 1972, works with Bruce Lauritzen and also joined us for lunch
Greg McCullough

Yum! Brands, Inc.
May 17, 2007

Investment thesis

YUM is a quick service restaurant (QSR) operator and franchiser with massive global growth potential. Of the company’s market-leading 34 thousand units across the globe, 20 thousand are located in the United States and 14 thousand are located internationally - a mere 2 thousand of which are located in China. Needless to say, there is virtually unbounded growth potential in the Chinese market, as well as in other foreign markets. The company has added one thousand additional units each year for the past seven years and will continue this trend in the future. As the business mix shifts more heavily towards the company’s international divisions, operating margins will benefit. If the company is successful in improving margins domestically through its re-franchising and multi-branding efforts, the stock has significant potential upside. On the downside, the domestic business (representing 59% of revenues and 52% of operating profits) could continue to be a drag on overall performance.

Investment Considerations

• YUM’s five major concepts hold leading market share within their respective segments. As of year-end 2005, KFC held 47% of the chicken QSR segment, Taco Bell held 60% of the Mexican QSR segment, Pizza Hut held 15% of the fragmented pizza QSR segment, and Long John Silver’s held 33% of the seafood QSR segment.
• YUM’s key earnings growth driver over the next several years is likely to be its China Division. The Company has forecasted annual system sales growth in this division to be 22% annually and operating profits to be 20% annually, while adding at least 700 new units per year.
• Since YUM’s separation from PepsiCo in 1997, the percentage of company-owned restaurants has decreased from 34% of total global units to 22%. This strategy has led to enhanced operational performance and improved system-wide profitability, as franchise owners tend to be more “invested” in the business with their own money on the line. While re-franchising limits topline growth, enhanced operational efficiency generates a favorable impact on operating margin.
• Since 2001, the number of multi-branded units (i.e., placing two or more concepts within the same restaurant) has grown from 1,520 to 3,289 worldwide. The Company believes that combining two or more concepts under one roof could add $100,000 to $400,000 in annual sales per unit.
• As is the case with all other companies in the restaurant sector, YUM is particularly vulnerable to ingredient safety. The 2005 outbreak of avian flu in Asia and Europe, subsequent domestic E.coli scares in the United States, and the most recent rat scare in New York City had adverse affects on revenue.

Valuation

• Given the international growth prospects and the evolving revenue and EBIT mix, it is necessary to value YUM based upon discounted free cash flows.
• On the upside, I assume negative to flat sales growth in the US Division and low-teens sales growth in the International and China Divisions. I also assume gradual margin expansion with EBIT margins plateauing in the upper-teens. This generates a value of over $80 per share.
• On the downside, I aggressively assume loss of market share and margin declines in the US Division and no growth in the International and China Divisions. This generates a value of roughly $34 per share.
• Applying probabilities to these upside and downside scenarios generates an intrinsic value estimation in the low $70s. With the stock at a recent $66, this represents a mere 15% discount to intrinsic value. The Cavalier Fund currently owns YUM at an average cost of $59, representing an 11% unrealized gain since inception. Still, the stock’s current valuation fails to capture the potential for fundamental improvement and growth.

For questions, comments, or to view the full report, please contact Greg McCullough at McCulloughG08@darden.virginia.edu

The Advisor
Investment thesis
Toro is a mid size specialty player (Golf Course/Turf Management) in the Farm Machinery/Heavy trucks industry within the Industrials Sector. Toro’s mission is to help professionals and homeowners create and maintain beautiful outdoor spaces. TTC is focused on finding better ways to care for these landscapes in an environmentally friendly manner.

Toro’s operational focus is ‘growing lean’ with two key objectives: continuous improvement and to continue to foster an innovative corporate culture. In its quest for this balance TTC has grown their R&D by 11.6% in each of the last 4 years, while keeping total SG&A growth below revenue growth.

International sales accounted for 21% of total 2004 sales topping 27% in 2006 with an eye on 30% of total sales going forward. This increased international expansion not only increases Toro’s global penetration, but also provides the company with ‘weather diversification.’

The professional segment (67% of sales) is expanding; in 2006 Toro realized almost 7% revenue growth in golf, sports fields & grounds, landscape contractor and ag markets. This segment typically has a quicker ‘return buyer rate’ as the equipment is required for every day use. Golf courses in particular are extremely brand loyal when it comes to their grooming equipment.

If Toro is able to continue to innovate and expand their product offering while focusing on further international penetration with the same margin discipline they have exercised in the past then they will continue to clip the competition.

Investment Considerations
• Toro operates in a cyclical industry, and is far from the ‘biggest player’ in the market. Therefore, the cost of continued innovation could outpace revenue growth with a pull back in sales due to recession etc.
• As mentioned above, due to the nature of being in the ‘nature business’ Toro is subject to weather risk in the different regions and countries it operates in. Seasonal catastrophes could negatively impact sales for an entire year.
• Continued contraction in the residential market due to broader competition.
• Reassessment by larger competitors (i.e. Deere) with the capital and the patience to make a more focused push to take market share from TTC.

