

Akre Capital Management, LLC

January 15, 2011

Year-End Letter

2010 had a better outcome investment wise than we expected as recently as August, when we were still hoping for a positive result for the year. Surprisingly, we accomplished a 'better than average' result across virtually all portfolios while carrying large amounts of cash in all but a few.

Do we think we can rationally account for this outcome? Not easily. The precipitating event for the final third of the year market rally is generally given to QE2, which you will recall, was Chairman Bernanke putting in place a program intended to lift all asset prices. It did!

The striking thing about our portfolios today is that most have about a dozen holdings, along with cash balances often near twenty percent. Most of you also hold Hartford Financial convertible preference shares amounting to approximately five percent of the portfolio. These shares have a yield near 7% based on your cost, with an expectation that we will effectively increase that yield by a couple of points by the time it converts into common in April 2013. So in effect, your 'reserve' balances are really higher by this five percentage point holding.

Our goal has always been to compound your capital at an above average rate while incurring a below average level of risk. Holding cash and preference shares does not intuitively coincide with the notion of "compounding capital at an above average rate."

We have maintained this very conservative posture because we continue to believe that using caution makes enormous sense in face of worldwide uncertainties. You know well our view that the fiscal "crisis" facing the U.S. is not sustainable, and that any reasonable solution necessarily entails discomfort for virtually every part of our society.

Nevertheless, American businesses have today more liquidity and stronger balance sheets than at any time in recent memory. Many public companies are also selling at very modest valuations as well. Business is picking up in lots of places, including those places outside the continental U.S. We are utterly unable to predict how the market will respond to all the crosscurrents affecting our world. We do know well from experience that outstanding businesses managed by executives possessing equal parts of skill and integrity, and which have an outstanding record of and prospect for reinvesting all excess cash at attractive and accretive levels will build value at attractive rates over a long time frame. We believe your portfolio today is just such a collection.

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Please remember to let us know if there is any change in your needs or requirements as it relates to this portfolio which you have entrusted to us. We reiterate that it is our firm belief that your portfolio is populated with well above average businesses which are conservatively valued. Our expectation is that this will lead to above average outcomes, as has historically been the case.

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We would like to remind you of our periodic requirement to make available to you Part II of our Form ADV filed annually with the Securities and Exchange Commission. Please let us know if you would like to receive a copy.

Akre Capital Management, LLC

October 15, 2010

Third Quarter 2010

Unusual Uncertainty; Not

I have just spend two days in New York attending a value investing conference at which some very smart folks separately argued for a reasonably robust economic and stock market environment while others argued for a decidedly more austere scenario. Here's what I know. The U.S. has an unsustainably high level of government debt, which by some estimates in 2025 will require 100% of government income (revenue) just to pay the interest on it. This is not workable! At the same time, a number of economic indicators, such as railcar loadings, clearly point to a steady pickup in industrial activity. Finally, while unemployment remains devastatingly high, businesses lack the confidence to make new investments in people, despite having record levels of cash. Against this backdrop, several of the speakers argued that stock valuations were as cheap as any time in the last 40 years, and others argued that on an inflation-adjusted basis, valuations are currently very high.

All of us are faced with the dilemma of how to position ourselves for whatever comes our way. Will we encounter further deflation as interest rates go to zero, or perhaps even negative, while the Fed maneuvers to stimulate growth through quantitative easing (QE)? Or will we be faced with rapidly rising interest rates accompanied perhaps by rising inflation as the Fed scrambles to devalue the dollar in order to be able to pay back all of the U.S. borrowings? Just today I learned that the largest owner of U. S. treasury debt is no longer China, but is instead the U.S. Federal Reserve Bank. It makes my head swim.

Unlike the fall of two years ago, we are not now faced with the immediacy of the calamitous situation where investment banks and commercial banks were collapsing all around us. But perhaps today we face a much larger issue than the frightening experience of 2008. This is of course, 'how do we stabilize and accommodate all the competing demands for dollars which are not available?' This is broadly played out as individual households struggle to pay all their bills, and counties and cities and states also struggle with the exact same issues of how to pay all their obligations as they come due. Finally at the national level, our Congress which is charged with managing our revenue and expenses has in each of the past two fiscal years handed the U.S. citizens a budget shortfall (deficit) of more than one trillion dollars. Fortunately, neither our creditors, nor our bankers, nor our laws will allow us to individually carry on like the Federal government. We must pay our bills or face the immediate consequences.

