



OAK VALUE CAPITAL MANAGEMENT, INC.

Portfolio Commentary – Third Quarter 2005

EXECUTIVE SUMMARY

- ❖ In contrast to more commodity type businesses dominating recent leaders' boards, we maintain a focus on companies we believe reside firmly within our circle of competence - assessing competition and its impact on long term profitability. In the aggregate, the client portfolios we have constructed are comprised of a carefully selected group of high profit margin, high return on capital businesses which we believe are a prelude to good investment results.
- ❖ Rising oil prices, increasing interest rates and natural disasters are squared off in the investment arena against the team of still low nominal interest rates, relatively healthy corporate earnings and increasingly attractive valuations in selective areas.
- ❖ In this environment, we continue to find a handful of durable businesses that we believe can grow their cash earning power over the long term. In aggregate for client portfolios, we expect five year average earnings growth rates for these companies to be in the low teens with operating margins and returns on equity metrics in excess of twenty percent.
- ❖ In the aggregate, portfolio activity remained light during the quarter, with no new companies added and no existing positions eliminated. We did increase the weighting of one diversified business held in client portfolios, based on mild stock price weakness and growing confidence in execution across a diverse manufacturing and service portfolio.
- ❖ For the quarter ended September 30, client portfolios generally posted slightly negative returns and lagged the broader market. Despite the tempestuous weather along the Gulf Coast, the summer months passed with little aggregate change in the market value of Oak Value client portfolios.

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3Q 2005 Client Portfolio Activity Summary

Note: Not all Holdings listed may have been purchased, held or sold for all client positions.

New Positions	Eliminated Positions
No New Positions	None Eliminated

INTRODUCTION AND

OVERVIEW

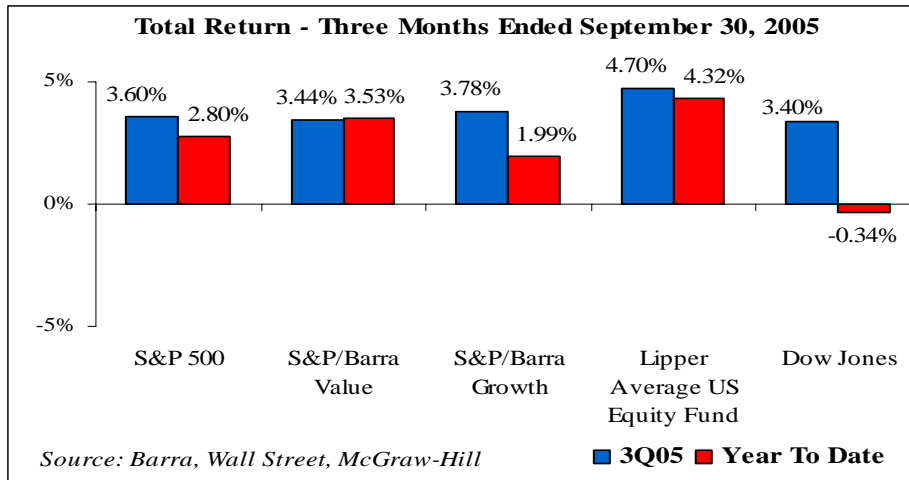
“Curiouser and curiouser!” cried Alice...

Lewis Carroll, Through the Looking Glass

We approach the close of the year observing some peculiar cross-currents on the investment landscape. Rising oil prices, increasing interest rates and natural disasters are clearly squared off in

the investment arena against the team of still low nominal interest rates, relatively healthy corporate earnings and increasingly attractive valuations in selective areas. In this environment, we continue to find a handful of durable businesses that we believe can grow their cash earning power over the long term. Most of them are in our view conservatively financed, and often have shown improved financial positions relative to peers and their own their own historical experiences. Even in a period exhibiting little visible traction, we believe client portfolios today represent such *good businesses*, with *good management*, available at *attractive prices*, a combination that tends toward favorable investment outcomes over time.

