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Bruce Berkowitz: Saving St. Joe

Bruce Berkowitz, who led his Fairholme Fund to top returns, is focused on turning around St. Joe Company

FAIRHOLME AT A GLANCE

- Based: Miami
- Fairholme Capital Management: the privately owned investment advisor that manages the Fairholme Funds.
- Fairholme Funds: \$23 billion in total, owned by shareholders, including the Fairholme Fund (FAIRX), and the newer, smaller Fairholme Asset Allocation Fund (FAAFX) and Fairholme Focused Income Fund (FOCIX).
- Fairholme Fund's return: about 11.4 percent per year since its inception Dec. 29, 1999, or 194.5 percent cumulative, compared to a 2.62 percent per year increase for the S&P 500 Index. Year to date 2011, as of Thursday,

BY INA PAIVA CORDLE
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Bruce Berkowitz's mind is racing with thoughts of Asia and Northwest Florida.

The Miami-based mutual fund manager has recently returned from trips to the Panhandle and South Korea, Singapore and Hong Kong. His \$23 billion Fairholme Funds have invested \$1.5 billion in two Chinese insurance companies during the past few months. And next week, he and Fairholme Capital Management President Charlie Fernandez will host the chairman of the huge

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- Major stock holdings include: AIG, Goldman Sachs, Bank of America Corp., Citigroup, Morgan Stanley, Sears Holdings, Regions Financial, Berkshire Hathaway, St. Joe Company.

- Minimum purchase: \$10,000.

THE ST. JOE COMPANY AT A GLANCE

- Based: WaterSound, Fla.

- Ticker: JOE on the New York Stock Exchange

- Business: real estate development, with 574,000 acres of land concentrated primarily in Northwest Florida between Tallahassee and Destin, including 5.5 miles of beach along the Gulf of Mexico, four golf courses and two hotels.

- Recent financial results: Loss of \$35.9 million in 2010; loss of \$130 million in 2009.

BRUCE BERKOWITZ AT A GLANCE

- Current titles: founder, managing member and chief investment officer of Fairholme Capital Management, president and a director of Fairholme Funds, and chairman and a director of the St. Joe Company.

- Age: 52

- Education: Bachelor of Arts in Economics from the University of Massachusetts at Amherst in 1980

- Personal: married since 1980 to Tracey Berkowitz, three children, ages 25, 22 and 18.

- First rule of investing: "Don't lose."

state-owned Chinese Pacific Insurance Corp. on his first trip to Miami. They will tour the Panhandle and discuss business opportunities on the land owned by the St. Joe Company.

Since Fairholme bought a 29 percent stake in St. Joe, Berkowitz has publicly struggled — and succeeded — in maneuvering the ouster of the storied real estate development company's top executives and the majority of its board. A month ago, he took the board's helm as chairman, and named Fernandez vice chairman and former Governor Charlie Crist and Carnival Corp. Vice Chairman Howard Frank as directors. He also brought in a new chief operating officer, Park Brady.

"We plan to very quickly do what needs to be done to move St. Joe forward," said Berkowitz, 52. "Acquisitions, hiring, restructuring, capital raising — we're open to all the possibilities."

Berkowitz's fight to turn around money-losing St. Joe has placed a brighter spotlight on the unassuming multimillionaire, dubbed "the megamind of Miami" in December by Fortune Magazine.

In fact, agreeing to be interviewed for this story required some soul searching. After all, he said, he lives here and likes to walk into a restaurant and not worry about being recognized.

But even before St. Joe, Berkowitz had made a name for himself and his Fairholme Fund, which

he founded Dec. 29, 1999 in Short Hills, N.J. and in 2006 moved it to Miami. In January 2010, Morningstar named Berkowitz, founder and managing member of Fairholme Capital Management, the domestic stock fund manager of the decade, and 2009 Domestic-Stock Fund Manager of the Year. And Lipper recently

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ranked Fairholme's performance No. 1 in 5-year and 10-year returns, among 244 and 102 funds, respectively, with similar investment objectives.

In fact, during the past 10 years, the Fairholme Fund has appreciated about 11.4 percent per year, compared to a 2.62 percent per year increase for the S&P 500 Index. That means that \$10,000 invested in The Fairholme Fund at its inception, with dividends reinvested, has grown to \$44,263, while \$10,000 invested in the S&P 500 with dividends reinvested has increased to \$11,118.

