

Sustained Values

Many businesses can grow, but few can sustain their growth over a long period of time through both good and bad economic environments. The Wasatch Core Growth Fund seeks to purchase long-term growth stocks at reasonable valuations relative to the fund manager's projection of companies' five-year earnings growth rates. JB Taylor, fund manager, focuses on the competitive positioning of the business versus other comparable companies in the market.

Q: What's your investment philosophy?

A: We are buy and hold investors; we are not traders. We are looking for companies that can grow earnings in a consistent fashion over a long period of time through both good and bad economic environments.

Q: What kind of companies are you looking to invest in?

A: We focus on the competitive positioning of the business and compare the quality of the business to other companies in the same market. Many businesses can grow, but the key is to find companies that can sustain their growth and also maintain consistently high margins. In order to do that, a company must possess some sort of sustainable competitive advantage. It can be a product or a service or a competitive position that would be difficult to replicate. It could also be a company's culture or the management team that allows it to execute better than its competitors.

We focus on companies that will grow better than their markets and faster than the general economy. We think if we stick to those types of companies and pay reasonable prices, then stock performance will take care of itself.

Q: What type of growth are you looking for?

A: We stick to what we are good at, which is sizing up long-term growth companies

with a sustainable competitive advantage. We are looking for companies that can at least double their earnings over the next five-year period. Many of the top 10 holdings of our fund right now have been owned, at various weights, for almost 10 years.

Q: How do you find ideas? How is your research process organized?

A: The entire process is bottom-up fundamentals investing. When we find a company in a good business, with the type of competitive advantage that gets us excited and with a management team that we like, and assuming the valuation is good, we put it in the portfolio. We spend less time thinking about our sector allocation or areas of the market that we want to or don't want to have exposure to. Instead, we focus on assembling a great collection of companies that can grow their earnings over the long term.

First, we do a lot of quantitative screening. Some of our proprietary screens make narrowing the universe of stocks easier. Basically, we look for attractive revenue growth rates, attractive track records of consistent and high operating margins, favorable trends in key operating metrics, and high returns on capital. High levels of return on capital and improving returns on capital are the key metrics for us. High returns on capital, especially in relation to a company's competitors, can be a great signal as to whether there's a real competitive advantage or not.



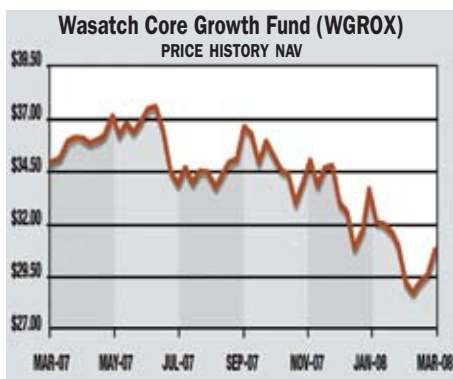
JB TAYLOR has been a Portfolio Manager for the Wasatch Core Growth Fund since 2000. He joined Wasatch Advisors as a research analyst in 1996 working on the Micro Cap portfolios. Taylor began working on the Core Growth Fund as a Senior Analyst in 1999.

Taylor graduated from Stanford University, earning a Bachelor of Science in Industrial Engineering.



PAUL LAMBERT has been a Portfolio Manager for the Wasatch Core Growth Fund since 2005. He joined Wasatch Advisors as a research analyst in 2000 working on the Small Cap Value Fund. Lambert began working on the Core Growth Fund as a Senior Analyst in 2003.

Prior to joining Wasatch, Lambert worked for Fidelity Investments. He graduated from the University of Utah, earning a Bachelor of Science in Finance.



After we have identified companies through this process, we try to assess whether or not they are sustainable growth companies. We'll do background checks on management teams and read all the public filings that exist. We don't rely on Wall Street for earnings estimates. We build our own model of each company and we use that to assess the current and potential future valuation of the stock.