Top Ten Holdings as of September 30, 2005	
Company	Primary Business
AFLAC	Supplemental Health & Life Insurance
Berkshire Hathaway	Insurance, Reinsurance & Capital Allocation
Cadbury Schweppes	Int'l Confectionery & Beverages Manufacturer / Licensor
Cendant	Travel, Hospitality & Mortgage Finance
Comcast	Entertainment & Information Services
Constellation Brands	Wine, Beer & Spirits Production / Distribution
E.W. Scripps	Entertainment & Information / Media
IMS Health	Prescription Medication Care Provider
Time Warner	Entertainment & Information / Media
Zale	Fine Jewelry Retailing

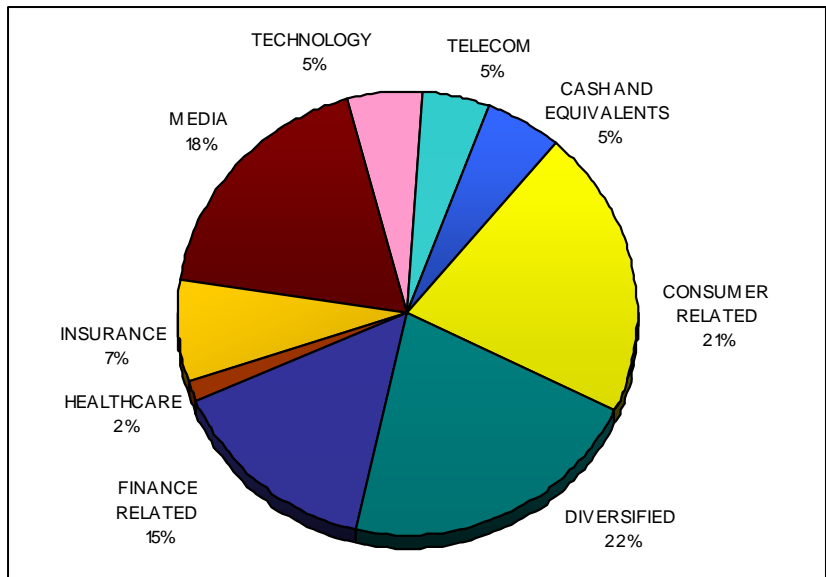


The upshot of these discordant pressures is that we are satisfied that the overall backdrop from which we are making today’s investment decisions leans toward favorable. Despite several challenges that may induce short term price volatility, the compression in valuations of late offers the patient investor the unusual opportunity to own high quality businesses at valuations relatively similar to those of lesser quality. In aggregate for client portfolios, we expect five year average earnings growth rates for these companies in the low teens with operating margins and returns on equity metrics in excess of twenty percent. Generally such mouth watering economics are offered at sizable discounts to intrinsic value as a result of continued business progress and limited stock price movement over the better part of almost two years.

PORTFOLIO UPDATE

Despite the tempestuous weather along the Gulf Coast, the summer months passed with little aggregate change in the market value of Oak Value client portfolios. About half of the companies held had stock price gains and roughly half had losses during the third quarter. For the quarter ended September 30, 2005, client portfolios generally posted slightly negative returns and lagged the broader market. In considering recent short term portfolio outcomes, the deficit for the quarter continued a recent pattern in that it was largely attributable to what client portfolios did not own rather than what they did. Most of the S&P 500's return for the third quarter came from two sectors – Energy (now nearly a two year old theme) and Technology.

Business Category Allocation- September 30, 2005



In what may be viewed as a signpost of the potential we see in client portfolio companies, two of them, **Certegy** and **IMS Health Systems**, were involved in merger/acquisition discussions during the third quarter. We are not surprised by the interest of corporate investors in these high quality companies. We too were attracted to the operating and cash flow efficiency whereby they convert data into information and then to growing revenues.

The outcome of both potential deals is yet to be determined and the economics may be adjusted prior to closing. We advise that stock prices can be volatile pending transaction outcomes, and note that the IMS deal in particular appears to be facing some challenges.

