THE DARDEN CAPITAL MANAGEMENT ADVISOR

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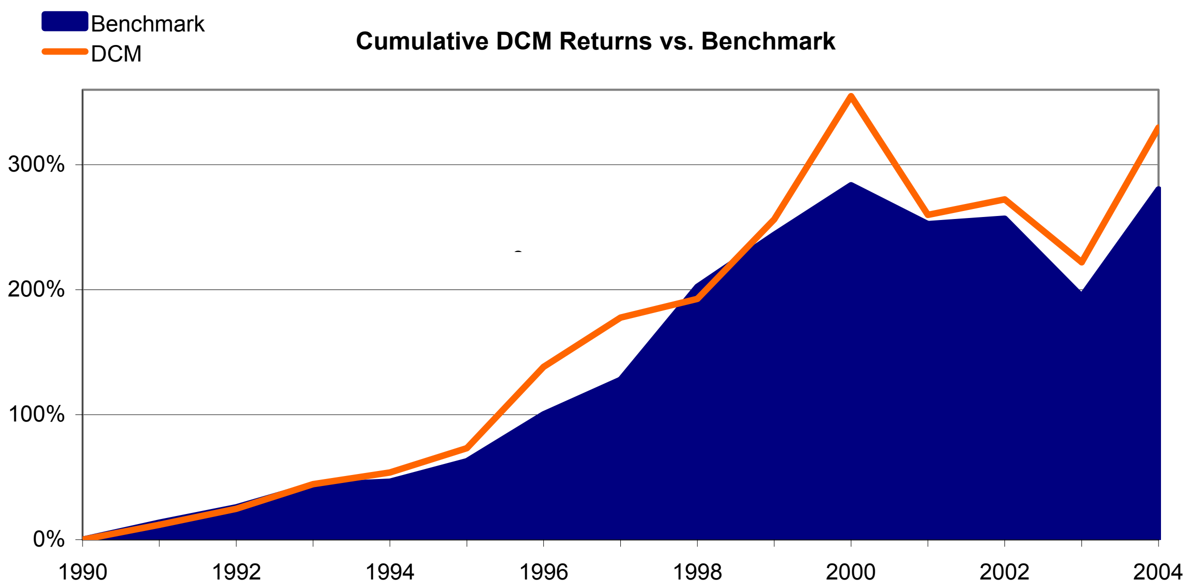
Darden Capital Management Posts Extraordinary Long-Term Returns

By Peter Goulding, David Briggs, and Ben Monson

Since its inception in 1990, Darden Capital Management (DCM) has delivered extraordinarily strong performance. DCM's average annual total return over its 14 year history is 12.1%—a cumulative 14-year total return of 330%. DCM's benchmark index returned an annual average of 10.8% and a cumulative 280% over the same period. DCM outperformed the benchmark in 11 of 14 years, and on average DCM exceeded the index by 1.3% per year. The following chart shows DCM's cumulative performance since inception vs. the benchmark.



Benchmark = 60% S&P 500 TR - 40% LEH Interm. Gvt.-Corp. TR Until 2001; 80% - 20% Thereafter

Darden Capital Management's best year of performance was 1996, when the club posted a 38% total return, exceeding the benchmark index by 14 percentage points. DCM's best year of relative performance was 2000, when the club's total return of 28% exceeded the benchmark by 16 percentage points. The club's worst year of performance relative to the index was 1998, when the index increased 33% and DCM posted a total return of only 5%. In addition, DCM's relative performance trend has improved over time, as evidenced by the table on the right.

Based on returns, Darden Capital Management would likely place among the top half of professional investment managers with similar goals, and likely in the top tier.

