

Economic Returns

Investing in companies with market leadership positions in stable and growing markets is generally rewarding, especially when stocks are purchased in times of weakness. JB Taylor and his team of managers look for small cap growth companies with high economic returns when they are out of favor.

What drives your investment philosophy?

We want to own the highest quality steady growth companies in the small cap market. We believe that owning high quality companies with sustainable competitive advantages is a winning strategy over the long term. We look for good returns on capital, great management teams and good businesses in growing industries.

How does your team approach help your investment decisions?

Wasatch's investment process is very team oriented. We have what we call a "multiple eyes" approach where we are consistently consulting with each other to figure out which are the very best companies. Our experience makes us unique in this regard. Wasatch has specialized in small cap investing for over 30 years, and the current team has been investing together for well over a decade.

"We are not focused on the high-profile, fastest growth companies in the economy. We will take consistent and predictable growth over high growth every day. And due to our long-term orientation, our trading tendency is to buy up even more of our types of companies when markets and stock prices get weak."

So while I am the lead manager and work with Paul Lambert, my co-manager, to make the final investment decisions, there are more than 10 other portfolio managers and analysts that have contributed to this portfolio with idea generation and due diligence on companies. We are also continually traveling together to unearth new opportunities.

How do you define "Core" in the Wasatch Core Growth Fund?

"Core" to us is really a descriptive word. A "core" company can grow revenue and earnings at a steady clip in both good and bad economic environments.

We are not focused on the high-profile, fastest growth companies in the economy. Those companies are typically heavily followed by Wall Street and have usually been bid up to valuations that make less sense to us. We will take consistent and predictable growth over high growth every day. And due to our long-term orientation, our trading tendency is to buy up even more of our types of companies when markets and stock prices get weak.

What is your investment strategy?

The types of businesses we invest in tend to be somewhat of an eclectic mix of companies with growth drivers that are not necessarily tied to the macroeconomic environment. A strong return on capital, and the financial flexibility it affords a company, is very important to us. In a weak economic environment, our companies typically have the wherewithal to continue growing by making acquisitions or they can improve earnings growth by repurchasing their stock.



J.B. 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 Fund.

Taylor began working on the Core Growth Fund as a Sr. Analyst in 1999. He graduated from Stanford University, earning a Bachelor of Science in Industrial Engineering. Taylor is a California native who speaks Hungarian. He enjoys basketball, reading, and spending time outdoors.

Performance - Price History N.A.V.

WASATCH CORE GROWTH FUND (WGROX)



	2008	2009	2010
+Russell 2000 Index	-33.8%	27.2%	26.9%
Wasatch Core Growth Fund	-44.3%	45.2%	25.0%

One metric we use that helps explain the high quality nature of our businesses is EBIT-ROA, or earnings before interest and taxes relative to (i.e., divided by) assets. It is a rough measure of how much cash a business generates with the assets that have been deployed. For instance, our portfolio average EBIT-ROA is around 35%, whereas the average company in the Russell 2000 generates an 8% EBIT-ROA. Our companies are simply much better at utilizing their assets to generate cash.

We aim to buy companies with market values less than \$3 billion, and will look at companies as small as \$300 million. We are happy to hold companies if they exceed the upper limit as long as they are performing well, continuing to grow and have a reasonable valuation.

An example would be our largest holding, Copart, Inc. It's a company we have owned for over 14 years. They provide online auctions and vehicle remarketing solutions for the auto insurance industry. When an insurance company pays out a claim on a totaled car, they need to sell the damaged car to recoup some of their losses. Copart steps in by picking up the cars, storing them at their facilities and auctioning them off to the highest bidder. They have roughly a 40% market share and dominate this steady growth market.

Copart has consistently used technology to stay ahead of its competition and it shows in the business results. By using the internet to open up their auctions to bidders all over the world, they have deepened the pool of buyers, which translates into higher prices at auction, and higher returns to the insurance company. Utilizing technology has also allowed Copart to

take costs out of the business, resulting in high operating margins that are 2x that of their closest competitor.

It is a great example of the type of high quality companies in which we invest. Copart's end market is relatively stable, they have an experienced management team that owns a large percentage of the company, and they generate a great return on capital.

What does "quality" mean to you?

We define quality as the combination of a strong economic model, a high caliber management team, and the ability to grow through a tough economic environment. Quality management teams are a wonderful thing to study and track, because "management" is not a simple metric that can be screened for like EPS growth or the P/E ratio. We think our long experience in the small cap space gives Wasatch a competitive advantage here.

How do you find ideas and evaluate different ideas?

There are several ways new ideas get into the portfolio.

One way is through our consistent numerical screening of the investment universe. We are routinely running screens looking for companies with solid growth and high or improving returns on capital.

The second way is by getting out on the road and visiting management teams. We try to visit all the companies we own at least once each year, at their facilities. Whenever we go see a portfolio company in a given city, we look for new ideas and visit as many small cap companies in the geography as we can.