We will evaluate each relative to our assessment of the future prospects of that which current Certegy and IMS shareholders are to receive balanced against that with which they will be parting. In any event, we remain attracted to the ongoing value inherent in the information franchises of both companies, on a stand alone basis or – pending the outcome of our review – in conjunction with a merged, more diversified entity. As is typically the case, our actions on your behalf will reflect our analysis.

Oak Value client portfolio values and equity markets overall have held up rather well in our view despite a challenging setting. Even more importantly in our view, the values of the underlying businesses in client portfolios are, by our reckoning, proving their durability despite macro headwinds. The top performers for the third quarter generally represent portfolio “vintages” ranging from long time positions to a newcomer added earlier this year. We also note that several sell decisions we have made for individual portfolio companies over the past year or so have had the effect of shifting the character of client portfolios somewhat, with reduced exposure to catastrophic events (less insurance) as well as lower sensitivity to oil price increases and the potential downstream negative impacts on consumers (less retail).

Of the lagging third quarter client portfolio performers, three were positions established earlier in 2005. Downward price volatility in such situation is unsurprising to us, where the uncertainty that we believe helped create our investment opportunity remains fresh in the air and on investor's minds. There were also a handful of the

companies that gave up some ground in the third quarter which have been solid long term client portfolio performers. They experienced what we would view as the garden variety price changes inherent in liquid markets. All else being equal, additional downward price action for such high quality businesses is likely to whet our appetite for additional ownership in client portfolios. All in all, reviewing the current “state of the union,” at the individual company as well as the portfolio level, the businesses we have selected for client portfolios have very attractive underlying economics and trade comfortably below our intrinsic value estimates, leaving us excited about prospective opportunities.

Portfolio Changes

In the aggregate, portfolio activity remained light during the quarter, with no new companies added and no existing positions eliminated. We did increase exposure to one diversified business held in client portfolios, based on mild stock price weakness and growing confidence in execution across a diverse manufacturing and service portfolio.

As you know, we constantly try to add to our knowledge base, hopefully placing near term events and outcomes in the longer context of our investment theses. While we do not believe that hyperactivity paves the road to investment success, neither is the investment business one which rewards ignorance or sloth. In this light, we reduced exposure in Ambac during the third quarter; as one of our previously larger positions, often in the top ten portfolio holdings, we thought an update on the shift was warranted.

In our view what you don't know **can** hurt you in investing, as business values expand or contract in response to competitive forces and other environmental changes. Vigilance in the realm of maintenance research is rarely a source of regret in our experience, especially in financial services businesses where complexity and uncertainty tend to multiply with growth and time. Over the summer months, we therefore revisited the balance between our attraction to Ambac's historic profitability record and our ongoing appreciation for an evolving risk/reward profile. While there is much to admire in Ambac's business model, shifts in its business mix and increasing competition (as well as substitutes) for its risk-transfer services presented us with sufficient reason to re-evaluate our assessment of its intrinsic value range. The result of that analysis was a general reduction in Ambac position sizes in client portfolios to a level more consistent with our required margin of safety and predictability.

Five Largest Holdings Update

AFLAC

After a period of price weakness earlier this year (an opportunity which we used to sizably increase positions), Aflac's share price has steadily climbed in response to improving business outcomes in both of its major markets, Japan and the US. Our experience with Aflac's business over many years is that their continuous product innovation and focus on efficiencies more than adequately compensate for occasional brief slowdowns, macro challenges, and shifts in the competitive landscape. In Japan, they continue to build on a successful cancer insurance history with products designed to support an aging population faced with rising co-pays in government sponsored health plans. They may also continue their success in penetrating the small and mid-size business market with the proposed 2007 entry of banks as distribution partners. In the US, Aflac continues to

make progress in better managing the growth that their status as the only company purely focused on secondary product offerings has helped to create. For this great company, opportunities identified and seized have been a hallmark of its great management team over time.