One of my takeaways from the 2008 experience was that I felt a need to better integrate my 'world view' with my individual stock selection and portfolio construction, so as to try to be a better steward of the capital entrusted to me. This causes me to recall Buffett's two rules of investing: 1) don't lose money; and 2) don't forget the first rule. On the surface of it, the discussion above might reasonably leave an investor with an unusual level of uncertainty. The data is confusing, and the outcome is in fact unknowable. Therefore, in the face of these perplexing issues, we choose to hold more cash than usual, as we have done for nearly two years. One outcome of this is that in a robust market, our portfolios will likely do less well than the broader market. But we view this as a short term phenomenon. In addition, we are trying to make sure that our investments are not likely to be negatively affected by the current difficult environment dominated by the 'constrained consumer' nor by any of the scenarios which we may face soon, whether it be inflationary or deflationary. Our firm belief is that a concentrated portfolio of superior business characterized by high returns on the owner's capital, run by managers with equal parts of skill and integrity where there also exists an opportunity to reinvest all the excess capital to duplicate the high returns already being earned, will likely lead to an outcome we characterize as 'better than average with a below average level of risk.' Just maybe this uncertainty is not all that unusual, as again, Buffett reminds us: 'recall that the future is never certain, and that uncertainty is actually the friend of the buyer of long term values.' This all falls under the heading of 'risk management,' a primary focus of our job with your assets.

We are often asked about owning gold and bonds. As to gold we suggest that it is viewed as a 'defense' against political instability, fiat currencies, and general levels of uncertainty and anxiety. We know many who believe that it is an essential holding in light of the current situation in the U.S. and beyond. We don't personally own any today, but absolutely reserve the right to change our mind. As to owning bonds, we conclude that owning anything with a maturity longer than a few years is pure lunacy. We believe that two years is a proper target, and recognize that the return prospects from same are dismal today. Our record of correctly predicting the direction of interest rates is abysmal, so you may want to bear that in mind as you think about what to do. In lieu of bonds we do favor a few dividend paying issues where an investor desires to generate income which is not in fact a capital gain.

As always, we delight in our conversations with you, and look forward to them. Please be sure that we understand fully your true financial needs relating to these assets, as well as any concerns you may have in general about the market and the economy. After the horse has fled the barn, closing the door is of little use.

We would like to remind you of our periodic requirement to make available to you Part II of our Form ADV filed annually with the Securities and Exchange Commission. Please let us know if you would like to receive a copy.

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Akre Capital Management, LLC

July 13, 2010

Second Quarter 2010

Less Fun

The Second Quarter was less fun than the first quarter, because the stock market ended on a 12% to 14% decline from its earlier highs. The declines were not unexpected. And as a counter to our 'less fun' headline, we actually performed favorably relative to the market during this quarter end period, because of our defensive position.

All of you know from years past that until recently we have generally avoided speaking about economics and politics in our periodic letters to you. You will also recall that we said then that it is our job to focus on the individual operating businesses. Further, we would work hard to make certain that our entry prices were attractive, and that the strength of the individual businesses would take care of us in the long run. This has largely been the case.

You can rest assured that we are as focused as ever on our individual investments. Yet, over the past year or so, the tone and nature of our missives have changed, such that we are now regularly commenting on the economy. So you reasonably ask 'Why? What's changed?' The experience of 2008-2009 market collapse and subsequent "great recession" continue to have such an impact on us, as well as on clients and partners, that it seems to us imperative that we better incorporate our view of the world into our investment process. We are striving to "up" the level of macro thinking with the hope that we will reduce the level of anxiety experienced this last go around.

In that vein, we are going to make an observation here, which we believe is practically self-evident to any thoughtful person. The United States (and by no means alone in this world) is somewhere in the middle to late innings of a severe and unprecedented debt crisis. Lately, our thoughts have turned more to the "public" or "fiscal" side of this crisis.