CUMULATIVE	
DCM +/- Benchmark* Cumulative	49.5%
Arithmetic Average DCM +/- Benchmark*	1.3%
Compound DCM +/- Benchmark*	1.0%
LAST FIVE YEARS	
DCM +/- Benchmark* Last 5 Years, Cumulative	10.0%
Arithmetic Average DCM +/- Benchmark*	2.8%
Compound DCM +/- Benchmark*	1.8%
LAST THREE YEARS	
DCM +/- Benchmark* Last 3 Years, Cumulative	11.5%
Arithmetic Average DCM +/- Benchmark*	3.5%
Compound DCM +/- Benchmark*	3.5%
LAST YEAR	
DCM +/- Benchmark*	4.3%

This article was developed based on research and a report compiled primarily by Peter Goulding ('05) and David Briggs ('05) for the Darden School Foundation Board of Trustees, which oversees Darden Capital Management.

Darden School Foundation Boosts DCM's Funds Under Management to $3 Million

By Tyler Lifton ('05), from the Cold Call Chronicle

Christmas in April came early this year for Darden Capital Management as the Darden School Foundation surprised the money managers with a $700,000 infusion, upping the amount of funds at their discretion to $3 million. DCM's money will be equally distributed among the Darden, Monticello and Jefferson funds.

With the increase, Darden now ranks fourth among business schools in terms of assets under management. Impressively, Darden Capital Management's capital base is nearly three times the combined total of rivals Wharton, Kellogg, Tuck, and Stanford. The increase represents quite a boon in the competitive world of asset management. In addition to providing asset management services to the endowment, DCM is an important asset for Darden to attract perspective students interested in careers in money management.

"The recent decision of the trustees to increase the amount of money under student management… serves as a powerful signal, rewarding both excellence in past performance and student dedication and investment discipline," said Yiorgos Allayannis, finance professor and faculty advisor to DCM. He added that the increased commitment "paves the way for an even stronger and more credible program."

John Macfarlane ('79), Managing Director and Chief Operating Officer of Tudor Investment Corp. and head of the investment committee for the Foundation, wrote in an email to the Cold Call Chronicle that increasing the capital "was appropriate given the quality and importance of the program to Darden and to its students."

Since its inception in 1990, DCM has cumulatively outperformed its benchmark by 49.5%, net of fees and expenses, and the fund's annual outperformance is trending higher, averaging 1.3% since inception, 2.8% over the past five years and 3.5% over the last three years.

DCM Fund Managers Trek to Omaha for Berkshire Hathaway Annual Meeting

By Steven Majocha

On Saturday, May 1st Berkshire Hathaway's Annual Shareholders Meeting took place in Omaha, Nebraska. Approximately 20,000 Berkshire Hathaway shareholders and Warren Buffet enthusiasts came from all over the country to listen and learn from the "Oracle of Omaha." Darden Capital Management fund managers David Briggs ('04), Josh Goldstein ('04), Joao Mariano Rotta ('04), and Steven Majocha ('05), and Akash Raj ('04) were fortunate enough to attend the shareholders meeting and enjoy the festivities over the weekend.

Photo: Josh Goldstein, Steven Majocha, and David Briggs

In order to be admitted to the meeting, attendees must be a shareholder of Berkshire Hathaway. All three of DCM funds have held Berkshire Hathaway Class B stock over the years. The five DCM members were able to attend the meeting this year because of the overwhelming generosity of Darden Alumnus Bruce Lauritzen. Mr. Lauritzen is currently the chairman of First National Bank and also a community leader in Omaha.

The highlight of the weekend was Saturday's Shareholders Meeting. For over five hours, Warren Buffet and partner Charlie Munger answered any and all questions from investors about Berkshire Hathaway, their investment philosophy, and broader issues with the patience and humor that is unique to the two legendary investors. The general consensus from the group can be summed up by first year student Steven Majocha, "Attending the shareholder's meeting was both educational and enjoyable, and I believe the lessons learned from the meeting will be indispensable in managing a DCM portfolio and in my career in the future."

May 2004 Investment Ideas

Oshkosh Truck Corporation (OSK—$53.45)

Joe Burkhart, '05
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Target Price: $70.00
Market Capitalization: $1.9 Bil.

Description: Oshkosh is a designer, manufacturer, and marketer of a range of specialty trucks and truck bodies, including concrete mixers, garbage trucks, fire and emergency vehicles, and defense trucks.