Berkshire Hathaway

Berkshire remains a “tale of two stories” in our view. One is the regulatory uncertainty that we believe continues to obscure the business progress to some degree. In September, the chief executive of Berkshire’s Gen Re subsidiary received a notification from the SEC that it is considering regulatory proceedings against him, keeping the concern on investors minds. That we are having some discussion about legal or ethical concerns inhibiting Berkshire’s share price is perhaps the ultimate irony given its history of management continuity, fair dealing, and uncompromising standards. In point of fact, the latter may be prolonging a resolution, as we suspect Berkshire is far more willing than most public companies to follow any allegations through to a finding of fact as opposed to settling for cash in the interest of “closure.”

Some level of unacceptable behavior by a small number of insurance managers highlight that Berkshire is subject to the same challenges as other large businesses with many employees in guarding against unethical and illegal behavior. Nonetheless, we believe Berkshire is better than most companies at setting a high ethical bar and more diligent in maintaining it. Employees found to have engaged in deceptive rather than debatable practices have been terminated, a standard to which we would expect Berkshire’s senior management will continue to adhere. We continue to find it unfathomable that Mr. Buffett was personally involved in unlawful actions or activities. Perhaps most pertinently, we remain of the opinion that the resolution of the insurance transactions which have been publicly identified thus far will not have a significant economic impact on Berkshire. Nothing about how these regulatory matters are ultimately settled would in our view have any ability to damage Berkshire’s business model or substantively impact its intrinsic value, which remains significantly above its recent stock price.

The other account of Berkshire in our view is much more relevant to our investment thesis, and that is a tale of ongoing value creation that is clear (to us at least), though not obvious or visible in stock price behavior. Berkshire has so profusely coined money of late that searching for a comparable recently left us wryly comparing to Rumpelstiltskin or King Midas. In keeping with an opinion we proffered several years ago, Berkshire’s diverse collection of operating businesses is producing an enviable cash hoard. There is of course some level of challenge represented by the scale of its reinvestment opportunity, though Berkshire notably has a wider menu of investment options available to it than most single industry businesses, and of course maintains well-honed capital allocation skills as a core competency. In fact, just what the deployment of its cash has the opportunity turn into - the value it can create over time - is the critical question for Berkshire shareholders.

Berkshire made some progress on this front in 2005, purchasing an insurance subsidiary from General Electric for just under \$1 billion, leisure vehicle manufacturer Forest River for an undisclosed sum, and incorporating Scottish Power’s former PacifiCorp subsidiary into its MidAmerican Holdings subsidiary for roughly \$5 billion, plus \$5 billion in assumed debt. The recent repeal of the Public Utilities Holding Company Act (PUHCA) in Energy legislation signed by President Bush should help Berkshire

redeploy some of its billions into a utility area with capital needs and regulated return potential far above Berkshire's very low cost of capital.

To assess Berkshire's intrinsic value, we make assumptions about investment results on Berkshire's vast capital pool, value its non-insurance operating businesses and adjust for its minimal debt. Even our conservative scenarios indicate a sizable discount of the current stock price from a rational appraisal of Berkshire's intrinsic value.

Cendant

Cendant's share price backed up some during the third quarter, as its near term results were impacted somewhat by Katrina and Rita hurricane exposure (property damage and lost revenue for properties, rental cars, real estate services, etc.). With a confidence in the underlying businesses and a comfortable gain in Cendant from average purchase prices, we are little influenced by what amounts to trading noise. Much more noteworthy was Cendant's post third quarter announcement that it will split itself into four separate companies that are more narrowly focused on specific business segments of real estate, travel distribution, hospitality, and vehicle rental. While this falls into the category of an evolving situation we are evaluating, it is to some degree the ultimate outgrowth of the business streamlining process that Cendant has been undergoing for several years.

One of the challenges to value realization at Cendant in our view has been the disparate nature of its operations, coupled with a "moving target" aspect to its financials, as the iterations of business transactions inhibited direct comparability with prior periods. With some difficulty in assessing the "steady state" movement of individual businesses, we believe Wall Street analysts have been discounting the whole package to counterbalance their uncertainty. Cendant's management, somewhat frustrated at what it viewed as a perennial discount from business value, has chosen to lay the path clear with four "pure play" businesses, each with its own capital structure and operating mandate, run by experienced management teams pursuing their own success.