"That's yesterday's news," Berkowitz responds to his fund's past performance. "It's about what we do in the future."

His investment philosophy, he said, boils down to one mantra: "Don't lose." Fairholme invests in 20 companies, with about 50 percent of its portfolio in financial services. Its investments have made Fairholme the largest private investor in AIG, and the largest owner of shares in Regions Financial Corp. and CIT Group. It's the second largest owner of shares of Sears Holdings Corp. and among the top five owners of Citigroup, Bank of America Corp., Goldman Sachs and Morgan Stanley. Fairholme also holds about \$6 billion in cash.

"We're very much involved with the restructuring of corporate America's balance sheets, as the country rises from the Great Recession," Berkowitz said, during breakfast of eggs benedict, tomato juice and Earl Grey tea in the outdoor courtyard of the Fontana Restaurant at the Biltmore Hotel in Coral Gables on a recent Saturday.

Berkowitz, himself, has all of his family's money, or more than \$300 million, invested in his primary fund and two newer, smaller Fairholme funds, according to Morningstar. The funds have about 500,000

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and two newer, smaller Fairholme funds, according to Morningstar. The funds have about 500,000 investors.

Lately, the fund has focused on companies in stressed industries, and has turned to insurance companies in Asia, where the middle class is growing. The fund's investment in China Pacific makes it the third largest private shareholder. In China alone, 27 million people are moving from the country to the cities, each year — almost the size of Canada's population, Fernandez said.

Though Fairholme has been actively focused on St. Joe, whose stock it began buying a few years ago, the company represents just 2.6 percent of the fund's investments.

"It's very unusual for mutual fund managers, and for Bruce, to become so active in a particular holding," said Ryan Leggio, mutual fund analyst with Morningstar, an independent investment research firm based in Chicago, which gives the fund its five-star rating. "From the moment he announced his active position to now, he has probably saved St. Joe shareholders a lot of money, and has made money, and will make more money for Fairholme shareholders because of his actions."

Berkowitz left his position as managing director at Salomon Smith Barney to start Fairholme, named after the street he had last lived at in London when he worked for Lehman Brothers.

"I had certain ideas that were non-traditional and would not work well in a large firm," he said, citing fewer, bigger and very focused investments and nonpublic investments that are not typical of a mutual fund.

His clients followed him to Fairholme.

Carnival's Frank met Berkowitz when Berkowitz managed one of the portfolios Frank had personally invested in at Salomon Smith Barney. Frank later rolled his investments into Fairholme, and serves as a director of Fairholme, in addition to St. Joe.

"He clearly has one of the best track records on Wall Street," Frank said. "He has a unique investing style that has been enormously successful."

Wearing jeans, a light blue shirt and boat shoes, Berkowitz's relaxed demeanor belies his serious intent. Fernandez calls him the most focused and detailed person he knows.

"I've never met anyone who can dig as deep as Bruce," he said.

Berkowitz said he has also been told he is a little impatient. He sees a solution and wants to jump ahead, rather than dealing with legal intricacies, Fernandez said.

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Berkowitz views investing like managing a business as a silent partner, and the philosophy has no doubt translated to Fairholme's performance. Among the fund's greatest successes was its investment in mall owner General Growth Properties, which resulted in a \$1.4 billion profit for shareholders over a 10-month period. The fund also made a \$618 million profit over two years, on the sale of Americredit to General Motors.

But Fairholme hasn't had all positive returns. In 2008 the fund lost 29.7 percent — still not as steep as S&P's losses — and in 2002, lost 1.58 percent, according to its prospectus. And in 2009, the fund lost about \$80 million on its Wellcare investment. "In this business you have to trust, but verify," Berkowitz said. "Sometimes you misjudged management or the durability of a business."

He acknowledges that investors put a lot of trust in him. "It's a lot tougher to invest someone else's money than your own money, because of that trust," he said. "And a lot of shareholders are going to need that money and more."

Cesar Alvarez, executive chairman of the law firm Greenberg Traurig, met Berkowitz through Fernandez, and is an investor and on the Fairholme board. He said Berkowitz is rich in ideas, and doesn't have an ego that gets in the way.