Positive Considerations: Beginning in FY96, Oshkosh embarked on a strategic initiative aimed at shedding underperforming assets and diversifying its existing product line. Following a series of acquisitions and efficiency initiatives, sales and earnings have posted compound annual growth rates (CAGR) of 29% and 24%, respectively, through the end of FY 03.

Oshkosh currently has over 6,500 vehicles in Iraq dedicated to the delivery of supplies and equipment to coalition troops. These vehicles on average put on a year's worth of designed mileage every month and Oshkosh will benefit from refurbishment contracts with the military.

Oshkosh's commercial segment will benefit from the Federal Highway Bill and the US's continued economic recovery. The company's next generation concrete truck is scheduled for release this summer and the company has received strong indications of interest from the market.

Risks: Declining municipal tax receipts and tighter budgets could depress demand for Oshkosh's fire & emergency and refuse collection products.

Valuation: Our price target of $70 is based on DCF, takes into account market growth, and is supported by applying a comparable P/E to Oshkosh's forward earnings.

Marvel Enterprises (MVL—$21.50)

Ben Monson, '05
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Target Price: $25.00
Market Capitalization: $2.1 Bil.

Description: Marvel Enterprises is one of the world's foremost character-based entertainment companies with a portfolio of 4,700 characters developed over 60+ years. These iconic characters include Spiderman, X-Men, The Hulk, and The Punisher. The company derives its revenues from (a) intellectual property licensing for movies, TV, video games, toys, etc., (b) comic book publishing, and (c) limited toy manufacturing.

Positive Considerations:

Restructuring: The company has restructured itself from primarily a toy manufacturer (high-cap ex, low margin) to a licenser of patents (low cap ex, high margin).

R&D: MVL develops its characters through its profitable comic book publishing business—which essentially serves as free R&D.

Licensing: The company is driving its substantial revenue and profit growth—which will ultimately drive share price appreciation— through licensing its intellectual property. The company is capturing an increasingly large piece of the financial pie from its projects. Licensing revenues increased from $40 million in 2001 to $189 million in 2003. The company's pipeline of projects through 2005 is strong.

Risks: Shifting consumer preference, dependence on success in other media, lumpy earnings stream.

Valuation: MVL shares trade at a discount to peers (on a P/E and EV/EBITDA basis), and our target price of $25 is based on multiples of 14x and 25x 2005 EV/EBITDA and P/E, respectively.

Orthodontic Centers of America (OCA—$7.46)
Jonathan Right, '05
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Target Price: $12.50
Market Capitalization: $374 Mil.

Description: Orthodontic Centers of America (1) provides integrated business services to orthodontic and pediatric dental practices and (2) develops orthodontic centers and manages the business operations and marketing aspects of the affiliated orthodontists' practices.

Positive Considerations: With 75% of payments made by the patient (and only 10-25% covered by insurance), orthodontics services are considered a discretionary expense. The company was adversely impacted by the recession, rising unemployment, and bankruptcies. Employment trends are positive and bankruptcies are beginning to fall.

Risks: Litigation risks are overstated. Analysts that are negative on the stock cite the uncertainties involving current and future litigation. Downside risk testing mitigates fears of a blowup, and OCA does not record revenues for non-performing or litigating affiliates. If anything, there is significant upside when OCA wins the suits.

Valuation: OCA shares are attractively priced, trading below 8.5x FY1 EPS, 0.76x book value, and at 4.2x EBITDA. We view the current valuation as underpriced for a firm with high historical growth and strong prospects for the future. Further, a DCF analysis based on (1) analyst expectations for 2004/05 for revenue, EBITDA, and EPS, (2) moderate growth beyond 2005, and (3) little multiple expansion prices the company at more than $11.50. Comparable company analysis shows dramatic undervaluation based both on health services providers and business service outsourcers.

DIMON Incorporated (DMN—$7.39)
Ben Monson, '05
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Target Price: $9.25
Market Capitalization: $330 Mil.