The process from there is multifaceted. We want to know the company as well as any outsider possibly can, so we read everything that can be found in the public domain (Annual Reports, 10-Ks, 10-Qs, conference call transcripts). We also build all of our own earnings models, which is really when we begin to understand the important drivers of a business. We have thousands of excel spreadsheets devoted to understanding companies, and we don't rely on Wall Street to determine our long-term forward earnings estimates.

The models are also a great generator of questions for management. Over time, we establish an ongoing dialogue with management through visits and conference calls.

Looking back, almost all of our biggest winners can be traced back to identifying, in real-time, a world-class management team.

Can you give examples that illustrate your investment preferences?

An example would be IDEX Corporation. IDEX is an industrial manufacturer, specializing in fluidics. They sell an array of pumps, flow meters, fluid dispensing equipment, as well as industrial pumps and air motors and compressors.

IDEX is interested in any growing industrial market where there is a need for a complex technology solution. Many of their solutions end up in the healthcare, chemical processing and energy markets. However, we really view IDEX as a management story. They have a tremendous track record of efficiently running their basket of businesses, focusing intensely on return on invested capital.

We have known IDEX for a long time and it is a large portfolio weight. The stock has recently been weak due to larger macroeconomic fears, but possibly also due to the recent departure of their well-respected CEO. We did as much research as we could about the newly named CEO, and then visited the company. The visit reinforced our view that IDEX had a very strong succession plan in place, and that the company is still poised to succeed. We used the market weakness to increase our stake.

Life Time Fitness, Inc. is another holding of ours. It is a national chain of fitness centers.

Life Time Fitness builds fitness clubs that are superior to anything in the market. They deliver the best experience to the customer, but for a reasonable price. Their competitors are typically the small gyms, “or a bunch of weights in a small room” as Life Time’s CEO might call them. By contrast, Life Time’s centers are over 100 thousand square feet, with full-court basketball courts, several Olympic-size swimming pools, a café, a spa and a kids’ center offering free babysitting. They offer a “country club lifestyle” for the masses. These clubs go into new markets and take massive amounts of market share.

We found Life Time Fitness back in 2005, when screening through companies with interesting growth numbers. We had some initial concerns as these centers were quite expensive to build - \$30 million to \$40 million- and they relied heavily on mortgage financing to fund growth.

As we delved deeper into the company we found that Life Time Fitness had less than 300,000 members, so they were tiny considering there is a market of over 40 million paid fitness memberships in the U.S. We visited their centers in several cities and talked to the employees and customers and found they truly viewed Life Time as being unique: centers could draw members from a wide geographic net wherever they went. They were consistently pre-selling upwards of 3000 memberships before opening a new club. And while Life Time’s return-on-capital was well below our portfolio average, we knew that metric would rise as each club steadily ramped up membership in excess of 12,000 members.

A key early modeling insight was that Life Time’s customers consistently spent higher and higher amounts inside the clubs on personal training, healthy food and spa services. This continued right through the recession and I believe is evidence that Life Time has carved out a niche of serving the most profitable customers in the industry.

What is your sell discipline?

We sell a stock if a company breaks thesis or has competitive weaknesses that make it no longer one of the highest quality growth stories in the small cap universe.

We are also quite disciplined about valuation, and will sell as the P/Es of our companies start to move well above the long term sustainable

earnings growth rate. We never count on a high expected future P/E in calculating our return assumptions.

How do you execute your portfolio construction?

Typically, we own between 50 and 60 companies. A typical starter position for us is .75 to 1%, and our top 10 holdings are typically 3% to 5% weights.

We don’t use the benchmark to construct our portfolios. The portfolio is the expression of our bottom-up stock picking. We never use the words “exposure to a sector” or “exposure to a theme” in order to make investment decisions. A portfolio company has to stand on the merits of its business model and the future earnings we expect that company to generate, irrespective of what themes or sectors may be strongest in the market at any given time.

For example, we have been chronically underweight energy and high technology, two of the more volatile--both to the positive and the negative--sectors of the market over the last year. In the energy sector, it is difficult to find sustainable competitive advantage stories, especially when the bulk of the economics are predicated on the direction of the commodity price. In high technology, it’s difficult to predict what a company will earn 6 months from now, let alone over the 5-year time frame we use in our models.

What do you consider risk and how do you manage it?

The biggest risk that I consider is misreading a company and investing in a business and management that I think are high quality and then realizing they are not. These are tough lessons, but they are invaluable teachers. We have a deep file of lessons learned.

We safeguard against risk with our due diligence and by focusing on quality. When stock prices are down, we use it as a signal to recheck our thesis and make sure we understand a businesses and its growth potential. Then, we will typically buy more.