One of the things we do in the Core Growth Fund is we try to visit every single company we hold in the portfolio at least once a year. It's really the on site visits that allow us to pick up big insights into a company's culture or how the management team works together and what makes that company different.

Q: How important is valuation in your strategy?

A: Just because a company is growing or is in an attractive market, doesn't necessarily mean that we can make money owning the stock. That's where our own internal valuation models come into play.

We look out three to five years on every single holding using our models. We esti-

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mate the company's future performance and identify the key drivers in the model to come up with our valuation. Basically, we make some very conservative estimates about what the earnings multiple will be in the future. And then, with a high degree of certainty, we want to determine what we think the earnings growth and earnings targets will be.

Q: Who are the people that manage the portfolio?

A: This portfolio is managed by a team of Wasatch portfolio managers with Paul Lambert and me being the key decision-makers. I've been on this portfolio since 1999 and Paul joined the team as a portfolio manager in 2003. We are just two of 20 portfolio managers at Wasatch. It's a very collaborative, teamwork-focused environment.

Paul and I determine the specific stocks and the position sizes that go into the portfolio. It's not uncommon for any Wasatch portfolio to have the majority of its holdings come from ideas generated outside of the immediate team by our research partners here at Wasatch. We are all out looking for attractive, interesting companies and each of us has a slightly different approach to investing. We work through each company together in order to get what we refer to as a thorough "multiple eyes" perspective on that company.

Q: Can you give us one or two historical examples of stocks that you have identified through your research process?

A: Our top holding right now is a company called Copart (CPRT). Copart is the country's largest provider of auction services for salvaged vehicles, provided primarily to the auto insurance industry. It's been probably 10 years that we have owned this stock.

Copart was found on one of our numerical screens for attractive margins and positive trends in fundamentals. The thing about Copart that stood out was its high revenue growth. At the time, it was growing around 20%, had high margins and good returns on capital. .

Another thing that made Copart different is that it had an Internet portal at the time when the Internet was just gaining traction. By using the Internet to open its auctions to a wider audience, the values that were received at the car auctions increased, which helped the company capture market share.

In the research process, I visited three or four salvage yards to meet with the operators and the buyers and to understand how the auctions worked. I met with the management, both here in our offices, and in their San Francisco area location. We then built our own earnings model and determined how much capital was required to run the business.

In 2003 the stock was extremely weak because company management had gone out and expanded too quickly and accumulated a lot of real estate to do so. Their business slowed and Wall Street hated it. It was important for us at that time to understand management's philosophy. They could look out three to five years and see huge opportunities for Copart because their service was so much better. Management knew they were going to get more cars to auction but they simply didn't have the land to accommodate the inventory of cars, so they were investing in real estate at a time when it wasn't convenient for Wall Street. The stock was punished, but it was a good time to be buying the stock, which we did.

Q: Why did you believe that Copart would continue to grow?

A: Copart's margins were better because it was using the Internet at a time when all its competitors were still holding old-fashioned auctions at their salvage yards with an auctioneer and bidders walking from car to car. By using the Internet, Copart was attracting more buyers and the prices at auction were higher because there were more competitive bids.

The company eventually stopped holding physical auctions completely and went to an all-Internet auction, which had a tremendous positive impact on margins because all the costs of holding physical auctions went away. Copart had better operating

margins, faster growth and better returns on capital than the rest of its market. And the chief executive, Willis Johnson, owned about 20% of the stock. All those things gave us confidence that this was, and still is, a long-term growth company.

Another example is Pediatrix (PDX), a physician practice management company that serves neonatologists and emergency care pediatricians. First, the number of sick babies that are delivered and need emergency care every year is very consistent, so it's a very stable business. Pediatrix works with approximately 30% of the emergency care pediatricians and neonatologists in the United States, which is a market position that is very difficult to replicate. The company has been the largest physician practice management company ever since it controlled 10% or 15% of the market, and it has continued to grow. Pediatrix has a long history of making physician practices more profitable, which is in part a result of better contracting with insurance companies. Their size is a great competitive advantage. So, these are two examples of why we focus on the business model and the sustainability of the margins.

