REPRINTED FROM JUNE 3, 2019

THE WALL STREET TRANSCRIPT
Connecting Market Leaders with Investors

Buying High-Quality Businesses That Aren't on Wall Street's Radar

ST. DENIS VILLERE III is Partner/Portfolio Manager at Villere & Co. He joined the firm in 1999 to launch and manage Villere's first mutual fund. He started his career as an institutional research analyst and equity sellside analyst with Gerard Klauer Mattison, a Wall Street institutional equity research firm. He received a degree in finance from Southern Methodist University. He is a member of the CFA Institute. Mr. Villere has been frequently quoted by *The Wall Street Journal*, Associated Press and Reuters. He is a regular guest on CNBC and other financial media outlets. Mr. Villere dedicates much of his personal time to New Orleans charities. As President of Carrollton Boosters, he oversees 5,000 players in youth baseball, softball, basketball, soccer, flag football and lacrosse. He is the former Board Chairman of Trinity Episcopal School. He also serves on the board of Pro Bono Publico Foundation, helping the organization raise $1 million for New Orleans charter schools every year. In 2004, he was a co-founding trustee of Choice Foundation where he served as Treasurer. Mr. Villere is married with three children.

SECTOR — GENERAL INVESTING

TWST: Could you tell me a little bit about the firm and your title there?

Mr. Villere: Sure. I'm one of the partners and portfolio managers. And we're a fourth-generation money manager. Our firm was founded in 1911 by my great-grandfather.

TWST: Is there a distinct investment philosophy?

Mr. Villere: Yes, we generally focus on small- and mid-cap stocks that are basically growth at a reasonable price. We love companies that have very low debt relative to their cash flow characteristics and love to find companies with low price to earnings relative to their growth. We're always looking for names that are a little bit off Wall Street's radar screens. High-quality companies that dominate a niche, but maybe the rest of Wall Street doesn't quite know about them yet. We are also more concentrated, with high-conviction positions, in the 20- to 30-holdings range.

TWST: Why might investors be interested in reaching out to a firm like yours, which has been in the same family for a while?

Mr. Villere: We are ingrained in our community, and we're ingrained in our clients' lives. And so I think there's a trust factor that we definitely take for granted — that we keep hearing from clients that there's implicit trust and that we're always looking out for their very best interests.

TWST: And did you want to highlight a stock that you find interesting?

Mr. Villere: Yes, one of the names that we like a lot here is a company called **Roper Technologies** (NYSE:ROP). It is a little bit larger than we typically buy, but we were able to add it to the portfolio in December of 2018.. Roper is a highly acquisitive company with a focus on running and buying niche-focused, asset-light businesses, including technology-oriented companies that are very high in gross margins, about 63%. Roper also focuses on businesses with sizable competitive advantages, strong market positions, and decent growth opportunities.

It has high EBITDA margins, about 35%. And about 50% of their revenues have been recurring in nature, which we really like. They use the cash flow that these businesses produce, and they continue to make more and more acquisitions. And it's one that I think is going to work out well and can be held for our time frame, which is at least three to five years.

TWST: Is there something particularly interesting for investors that's on the company's horizon? You mentioned acquisitions. Is that something that they might continue with?

Mr. Villere: Yes. Technically, the future acquisitions never get baked into the valuation. So it always seems a little bit more expensive than it really is. They just continue to do these acquisitions that continue to tack on these very asset-light companies that really do not require a lot of capital expenditure — capex — investment. And so just the cash flow characteristics are so attractive that the company as a whole should continue to perform quite well.

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TWST: And when these acquisitions take place, the companies find efficiency within the framework of the existing company?

Mr. Villere: That's exactly right. They can rightsize the businesses, and they can find other efficiencies to make them extremely efficient. They do a great job of tacking on these businesses and also streamlining them — just making them run even more solid than they were prior to acquisition.

TWST: Is Roper in a lot of different fields?

Mr. Villere: They have about 50 companies right now. And while they are in many fields, all the companies that they acquire have similar characteristics, which again are very high, high margin and very high recurring revenue type of businesses and very capex light.

TWST: And although it's in broad and diverse fields, how does the company make sure that they head in the right direction with that kind of diversity? Some companies like to keep a narrow focus, and this one sounds like it's looking for a broader focus.

Highlights

St. Denis Villere III discusses Villere & Co. He looks for growth at a reasonable price in small-cap and midcap stocks. Mr. Villere likes to find high-quality companies that are off of Wall Street's radar screens. He wants to hold stocks for at least a three- to five-year time frame. According to Mr. Villere, volatility is here to stay. He uses volatility as a friend, rather than an enemy.