To quote Niall Ferguson, eminent Harvard historian, "...public debt crises are always and everywhere a political phenomenon. They're the consequences of political weakness."^{*} Without getting into the politics of past behavior on the part of hundreds of elected officials, suffice it to say that all or virtually all of our tax revenue stream would be consumed simply by the interest payments on the Federal Debt in another thirty years,

* - Ninth Annual Niarchos Lecture: "Fiscal Crisis and Imperial Collapses: Historical Perspective on Current Predicaments"
Niall Ferguson, Harvard University
Peterson Institute for International Economics
May 13, 2010

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IF nothing were changed in our current trajectory. Ferguson argues that there are six ways to get out of the debt crisis: 1) raise GDP; 2) lower interest rates on borrowing; 3) get bailed out by somebody; 4) fiscal pain; 5) print money; and 6) default. He further argues that these choices one, two and three, are highly unlikely, leaving just 'cut, print, or default.' He then summons his recall of history, pointing out that only once in recorded history has a country solved its fiscal crisis by 'cutting,' and we don't have the same profile, essentially leaving just 'printing' or 'defaulting.'

So our heading might well have read 'Bondholders Beware,' instead of 'Less Fun.' Consequently, it seems to us that the investors' dilemma today is not unlike that of 1974. In the depths of the dramatic market decline culminating in 1974, everyone was asking, "Where can I put the wealth which I have accumulated and have it retain its value and be safe?" In 1974 we were already on the path of inflation and rising interest rates. In January of 1981 the prime rate peaked at 21.5% and long Treasuries had a coupon of 15.5%. When reviewing the options, Bank Accounts, Corporate Bonds, U.S. Treasuries, Real Estate, Gold, Art, Oil or Gas, Timber, or Common Stocks, nothing seemed safe, and it sent shivers down the spine of many investors. Nonetheless, the market rebounded considerably off the panic of 1974. But after the rebound, returns on common stock investments remained generally weak until courageous leadership brought economic and monetary policy under control. With hindsight we can now see clearly that the opportunity cost of holding cash in the tumultuous late 70's was quite low. Investors would have done well to become more aggressive only in the early 80's, at the time interest rates peaked and policies more favorable to economic growth were visible on the horizon. Since then, we have had the powerful tailwind of a secular decline in interest rates for nearly 30 years. We must not underestimate the power of that declining interest rate backdrop on all asset values.

Considering more recent events, the panic of 2008-2009 has subsided, but our belief is that, as it was in the late 1970's, the opportunity cost of holding cash will remain quite low until our political and economic leadership squarely addresses the debt crisis that underlies all of the recent financial turmoil and fear.

So, if you believe as does Ferguson that the only likely choices for us in our fiscal crisis are print or default, then holding any bonds with longer durations seems wildly illogical. Sure, in the short run the crisis is causing some deflationary pressure. But at nearly zero Federal Funds rates and low levels of inflation, cash has no enemies in our mind.

Let's think once more about how this crisis will ultimately resolve. We have argued for some time that the "constrained consumer" is unable to spend today as he did in the past decade. This argues against remedy one above, 'raise GDP.' Number two, 'lower rates,' is also not possible, as we are essentially at zero now. There is no entity in the world which has the capacity to bail us out, so number three is out. There is no leadership in our institutions which could cause us reasonably to predict sufficient 'cutting' to resolve the crisis, so scrap number four. The bet for the long term must be number five, 'print money.' It is often suggested that it is simply human nature to try to pay back one's debts with dollars which are worth less than the ones borrowed. Number six, 'default,' is

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certainly not out of question. History shows that many of our “respected” world partners and allies have defaulted, often several times, in the last several hundred years.

As you all know, the list of troubling domestic issues we face is both long and deep. Added to this mix are the potential disruptive hot spots in the world, namely Iraq, Afghanistan, Pakistan, North Korea, Iran and let’s not forget the “PIGS” (Portugal, Ireland, Greece, and Spain.) Surely there are others, just not yet identified. Taken together, it is a wonder that any of us gets any sleep.