Description: DIMON Inc. is the world's second largest wholesaler of leaf tobacco. The company buys tobacco in 30 countries, processes and blends it, and supplies major tobacco companies. Tobacco wholesaling is a mature, commodity business. DIMON adds value by managing a complex global supply chain for customers, produces solid free cash flow, and appears undervalued.

Positive Considerations: Tobacco use is falling in developed markets, but rising in emerging markets. Large tobacco companies—DIMON's customers—are gaining market share. Generally, tobacco wholesalers have not been the target of major lawsuits brought by smokers or governments. Global supply and demand for leaf tobacco is generally in balance, and while prices will continue to decline over time, wide swings in pricing are unlikely.

DIMON is positioned to perform decently notwithstanding some near-term operational issues. The company has the largest or second largest market share in the U.S., China, Brazil, Mexico, Turkey, and several other countries. Dimon has been challenged by political problems in Zimbabwe and the weakness of the dollar. DIMON's revenues are mainly in dollars and many of its cost are in local currencies, hurting the company's results.

Risks: We can identify no obvious catalyst for the stock. Currency risk. Litigation risk.

Valuation: Our price target of $9.25 is based on a DCF analysis, a price/book multiple of 0.9x, and a 7x FCF multiple. The stock is currently trading at a 0.7x P/Bk.

REINSURANCE INDUSTRY

The Reinsurance Industry
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Industry Overview: Reinsurance underwrites and spreads risk for insurance companies. Reinsurers make money through (a) underwriting and appropriate pricing of risk; (b) managing assets/the "float".

Underwriting: A key to success in underwriting is appropriately pricing risk. Pricing cycles—especially in property/casualty and catastrophe reinsurance—tend to make this difficult over the long term. Reinsurers often have to make pay-outs on policies in the wake of disasters, but they also gain pricing power. As these events fade into the past, typically the reinsurance industry's pricing discipline deteriorates as competition heats up, resulting in less economic pricing of risk. This cycle has repeatedly led to underwriting losses in the past, and pricing is currently softening.

Asset Management: Reinsurance can be a great business because cash is collected *now* and claims *may* have to be paid at some unknown future date. This creates a pool of cash—"The Float"—that reinsurers can invest. Prudent and innovative asset management sets better-performing reinsurers apart from peers. If a reinsurer can break even in its underwriting operations, then "The Float" acts like a loan with no set maturity and no interest payments.

Stock Picks: Given a moderately soft pricing environment and fair valuations, we have identified two Bermuda-based companies that appear attractive. **PXRE Group (PXT)** focuses solely on catastrophe reinsurance is looks attractively valued. **Max Re (MXRE)** has an interesting investment strategy, allocating 35% of its float to hedge funds. DCM owns **Berkshire Hathaway (BRKb)**.

j2 Global Communications

J2 Global Communications (JCOM—$22.50)
Tyler Jayroe, '05
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Target Price: $35.00
Market Capitalization: $500 Mil.

Description: JCOM provides outsourced messaging and communications services to individuals and businesses. Services offered include: faxing and voicemail solutions, document management solutions, Web-initiated conference calling, and unified messaging services.

Positive Considerations: JCOM is a financially healthy, cash-generating growth machine with strong competitive advantages in its markets. Pre-tax earnings are expected to grow 60% this year due to strong revenue growth (40%) and extraordinary operating margins (44%).

The market opportunity is huge. The company says that a 2001 study approximated domestic fax services market at $80 billion. Competition is weak and barriers to entry are strong in the form of JCOM patents and its large customer base. Microsoft has announced plans to include JCOM products in its XP operating system. Insider ownership = 25%.

Risks: Earnings will soon be reported on a fully-taxed basis, hurting year over year comparisons. Shares are highly volatile and have a high short interest. Company cites "managing high growth" as biggest threat to business.

Valuation: JCOM's PE of 16 (TTM) is below the peer group multiple of 17X. Stock is also cheap relative to long-term growth expectations with a PEG ratio of 0.54. Applying a multiple in-line with JCOM's growth prospects and market position results in a 12-month target price of $35

Lafarge North America (LAF—$42.50)
Ben Monson, '05
Steven Majocha, '05
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Target Price: $52.00
Market Capitalization: $3.1 Bil.