Companies discussed: Roper Technologies (NYSE:ROP); Cypress Semiconductor Corporation (NASDAQ:CY); Silicon Laboratories (NASDAQ:SLAB); Teleflex Incorporated (NYSE:TFX) and LKQ Corporation (NASDAQ:LKQ).

1-Year Daily Chart of Roper Technologies

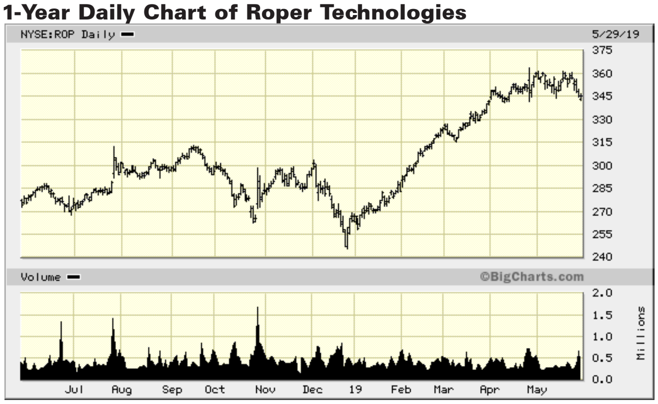

Chart provided by www.BigCharts.com

Mr. Villere: Yes, I think not unlike what we do, with having a very strict investment criteria and the companies that we invest in, they've got the same thing. Maybe they're more technology-oriented, but they're all businesses that share the same characteristics so that they can get the diversification that they want but also have the high cash flow characteristics that they look for. Their track record has been so successful that it gives us confidence that they're going to continue to find these great businesses in the future.

TWST: Did you want to mention a second company?

Mr. Villere: Another business I like is a company called **Cypress Semiconductor** (NASDAQ:CY). This is a bit smaller, about a $5.5 billion market cap. They really fly under the radar. They trade at about 14 times earnings. Competitors trade at about 20 times earnings.

These guys have a leading position in the internet of things. And it is also a great play on the increasing volumes of electrical vehicles. About 25% of their revenue right now is internet of things. It's growing quite rapidly, over 40% in 2018. Basically, the internet of things gives you the ability to be connected. For instance, when your alarm goes off in the morning, your coffee maker starts, and those types of things.

To compare, one of the pure-play internet of things companies, **Silicon Labs** (NASDAQ:SLAB), derives about 60% of their revenue from that area. And they trade at about a 27 multiple. So we think there's plenty of room for **Cypress** to get their multiple expanded over time as they get more credit for that business.

TWST: Is the internet of things something that's going to be growing? It's here now, but it's certainly going to be growing in the immediate future?

Mr. Villere: Yes, when you look at some of their customers, they supply Amazon Echo. For example, they supply Nintendo Switch, the newly launched Apple HomePod. Things like this I think aren't going anywhere and should continue to do quite well. I think internet of things is not only here to stay, but I think it's a trend that's going to be extremely popular going forward.

TWST: And it will affect both businesses and households?

Mr. Villere: Yes. I think there's going to be not only households, residential, but also commercial. As time goes on, I can see more and more things being connected, interwoven. And I think that's where **Cypress** is going to have a key play.

TWST: Did you want to mention another company?

Mr. Villere: Another company we like is a company called

Teleflex (NYSE:TFX). It's a little bit larger, about a $13.5 billion market cap. These guys were founded back in 1943. And they're really a pure-play medical device company. We love the trends. Right now, in health care, in general, you've got 10,000 people turning 65 in the U.S. every single day.

These guys also have an incredible track record of making acquisitions and improving their margins over time. They finished 2018 with 57.1% gross margins, and that's up about 130 basis points from 55.8% in 2017. They've got an incredible, quickly growing area in interventional urology, growing almost 19% year over year. This is from one of their products in the enlarged prostate area, or BPH, as they call it. It's called UroLift. And that continues to do quite well with an aging population.

So right now, it trades at about 27 times non-GAAP earnings per share. But this is versus their med-tech peers — that is as high as 41 times earnings. We still think it's a little bit undervalued versus its peer group and one that you can really hold on to, again, over the three to five years and should do quite well with it.

TWST: And one of the things about medical devices is there's a global need for a lot of these things. You're not just competing in one market.

Mr. Villere: Yes, that's right. **Teleflex** is also very diversified. And they can find the areas that are doing well and growing rapidly and make acquisitions, and then also digest them and do everything they need to do to make it more efficient and improve margins, etc. I think these guys have a great history and track record of doing that, and we look forward to them continuing to do that.