Valuation
• On the upside of a discounted cash flow analysis, I assumed 6% revenue growth throughout the next 5 years, while maintaining conservative average margins. Using a weighted average cost of capital of 10.7% and a terminal value of 10.75x EBIT I arrive at a value of over $72 per share.
• On the downside, I assume declining annual sales and narrowing margins over the same forecast period. This generates a value of approximately $41 per share.
• Looking at how TTC historically trades on a forward PE basis and comparing that with the DCF values we arrive at a weighted upside target price of above $68 and a weighted downside price of approximately $43. With the stock at approximately $51 as of the May 2nd pitch this represented a 33% discount to intrinsic value. With the upside favoring the downside by almost 3 to 1 the Jefferson fund chose to begin building a position in Toro.

For questions, comments, or to view the full report, please contact Michael Mussio at: MussioM08@darden.virginia.edu

Michael Mussio
Toro Company
May 21, 2007
Fund News

**Monticello Fund**

**Managers**
- Sr. Portfolio Manager: Ed Duggan
- Portfolio Manager: Danny Mooney
- Portfolio Manager: Edward Shim
- Portfolio Manager: Maureen Singer

**Performance vs. Benchmark**

![Cumulative Return Since April 1, 2007](chart)

**Investment Strategy**

The Monticello Fund uses fundamental analysis to identify and invest in companies that are well positioned for growth but inexpensively valued.

**Fund Holdings**

- AIG Corporation
- Berkshire Hathaway “B”
- CBS Corporation
- Devon Energy
- Genentech
- IBM
- Kellogg
- Newmont Mining
- Patterson Companies
- Target
- Wyeth

*Through 5/31/2007

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**Cavalier Fund**

**Managers**
- Sr. Portfolio Manager: Richard Bodzy
- Portfolio Manager: Robert Birdsey
- Portfolio Manager: Chris Delaney
- Portfolio Manager: Greg McCullough

**Performance vs. Benchmark**

![Cumulative Return Since April 1, 2007](chart)

**Investment Strategy**

The Cavalier Fund is a long / short equity hedge fund that focuses primarily on domestic equities including small, mid- and large capitalization companies.

**Fund Holdings**

- Microsoft
- Monsanto
- Unicore
- Verbatim
- Rent-A-Center
- VeriSign
- Wellcare Health Plans
- VCA Antech
- Pre-paid Legal Services
- iShare S&P 500 index

*Through 5/31/2007*
Darden Fund

Managers
Sr. Portfolio Manager Jeff Sutton
Portfolio Manager George Gao
Portfolio Manager Matthew Jackson
Portfolio Manager Neil Kansari

Investment Strategy
The Darden Fund is a small-cap fund that seeks to maximize returns through disciplined fundamental research and analysis. The benchmark for the fund is the S&P 600.

Performance vs. Benchmark

*Through 5/31/2007

Fund Holdings
Aldila, Inc.
America’s Car Mart
Clean Harbors, Inc.
Corrections Corp. of America
Delphi Financial Group Inc. (Class A)
Encor Group, Inc.
Equity One
FTI Consulting
Gardner Denver
Great Atlantic & Pacific Tea Co.
iShare S&P Small Cap 600 Index
Mueller Water Product, Inc. B
Netflix
New Frontier Media
Orchid Cellmark
Texas Capital Bancshares
Thom Industries
THQ
Taleo
TravelCenters of America, Inc.
Walser Industries, Inc.

*Through 5/31/2007

Jefferson Fund

Managers
Sr. Portfolio Manager Michael Mussio
Portfolio Manager Divyaksh Kapur
Portfolio Manager Tad Lehmann
Portfolio Manager Eric Logue

Investment Strategy
The Jefferson Fund seeks to generate excess returns through a value-based strategy with a concentration on companies with market capitalizations between $200 million and $5 billion.

Performance vs. Benchmark

*Through 5/31/2007

Fund Holdings
Anheuser Busch
Bank of America
Chevron
Chesapeake Energy
Chiquita Brands
FPIC Insurance
General Dynamics
Hanesbrands
Hospira
Ishare Russell 1000 Index
JP Morgan Chase
Nokia Corp ADR
Pengrowth Energy Trust
Pensmart
Pfizer
Pulte Homes
TEVA
Toro
Travelcenters of America
United Fire & Casualty
Unitedhealth Group
Verizon Communications

*Through 5/31/2007

THE ADVISOR

The Advisor is a publication of the Darden Capital Management Club at the University of Virginia’s Darden School of Business.

Darden Capital Management operates four student-run investment funds for the Darden School Foundation with approximately $6 million in assets under management.

To learn more about Darden Capital Management and the Darden School of Business, please visit:

http://student.darden.virginia.edu/dcm
http://www.darden.edu

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