"I have a great deal of confidence in him," Alvarez said of Berkowitz. "I think he combines a great intellect, a great passion for doing what is right for his investors and the shareholders, and something that few people have: he is intellectually honest. He can say 'I started on one course and it didn't work out,' and change direction."

SHAPING UP THE DAY

Tall, thin and fit, Berkowitz power walks at about 5 a.m. each day, with his right-hand man Fernandez, who lives next door in Coral Gables' exclusive Tahiti Beach enclave. In April 2008, Berkowitz paid \$14.2 million for his 14,495-square foot home on the water, and one month later, paid \$8.75 million for the house next door, later tearing it down to make it part of his yard.

Fernandez, 49, and Berkowitz met through Berkowitz's cousin Lauren, who Fernandez married four years ago, and who was the flower girl at Berkowitz's wedding nearly 31 years ago. Lauren's father, Robert Sturges, a partner in the Miami Heat, was previously president of the gaming division of Carnival Resorts and Casinos. Fernandez met his future father-in-law in 1988, through Fernandez's uncle, Amancio Suarez, who once owned Radio Mambi. Suarez was also previously a partner in the Miami Heat.

After their walk, Berkowitz heads to his home gym, where he has a treadmill, stairmaster and weights. Though Fairholme has an office on Biscayne Boulevard in Miami, where its 28 employees work, Berkowitz and Fernandez each retreat for the day to their home offices, which are connected virtually to

the main office. Berkowitz said he spends much of his day reading public company filings, while Fernandez spends six to seven hours working on the phone. They meet after the close of the market to rehuddle and discuss the day's activities, occasionally sharing martinis.

Overall, they say they work 18-hour days, six days a week.

BOOKMAKER AT 16

Berkowitz grew up in an apartment “on the wrong side of the railroad tracks.” in Chelsea, Mass., a working-class suburb of Boston. His father Barney was a taxi driver, bookmaker and shop owner. When his father suffered a heart attack when Berkowitz was 16, his son dropped out of school for three months and took over the bookmaking operation while he recovered.

The experience proved to be the best education, Berkowitz said, teaching him odds, probabilities, perverse psychology, and how the prospect of winning gave people hope. He likens Wall Street to a legal form of oddsmaking.

Berkowitz's first job was at 10 years old, delivering newspapers. He remembers walking through the dark hallways of apartment buildings, trying to find the light switch. His second job, at about 14, was working at the amusement park at Revere Beach in Massachusetts. He would sometimes stay overnight, to earn overtime at \$1.65 an hour, up from his usual \$1.30 an hour.

He went to college at the University of Massachusetts at Amherst, where he earned a bachelor's degree in economics. There, in the dorm, he met his wife Tracey. He lived on the second floor, “the rock and roll floor” and she on the third floor, “the disco floor,” which meant their friends didn't like each other, he quipped.

The two married the week Berkowitz graduated and turned 22. They have three children, sons 25 and 22, and a daughter, 18. Each has either graduated from, is attending or plans to attend the University of Miami.

It was Tracey who chose Miami in 2006 for their latest move, Berkowitz said.

“I wanted to get away from the noise of Wall Street,” he said. “I wanted to get more sun.” He also wanted a state without state taxes. And Tracey, who grew up in Boston, said she wanted to stay on the East Coast, where they both have family. Berkowitz's mother Hennie and sister Rhonda already lived in Aventura.

“Miami is still an underappreciated asset,” Berkowitz said. “Sometimes it's the south borough of New York and other times its Buenos Aires, which makes it fun and exciting.”

Tracey Berkowitz runs the family's Fairholme Foundation, as president and trustee. The couple put 20 percent of their income into the foundation, whose assets exceed \$100 million, she said. Their donations are primarily funneled into the local community, including the University of Miami, Miami Children's Hospital, the New World Symphony, the Friendship Circle and Big Brothers Big Sisters, as well as the Center for Jewish History in New York.

Bruce Berkowitz shrugs off his financial success, saying it doesn't make him different than anyone else, and that some people are just lucky that their minds are wired to enjoy poring through financial statements all day.