1-Year Daily Chart of Teleflex Incorporated

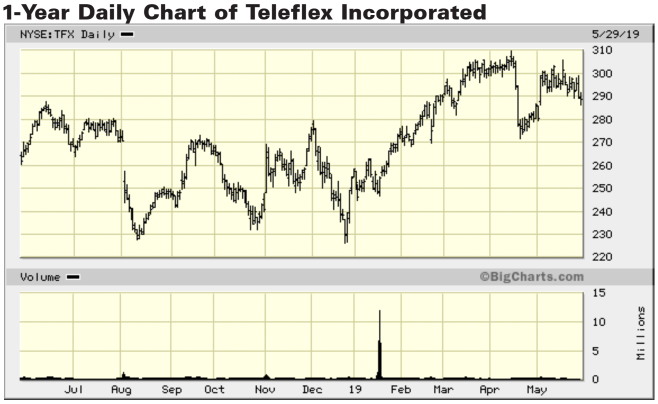

Chart provided by www.BigCharts.com

TWST: Did you want to mention one final company?

Mr. Villere: There's another business called **LKQ** (NASDAQ:LKQ). It's a common term for like, kind and quality. They're basically supplying refurbished and recycled auto parts to mostly body shops that are the same as new or OEM parts, but they're about 20% to 50% cheaper. They've been under a little bit of pressure. They had a weaker quarter. And I think that creates the opportunity.

"We're going to use volatility as our friend, not our enemy. And we're going to be able to pick up high-quality businesses that sell off for reasons that don't make any sense to us."

They're just finalizing an acquisition of something called **Stahlgruber**, which is the leading aftermarket parts distributor in Germany. And at their most recent analyst day, they talked about trying to improve margins, and they think they can improve their EBITDA margins about 500 basis points over the next 36 months. It also trades much cheaper than its peer group — down at almost 13 times numbers when you look at some of their peers that trade closer to 18 to 19 times.

It's just a key part of an insurance company's business, and they are able to replace and fix your car with an exact like-in-kind part, but a much, much cheaper part, so one that I think is going to still work out well. And it is still very cheap.

TWST: And in a lot of the world, given the price of automobiles, a lot of people are looking to repair the vehicles they've got and keep them longer. Would that help a company like this?

Mr. Villere: Yes. The higher the age of the vehicles are, in the U.S. and globally, the better these guys will do. They also benefit from accidents. Weather can control their destiny to some extent. But it's one of these businesses that you literally cannot replicate. They're like vultures, where they pick over the scrap, and they can price your car, and they can turn around and sell these refurbished and recycled parts, and a business that you just cannot replicate. We also love the huge barriers to entry in the business.

TWST: Changing direction, when you talk with your clients, what are some of their concerns, especially after the last quarter of last year? What are some of the topics that come up as they look to the rest of this year and into next year?

Mr. Villere: I think the key is that volatility is probably here to stay. And if we're going to get some volatility, when you see the VIX — CBOE Volatility Index — spike like it did back in February of 2018 as well as December of 2018, those are going to be buying opportunities. We're going to use volatility as our friend, not our enemy. And we're going to be able to pick up high-quality businesses that sell off for reasons that don't make any sense to us.

Right now, there's going to be continued choppiness as we try to sort through how this trade war is going to end with China. And if there's volatility like we saw yesterday, we will be in there trying to pick up good opportunities, high-quality businesses that are selling off for reasons that I don't think makes sense to us. So that's how we're going to navigate through this.

TWST: With volatility, is it difficult sometimes for some investors to accept the volatility and not want to jump out of a stock quickly instead of being there for the long run?

Mr. Villere: Yes. What we try to show is just history in general. Usually, when you look at the very best opportunities to buy a stock, it's usually when fear is the highest. The best opportunity to sell is when people are complacent in the markets, not trading a lot of volume, etc. And the best example is you go back to 1998, 1999 and everything was very rosy. And that would have been a great opportunity to sell.

The market peaked in March of 2000, when everybody was complacent, and then as it sold off, the Nasdaq ended up going down about 70% for March of 2000. And that would have been an incredible buying opportunity when everybody was scared. This dynamic is also similar to 2008 and 2009, when the market had sold off dramatically, which turned out to be a great opportunity to buy stocks.

TWST: It seems like a lot of times the markets don't like uncertainty. They want a resolution of things like interest rates or trade agreements.

Mr. Villere: Yes, whenever uncertainty is high is also when the market sells off. A lot of times, when you have uncertainty peaking is really when you want to be looking at your favorite buy list of names and consider adding stocks. Once the uncertainty is out of the market, that is when typically the market rallies. We often hear from clients that they would like to buy stocks when we, for example, hear something about China, when there's some final decision on this, that or the other. However, once that is final, the market could be 15% higher, and the opportunity to buy has passed.