We do positively conclude therefore that the “best” safe place for the preservation and future enhancement of our accumulated capital is in operating businesses which have ‘pricing power.’ So we continue down that very path which we have been on for several decades, searching for the outstanding businesses that demonstrate high returns on capital, managed by folks with equal parts of skill and integrity, where the ‘reinvestment’ thinking and execution are way above average. It turns out that in 1975, and again in 2009, that those businesses which have these attributes continued to build real economic value throughout the market collapse, and recovered much of their “lost” value in a reasonable time frame. We continue to purchase such businesses while being disciplined about price. We’re also mindful that in the midst of a massive debt crisis, having some cash on hand for a rainy day really isn’t awful. If we’ve explained it properly, our hope is that this defensive approach will appeal to you, although it most certainly will cause our results to vary from the indices.

As it relates to the overall fiscal picture, we highly recommend that you read Niall Ferguson’s entire talk delivered to the Peterson Institute on May 13, 2010. Niall is not only a great historian, but he is far more eloquent in summarizing our predicament. Make sure you have a tranquilizer or a tall whisky nearby when you read his piece.

What our governing bodies lack with respect to the public debt crisis is courage. The choices needing to be made are tough, and making them will cause disruptive outcomes for much of our population. However, not making these choices now assures that the outcomes at a later date will be far more painful! No doubt these hard choices will cause the journey for all of us to be ‘Less Fun’— but the fact is we cannot evade our reality much longer. The sooner our nation seriously confronts its debt problem, the sooner we may have comfort in adjusting our defensive investment posture.

Because we continue to experience difficult times in the economy and the stock market, it reinforces how important it is for all of us to be on the same page as it relates to those assets of yours which we manage. So we’d like to remind you to let us know what you are thinking about, or whether any psychological, emotional, or financial requirements have changed.

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Observations
April, 2010

We have recently discussed with clients and not yet clients alike, that our thoughts concerning the world at large are not the result of some strange metamorphosis into a "macro top-down" manager. Rather it is our attempt, post 2008, to better include our world view into our individual security selection process. In our most recent letters to you, we have commented at some length about our belief that the U.S. consumer will be less aggressive in this decade than he was in the last, largely due to his personal financial circumstances. Our view remains unchanged today.

Happily after a long and particularly hard winter, spring has come to Virginia. We have watched for several weeks as the fields green-up, and the trees leaf out. It feels too like spring in the economy, as we have the famous "green shoots" evidencing themselves everywhere. We welcomed the news this past week that employment actually showed a modest gain for the first time in several years, however fragile it may turn out to be.

We know only too well that trying to predict the direction of the market in the short run is a fool's game, and we remain committed to an agnostic position. Observably, there is a large and loud industry out there which on a daily basis tries to advise anyone listening exactly what they should do today, if not now, to be a better "investor." For most of us this daily blab is actually bad for our economic health. Our rather quaint notion of investing implies that one has gathered an arsenal of information, and from it, formed an opinion about what is likely to unfold over several years. Following that, we deploy some of our assets in a way which will capture the good outcomes hypothesized by these expectations. This remains our method of operating on your behalf.

The S&P 500 has risen approximately 76% over the past year from the March 2009 low point. This includes an increase of 5.4% in the first quarter of 2010, and in general, we weren't far behind this result. We are grateful for this result, as it has certainly calmed investor fears, if not created outright enthusiasm for the market and the economy. Everyone feels better, and appreciates the recovery in their invested assets. However, we continue to hold very significant cash reserves for client accounts because we are mindful of the constraints on the consumer (still 70% of our economy), as well as the certainty of a higher level of taxes which we will all pay. Our watchword remains "caution."

As always, please let us hear from you about any changes in your situation, whether it is financial requirements, or attitudes concerning your assets.

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** The S&P 500 is an unmanaged index that consists of 500 companies representing larger capitalization stocks traded in the United States. It is not possible to directly invest in the S&P 500. The S&P 500 has no management fees that reduce reported returns. The volatility and other risk characteristics of the S&P 500 may be greater or less than those of the separately managed accounts.