Q: Generally, how do you build your positions?

A: Our minimum positions tend to be 1% weights and our top holdings tend to be 5% weights. The stocks at the top of the portfolio with the largest weights are the ones we have known the longest and the ones we believe to be the most sustainable, consistent growers.

The smaller weights are positions where we think we found a consistent grower but it's going to take more time getting to know the company better and watching the management team execute their business plan.

Q: Could you describe your buy/sell discipline?

A: Our baseline valuation for a new position is a trailing P/E multiple that is equal to, or less than, our estimate of the long-term forward earnings growth rate. If a company is growing 20%, then ideally, we'd like to pay 20 times earnings.

When we get confidence in the sustainability and quality of a particular model, we'll increase our weighting in the stock. We are constantly comparing the quality of different businesses. If we think a company's prospects are becoming brighter or if a company has made some significant gains while another company seems a little weaker, then we may swap those positions.

Sometimes we'll have a 1% position in a quality company but think the valuation is too high, and our models tell us that we can't make our targeted 15% return going forward. We will likely sell that position and wait to buy the stock again when it is more attractively valued.


In all, there are really only two times we sell a stock. The first is when our original investment thesis is broken and the other is when we think the valuation is too high. If we don't see the potential for out-sized returns, then we sell the stock. We benchmark the portfolio against the Russell 2000 Index.

Q: What is the total number of holdings that you generally have?

A: We run a fairly concentrated portfolio. We currently have 69 holdings and that number could be 10 lower or 10 higher at any given time as we buy or sell positions. Right now, our 20 largest positions make up about 60% of the portfolio.

Q: What do you do to mitigate risk?

A: We take a simple approach to managing risk. We stay disciplined and focus on buying long-term growth businesses and paying a decent multiple.

We don't have any stop losses or technical trading risk mitigators. We believe that the key is to get the investment thesis and the long-term prospects of the company right. If we can own a portfolio of companies that are doing better than the market, better than the economy, and can grow their earnings faster over the long term, and if we pay reasonable prices for their stocks, then we think we'll be protected in terms of market risks and have the potential to produce attractive returns. 

Wasatch Core Growth Fund

Symbol	WGROX
Website	www.wasatchfunds.com
Address	Wasatch Funds PO Box 2172 Milwaukee, WI 53201-2172
Tel. No.	800-551-1700
Inception	12/06/1986

PORTFOLIO

Total Net Assets*	\$886.7
Avg Mkt Cap (\$ Weighted) *	\$7,600
Average Price/Earnings Ratio	27.13x
Average Price/Book Ratio	5.16x
Turnover Ratio	54%

INVESTMENT INFORMATION

New Investment	Open
Min Initial Investment	\$2,000
Min Subsequent Investment	\$100
Min Initial IRA Investment	\$1,000

RISK (AGAINST S&P 500 DAILY REINV IX - 3 YEARS)

Alpha	-0.49
Beta	1.30
R-Squared	0.70
Ann. Std Deviation	13.20
Sharpe Ratio	-0.12

RETURNS VS. S&P 500 DAILY REINV INDEX

	WGROX	Index
1 Year (Cum.)	-13.23%	-5.08%
3 Year (Ann.)	1.42%	11.32%
5 Year (Ann.)	12.75%	3.50%

RETURNS VS. RUSSELL MID CP TR INDEX

	WGROX	Index
1 Year (Cum.)	-13.23%	7.30%
3 Year (Ann.)	1.42%	5.18%
5 Year (Ann.)	12.75%	4.50%

FEES AND EXPENSES

Max Sales Charge - Front	0.00%
Max Sales Charge - Deferred	0.00%
Max Redemption Fee**	2.00%
Total Expense Ratio	1.18%

PORTFOLIO MANAGER

J.B. Taylor	2000
Paul Lambert	2003

* millions **2 months after purchase

Data through: 03/31/2008

Source: Company Documents; Lipper

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