TWST: What about the Baby Boomers? Do many of them still need to be involved in equities? Is it something that they need in order to continue to fund their retirement years?

Mr. Villere: Yes. When you look historically, there's been no better place to be than the stock market over the long run. And I think that if people can look past daily volatility and gyrations in the stocks that are blinking on your screen every day and think about them as real companies and as real businesses to own for the long term. And when you look at what these are and you speak to management teams and you realize they have really, really good products and services that we expect to deliver earnings, and stock prices follow earnings. So over the long run, good, high-quality companies should deliver good returns for investors if they can be patient.

TWST: Does it also mean that you just can't be looking at the dividends a company might pay but the overall quality of a company?

Mr. Villere: Yes, that's right. We believe in the total return concept. If we get a smaller dividend, we're hoping that those smaller companies are going to plough their money back into the businesses. Then, you are poised for a higher total return. More mature businesses may pay a higher dividend, but you could get a lower total return over a three- to five-year period. Overall, we're focused more on the growth aspect of businesses.

TWST: Do you think you're going to see more of the Millennial generation getting more involved in the market and investing?

Mr. Villere: Yes. I think we will over time. It's an interesting time. It's been so volatile. But I think as Millennials realize that they need to let their money grow, that's going to be something that they're going to be very attracted to over time.

TWST: Given that they're starting to pay off some of their early debt and take care of some of their personal expenses and there's more money around now, might that help them plan for their futures a little bit more now than maybe they were able to in the past few years?

Mr. Villere: Yes. I think they believe that cash is king. They think, "Let's just save our money." But I think there's no better way to grow your money over the long run than in stocks. And I'm talking about in IRAs, long-term vehicles, where you can get compounding returns on your money. And I think that Millennials will jump into that after three to five years, when they see that their low cash returns haven't really delivered the results that they were maybe hoping for.

TWST: Are some of your investors concerned about what is going to go on with interest rates?

Mr. Villere: I think the historically low interest rates should be good for the stock market in general. We saw when the Federal Reserve started to say that they were going to raise rates in 2019 almost indefinitely or they say they're going to raise them at least twice more in 2019. That's where I think Wall Street got a little bit nervous.

And that's part of the reason you saw the market sell off toward the end of December, and then in January, they do a 180-degree turn, and they say that we're no longer going to raise rates. We're going to be data-dependent. We're going to keep rates lower for longer. I think that was very helpful, and the market rebounded accordingly. So I think the low rates should be good for the market.

TWST: Is there anything we didn't talk about you care to bring up, either about the firm or about some trends out there?

Mr. Villere: I think a major trend right now is on index funds. There's been just over $1 trillion that's gone into index funds from active management. I think, when you look forward, active managers are well-positioned as they can keep cash on the sideline, actively manage and buy these good businesses, and have the opportunity to outperform. A lot of people have gotten kind of complacent and just put their money in an index because it has done well, but that does not mean that it will do well in the future.

TWST: Given some of these trends we've talked about, why would investors be interested in reaching out to a firm like yours with the history that it has?

Mr. Villere: I think we truly develop a partnership with our individual clients. We take their goals and objectives into consideration. We're a family business. Our name is on the door, and we care. I've been here at this firm for the last 20 years, and I'll be here for the next 40 years. And so it's one of those things that I think we will be here for the long run and feel good about taking care of our businesses over time.

TWST: Thank you. (ES)

ST. DENIS VILLERE III
Partner/Portfolio Manager
Villere & Co.
601 Poydras St.
Suite 1808
New Orleans, LA 70130
(504) 525-0808
www.villere.com
email: info@villere.com

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Basis Point (BPS) is commonly used for calculating changes in interest rates, equity indexes and the yield of a fixed-income security and is equal to 1/100th of 1%.

Cash flow measures the cash generating capability of a company, calculated by subtracting total liabilities from total assets.

Earnings before interest, tax, depreciation and amortization (EBITDA) is a measure of a company's operating performance.

Earnings per share (EPS) is the portion of a company's profit that is allocated to each outstanding share of common stock, serving as an indicator of the company's financial health.

Chicago Board Options Exchange Market Volatility Index (VIX) is a measure of the implied volatility of the S&P index options. Often referred to as the fear index or the fear gauge, it represents one measure of the market's expectation of stock market volatility over the next 30 day period.

NASDAQ Composite Index is a market capitalization-weighted index that is designed to represent the performance of the National Market System which includes over 5,000 stocks traded only over-the-counter and not on an exchange.
One cannot invest in an index.

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