Description: Lafarge North America is the largest producer of cement in North America, with strong positions in ancillary businesses such as aggregates, gypsum wallboard, and related services.

Positive Considerations:

Highway and government-related projects drive 50% of Lafarge's sales, and we believe that a $250-$300 billion highway bill will be enacted within six months.

Commercial construction projects account for 25% of sales, and we believe that commercial construction is rebounding from recession-driven lows. U.S. cement price increases over the past six months support this.

Residential construction drives 17% of sales. While we are positive on the long-term outlook for residential construction, we believe that a near term slowdown is possible.

Within this context, Lafarge is positioned exceptionally well, especially in cement. Lafarge's relatively new gypsum wallboard business became profitable in 3Q03.

Risks: Pension liabilities, 54% ownership of Lafarge SA, a slowdown in commercial, government, or residential construction.

Valuation: Our price target is based on a 13x 2005 P/E multiple and a price/book value multiple of 1.4x. At our price target, Lafarge would still trade at a discount to current comps.

eResearch Technology, Inc. (ERES—$32)
Tyler Jayroe, '05
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Target Price: $42.00
Market Capitalization: $1.1 Mil.

Description: eResearch Technology provides technology and services that enable the pharmaceutical, biotechnology and medical device industries to collect, interpret and distribute cardiac safety and clinical data more efficiently. The company provides centralized electrocardiographic services and technology that streamline the clinical trials process by enabling customers to evolve from traditional, paper-based methods to electronic processing that leverages the power of the Internet.

Positive Considerations: The FDA is strongly encouraging all compounds seeking approval to conduct cardiac testing. As the dominant CRO in this market, ERES is capitalizing on the growing demand for its services.

The company is debt-free and generates strong free cash flow, some of which it intends to use to buy back shares. Backlog is strong, providing substantial visibility through the next 18 months. Company has a consistent history of upside earnings surprises.

Risks: Shares are highly volatile and have a small float, which should improve following recently announced 3:2 stock split. Insider selling has been significant over the past year but insiders still hold 16% of shares.

Valuation: ERES trades at 26x forward earnings, which is a discount to its long-term growth rate, resulting in a PEG of 0.89. Applying a multiple in-line with ERES's growth prospects and market position results in a 12-month target price of $42.

Hain Celestial Group, Inc. (HAIN—$17.47)
W. Blair Farinholt, '05
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Target Price: $24.00
Market Capitalization: $618 Mil.

Description: The Hain Celestial Group, Inc. is based in Melville, NY and is the nation's largest manufacturer of natural foods. The Company manufactures, markets, distributes and sells natural, organic, specialty and snack food products under brand names that are sold as better-for-you products.

Positive Considerations: Natural/organic food and beverage is the fastest growing segment of the Healthy Lifestyles industry. Sales growth in this category is benefiting from escalating food safety concerns, declining prices, and an increasingly favorable regulatory environment. Despite its rapid growth over the past decade, the natural/organic food and beverage segment comprises just 2% of America's total food bill. This penetration rate underscores significant untapped distribution opportunities, particularly in the mass market, in our opinion.

Hain is currently trading at 12.7x EBITDA. Please note that an average acquisition multiple of 16x EBITDA gives Hain a 26% premium to current market valuation.

Hain's aggressive new product effort includes a major push into the low-carb category. The "CarbFit" launch includes 45 products in the snack, pasta, and cookie categories. There have been positive sales trends concerning this recent launch.

Risks: A domestic shortage has pushed soybean prices above $10 a bushel, twice the level of just seven months ago. It is likely that this increase in variable costs will be pushed down to the consumer.

Valuation: Historical average forward P/E has been 22x; HAIN currently trades around 18x forward projections. Due to its recent volatility, a discount to previous multiples is warranted.

Anheuser Busch Companies (BUD—$51)
Steven Majocha, 05'
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Target Price: $59.00
Market Capitalization: $41 Bil.