Lastly, a great advantage of investing in high-quality businesses that grow organically is that when the economy weakens, and markets sell off, our companies typically outperform. It tends to be a good risk control for us as well as anyone looking to invest in our fund. 

Wasatch Core Growth Fund

Symbol **WGROX**
 Website www.wasatchfunds.com
 Address Wasatch Funds
 150 Social Hall Avenue
 4th Floor
 Salt Lake City, UT 84111
 Telephone 801-533-0777
 Inception 12/06/1986

PORTFOLIO CHARACTERISTICS*

Total Fund Assets	\$442 M
Median Market Cap	\$1,166 M
Weighted Avg. Mkt. Cap	\$2,351 M
P/E Ratio (Trailing 12 Mo.)	18.7
Est. 5-Yr EPS Growth	19.3%
Number of Holdings	60
Alpha (10-Yr)	-0.01
Beta (10-Yr)	0.93
Portfolio Turnover	27.09%

INVESTMENT INFORMATION

New Investment	Open
Investment Minimum	\$2,000

***AVG. ANN. TOTAL RETURNS VS. +RUSSELL 2000 INDEX**

	WGROX	Index
1 Year	8.95%	-3.53%
3 Years	7.88%	-0.37%
5 Years	1.52%	-1.02%
10 Years	5.50%	6.12%
Since Inception	11.32%	7.96%

***AVG. ANN. TOTAL RETURNS VS. ++RUSSELL 2000 GROWTH INDEX**

	WGROX	Index
1 Year	8.95%	-1.12%
3 Years	7.88%	2.07%
5 Years	1.52%	0.96%
10 Years	5.50%	5.45%
Since Inception	11.32%	5.97%

FEES AND EXPENSES

Sales Charge	None
Gross Expense Ratio	1.41%
Net Expense Ratio	1.41%

PORTFOLIO MANAGERS

JB Taylor	2000
Paul Lambert	2005

09/30/2011; Source: Company Documents

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Data shows past performance. Past performance is not indicative of future performance and current performance may be lower or higher than the data quoted. For the most recent month-end performance data, visit www.wasatchfunds.com. Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost.

The statements and opinions expressed in this article are those of Ticker.com. Any discussion of investments and investment strategies represents the Funds' investments and Portfolio Managers' views as of the date of the article and are subject to change without notice. The investment objective of The Wasatch Core Growth Fund is long-term growth of capital. There is no guarantee or assurance the Fund's goals will be achieved.

The investment objective of Wasatch Core Growth Fund is long-term growth of capital. Total Expense Ratio: 1.41%. The Advisor may absorb certain Fund expenses, leading to higher total shareholder returns. Wasatch Funds will deduct a 2.00% redemption fee on Fund shares held 60 days or less. Performance data does not reflect this redemption fee or taxes

Wasatch Funds are subject to risks, including loss of principal.

*Data through 9/30/2011 and is subject to change.

Investing in small cap funds will be more volatile and loss of principal could be greater than investing in large cap or more diversified funds.

An investor should consider investment objectives, risks, charges and expenses carefully before investing. To obtain a prospectus, which contains this and other information, visit www.wasatchfunds.com or call 800.551.1700. Please read the prospectus carefully before investing.

+The Russell 2000 Index represents the smallest 2,000 companies in the Russell 3000 Index, as ranked by total market capitalization. The Index is unmanaged and widely considered to accurately capture the universe of small company stocks. ++The Russell 2000 Growth Index measures the performance of Russell 2000 Index companies with higher price-to-book ratios and higher forecasted growth values. You cannot invest directly in these or any indices.

(ROA) Return on assets measures a company's profitability by showing how many dollars of earnings a company derives from each dollar of assets it controls.

The Price-to-Earnings (P/E) ratio is a valuation ratio of a company's current share price compared to its per-share earnings.

EPS (Earnings Per Share) is a measure of a company's earnings per share for the year.

Alpha is a measure of a fund's risk/reward potential. A positive alpha means the fund outperformed the index. A negative alpha means the fund underperformed the index.

Beta is the measure of a fund's risk in relation to the market. A beta of 0.8 means the fund's total return is likely to move up or down 80% of the market change; 1.25 means total return is likely to move up or down 25% more than the market. Beta is referred to as an index of the systematic risk due to general market conditions that cannot be diversified away.

The ten holdings for Wasatch Core Growth Fund as of September 30, 2011 were: Copart, Inc. 5.5%, DFC Global Corp. 3.8%, Life Time Fitness, Inc. 3.4%, Waste Connections, Inc. 3.2%, IDEX Corp. 3.2%, Alliance Data Systems, Corp. 3.2%, Polypore International, Inc. 3.2%, MEDNAX, Inc. 3.1%, Herbalife Ltd. 3.0%, Monro Muffler Brake, Inc. 2.7%. Current and future portfolio holdings are subject to risks and may change at any time. References to specific securities should not be construed as recommendations by the Fund or its Advisor.



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