We will be evaluating the proposed split and assessing competitive positioning and rational intrinsic value estimates for each in determining our reaction to this proposed change in the ownership format for Cendant's assets. We will assess each entity in light of its future prospects, balanced against the market's assignment of a price related to that value. Our actions on your behalf related to Cendant and its offspring will reflect that analysis.

Cadbury Schweppes

Cadbury has worked diligently to execute its plan to rationalize global production, leverage its routes to the consumer and innovate new products based on its strong worldwide brand positions. Reported progress has been in line with projections of 3-5% revenue growth, though hopes to expand profit margins have been hampered by materials (plastic containers are a petroleum by-product) and transportation cost pressures (resource diversions for hurricane relief) in the US, the company's largest world market. Innovation has been most successful in the US drinks division, where the Dr. Pepper franchise has expanded into the diet area to drive volume growth. In Europe, the company is in the process of selling its beverage division,

delivering on a commitment to focus resources on their highest return opportunities and to rationalize those with more modest prospects.

In our view, Cadbury has executed well in its integration of the Adams gum acquisition and in subsequently beginning to deliver on the promise of that combination. Shares remain comfortably discounted from intrinsic value at recent prices, and we think the sales and margin increases they anticipate remain achievable for a great portfolio of brands that are a big part of many people's daily snack experience.

EW Scripps

Scripps continues to experience positive operating and financial outcomes, courtesy of its strong portfolio of media properties. Founded in newspapers, the management team has historically - and profitably - moved into television and cable networks, video shopping and now directly onto the internet. Scripps has a history of starting valuable media assets from scratch (HGTV) as well as acquiring them (Food Network). The company continues to make progress with its newer networks - Fine Living, DIY Network (do-it-yourself), and Great American Country (GAC) - expecting them to collectively begin contributing to the network segment profitability after several years of nurturing them. Scripps also continues to invest in its more direct entry in the commerce area, the Shop At Home network, which is growing revenue but requires investment to implement the electronic commerce vision of its management.

By operating across a broad range of media, Scripps hopes to be able to capture viewer-ship and advertising dollars that migrate to those other media over time. Because they develop and own the original programming used on its networks (at a fraction of other entertainment outlets' production costs), they are more suited to leveraging that content into other forms of distribution, in particular video-on-demand and the internet. Moreover, we think Scripps' rich relationships between specific content and viewers who are attuned to those interests makes their ownership ultimately more commercially exploitable for advertiser dollars than content with less of those features.

CONCLUSION

Especially for oil and other raw materials (natural gas, gold, steel, coal, etc.) that have so dominated recent leader's boards, it seems to us that the temptation for investors to "get on the bandwagon" is rising alongside prices at the gas pump. In our opinion, such investments generally lack the most crucial element in investing - long term predictability - that would place them within our comfort zone as prudent allocations of client capital. Pricing cycles are well-known and well-studied phenomena that have existed for centuries. During periods of high prices for commodity goods, the sky always appears to be the limit, though the real world factors of supply and demand ultimately adjust. Well-documented historical patterns indicate that when commodity prices remain persistently high, capital is attracted, new capacity comes on line and prices trace a downward path.

We remain our focused on companies we believe reside more firmly within our circle of competence. We maintain a preference for companies that possess what we believe to be superior strategic positions relative to the forces that can influence their ability

to generate cash for their shareholders. Such results generally pave a path for increasing value throughout various economic environments. If you look at the true long term economics of commodity type businesses (and we have looked), they fail to meet these tests. Conversely, in the aggregate, the client portfolios we have constructed are comprised of a carefully selected group of high profit margin, high return on capital businesses which we believe are a prelude to attractive investment results. Having diligently ferreted out a good value, investors in such situations are usually adequately compensated for waiting, as long as competitive positions can be maintained over time. We will wait patiently, while continuing to work diligently

We thank you for your continued interest and partnership and welcome your questions and comments.

Oak Value Capital Management, Inc. Investment Committee

David R. Carr, Jr.

Larry D. Coats, Jr.

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IMPORTANT INFORMATION

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