Description: Anheuser-Busch is the No. 1 domestic beer producer and marketer and operates four major business units: domestic, international, packaging, and entertainment.

Positive Considerations: Pricing Power—BUD is an attractive investment in both a raising interest rate and inflationary environment due to its ability to raise prices on it products.

BUD has now achieved 22 consecutive quarters of double-digit earnings per share growth.

Industry leading margins (5% better than Miller and Coors), superior returns on equity and invested capital. For example, ROE (ttm) is 79.19% and ROIC is 18.8%.

Low correlation to the overall market. Bud represents a solid defensive play as a result of its non-cyclical business.

BUD announced that it had bought 29% of Harbin Brewery Group (China's 4th largest beer brewery). This acquisition could be in jeopardy due to a hostile bid by SABMiller.

Risks: Beer industry volume is projected to grow at a modest 0.7-1.0% annual rate between now and 2010.

Life Style Changes: Low carb diet craze (Atkins, South Beach) has the potential to shift consumer preferences from beer to other alcoholic beverages.

Valuation: BUD currently trades at 16.7x forward estimates, which is a discount to the overall market. Based on conservative estimates, a DCF analysis yielded a $59 price target.

American Standard, Inc. (ASD—$105.70)
Brian Maguire, '05
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Target Price: $120
Market Capitalization: $7.57 Bil.

Description: American standard is one of the largest providers of goods in each of its three product categories: air conditioning systems, bathroom and kitchen fixtures, and vehicle control systems.

Positive Considerations: Future cost savings can be expected due to investments made in 4Q03 to streamline investments and implant six-sigma initiatives. Management expects to save $30MM in '04 and $36MM from '05 on.

ASD's share price does not reflect its solid cash flow due to concerns over its North American Commercial Air Conditioning sales, which decreased 7% in 2003 on top of 10% declines in 2002 and 2001. Many of their customers' units have a lifespan of 30 years and date back to the 1970's, thus are due for replacement. I believe that customers have been delaying expenditure on replacement systems until they are sure of the economic recovery in North America.

With FCF/diluted shares of $6.10 they have solid cash flows. They are using $2/3^{rds}$ of their cash flow to reduce its debt load and the remaining $1/3^{rd}$ to repurchase shares.

Risks: Raw materials prices have risen as commodity prices in general are swelling. These cost increases manifested themselves as COGS as a % of Sales rose from 72.1% in 2001 to 73.1% in 2002 and 73.7% in 2003.

Valuation: ASD trades at 16x estimated '04 EPS, compared to the 18x '04 earnings that the S&P 500 trades at. At earnings ASD would trade at around $120 a share. DCF supports a price range of $119 - $130.

Polymedica, Corp. (PLMD—$27.61)
Ryan Walsh, '05
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Target Price: $34.00
Market Capitalization: $844 Mil.

Description: PLMD is national medical products and services company. PLMD operates three business segments: Liberty Diabetes (~70% revenues) is the most significant and provides direct-to-consumer diabetes and respiratory products/services through television advertising to seniors. PLMD's pharmaceutical business provides oral medications and urological products.

Positive Considerations: PLMD is the category leader in the diabetic medical supplies market. Liberty's strong brand name is supported with effective national television advertising. PLMD commands 8.6% of the senior market and competes with much smaller, privately-held direct-to-consumer firms.

Benefits from favorable demographic trends: 17 million people in the U.S. suffer from diabetes—a population expected to reach 23 million by 2010. Medicare has increased focus on preventive care and is expected to allocate more money for testing procedures.

PLMD has a strong balance sheet with minimal debt, providing financial flexibility for possible acquisitions or investments in brand building.

Risks: The Department of Justice is investigating PLMD on Medicare billing and prescription fulfillment practices. PLMD faces a potential cash payment of up to $17.7 million. Medicare's long-term reimbursement rate may change.

Valuation: Based upon estimated FY 2005 EPS of $2.00 and a 17x target PE ratio, PLMD's 12-month intrinsic value is $34 per share. Comparable health-care firms trade at a much higher premium than PMLD.