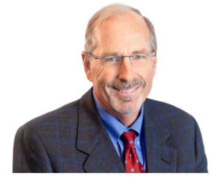
MAY 19, 2021



Bill Smead
Chief Investment Officer

Repeating Discovery's History

Dear fellow investors,

"History doesn't repeat itself, but it often rhymes."
– Mark Twain

On May the 17th of 2021, Discovery announced a merger with the media assets of AT&T. After an initial burst of enthusiasm, investors have turned sour on the deal. We have been through a very similar experience with Discovery (DISCA) back in November of 2017 and believe that these circumstances "rhyme."

The reaction to the deal fits perfectly with why growth investments have dramatically outperformed value over the last five years. The big streaming players have used algorithms and massive amounts of cheap capital to throw spaghetti up against the artificial intelligence wall to produce scripted TV shows and movies. The capital markets have rewarded them for good subscriber numbers and capitalized their future earnings at high multiples in this microscopic interest rate environment. Warren Buffett compares today's low interest rate environment to having the pull of gravity temporarily suspended on price-to-earnings multiples.

We bought shares of Scripps TV back in September of 2016, to gain access to their HGTV, Travel Channel and Food Network shows. We saw a gold mine of millennials eventually caring a great deal about house and home. In November of 2017, Discovery Communications saw what we saw and paid a 50% premium to buy Scripps with the blessing of the Newhouse family, their largest shareholder. The investment community didn't like the deal and Discovery shares fell in price below the collar set to protect Scripps shareholders.

This forced us to effectively take risk on DISC(A). We then analyzed DISCA and found a compelling value based on free-cash flow. Unscripted shows cost 90% less to produce than scripted TV shows. The popularity of Scripps and Discovery programs have had as much success gaining a wide audience as scripted shows do. Therefore, we sold our Scripps shares and bought DISCA shares at $17.45 per share. We had a gain of 45% in Scripps, which we pocketed.

Fast forward to today. Over the last three years we added to our DISCA holding and entered the year with over a 6% position. During the quarter, we sold a total of 7% of the portfolio out at an average sales price of $62 per share. This was a massive gain! When the Archegos debacle played itself out and the stock got crushed, we began to accumulate Discovery Series C common stock shares (DISCK), which we believe have the same economic interest the Series A shares have.

Now, we have Discovery making a very similar move by merging with the entertainment assets of AT&T. This creates a treasure trove of content from *Game of Thrones* to *Fixer Upper*, unparalleled anywhere among all the other streaming and cable content providers. However, it is content created by human creativity, rather than responding to what the artificial intelligence at a Netflix or Amazon or Apple TV tells you to create. No spaghetti thrown on the wall.

Fortunately for us, and unfortunately for shareholders of Netflix, there appears to be an underlying dissatisfaction with content provided at Netflix and Hulu. Here is how research firm, StudyFinds, looks at the current circumstances:

> *Of those planning on cutting back their streaming use, nearly half (46%) say Netflix is most likely to get the chop. Hulu (34%) and Amazon Prime (34%) follow closely behind. Over the past twelve months, half of those surveyed say they also turned to free, ad-supported streaming services as a way to cut costs and supplement their subscription bills.*

Compare that with blockbuster attraction to shows on HGTV, Discovery Channel and TLC's *90-day Fiancé*! Compare it to watching 190,000 hours of the Discovery library of *Deadliest Catch* or *Drive Ins, Diners and Dives*. Think of Tyrian in *Game of Thrones* proclaiming, "I drink and I know things!"

Lastly, what does the Newhouse Family's ownership of Discovery tell us about buying Scripps and merging with the media assets of AT&T? What does John Malone's voting control of Discovery tell us? The answer is they seem to be endorsing this transaction because it couldn't happen without their blessing. We like our chances for success being side-by-side with these outstanding investors, while the scoffers who believe in technology more than people, ridicule the deal.

Warm regards,

William Smead