"Sometimes, I look up and it's 5 p.m. and I'm still in my workout clothes," he said, adding: "The problem is, I could look up and I'll be 92."

In fact, Berkowitz acknowledges that he doesn't really have any hobbies. He owns an electric guitar he hasn't touched in a year. He tried golf, but it didn't catch on. He owns a 28-foot Boston Whaler, but only uses it when he and Fernandez go out to lunch at Fisher Island. The closest thing to a hobby, he said, is scuba diving, which he took up on a vacation to the Spice Islands in Indonesia a few months ago. Rather than watch TV, he falls asleep listening to conference calls on his headphones. "It's my own version of the Tonight Show," he joked.

The family has a second home on the ocean in Bridgehampton in the Hamptons, where Berkowitz goes for weeks in the summer. Fernandez has a home in Bridgehampton too, next door to Ron Howard.

Fernandez grew up in Queens, N.Y., and moved to Miami in 1979 to attend Florida International University, where he graduated with a bachelor's degree in finance and international business. He started his career restructuring Asian companies, living in Hong Kong for a year and a half. Much of his career was spent working with companies controlled by Phillip Frost, and he was on the board of IVAX for seven years. He retired at 43, met Berkowitz a year later, and began working with him in 2007, when Fairholme had \$4.6 billion under management.

MAKING CONNECTIONS

Fernandez is more "people oriented," said Berkowitz, who once said of Fernandez: "It isn't just what he knows, but who he knows."

In fact, it was Fernandez who introduced Berkowitz a couple of months ago to former Governor Crist, who Berkowitz decided was perfect for St. Joe's board, because "he's so passionate for the people of Florida."

"They're wonderful people, and what they are doing for our state I'm very excited about, and I'm very

excited to be a part of it,” said Crist, who is now an attorney with Morgan & Morgan in St. Petersburg. “It’s quite a thrill.”

St. Joe is the largest private landowner in Northwest Florida, with 576,000 acres of land, including more than 300,000 acres surrounding the new Northwest Florida Beaches International Airport, which was 20 years in the making.

With a new board and new management, the plan now is to stop the losses, cut expenses and find new revenue opportunities, Fernandez said.

“St. Joe, at its core, is an asset management company,” Berkowitz said. “Successful asset management companies are very profitable. There’s no reason St. Joe can’t be profitable.”

Berkowitz and Fernandez talk excitedly about St. Joe’s prospects, citing the airport, the proximity to Eglin Air Force base, the 5.5 miles of beach along the Gulf of Mexico, two hotels and four golf courses. The company, valued at \$2.5 billion, has a stock price that values its land at just \$4,200 an acre. St. Joe has no debt, \$125 million in cash and has an abundance of land purchased in the 1930s and on its books at original costs of \$2 to \$3 an acre.

“When you think of how much land touches the Gulf, and an international airport right in the middle, and when you think of the infrastructure on the land, the bridges, highways, waterways, and the beauty of the area, it’s a very simple value equation,” Berkowitz said.

But lately, St. Joe’s financial results have been far from stellar. The company lost \$35.9 million in 2010, after losing \$130 million in 2009.

And its stock hasn’t gone unnoticed by short sellers, particularly hedge fund manager David Einhorn of Greenlight Capital. In a 137-page slide show he presented at the Value Investing Congress last October, he criticized St. Joe, citing, among other factors, that the new airport presents little opportunity, that many of St. Joe’s developments are ghost towns, and that the company is little more than a timber company. Einhorn declined to be interviewed. Berkowitz scoffs at Einhorn’s assessment.

ST. JOE’S ROOTS

St. Joe’s roots date back to the 1920s, when Alfred I. duPont, black sheep of the Delaware chemical family, and his brother-in-law Ed Ball bought up Panhandle land. A new chemical process had made it feasible to use low-grade southern slash pine to make pulpwood, and enormous quantities of timber were needed. With the acreage assembled, Ball founded St. Joe Paper in 1936 — after duPont’s death.

Yet while historians have written that the Panhandle was expected to be developed before Fort

Lauderdale or Boca Raton, opportunities were lost.

Fernandez recounts the story of how Walt Disney, in 1958, was scouting Florida locations for Disney World, and came to Ball's office. Ball reportedly kept him waiting for five hours, finally sending out his secretary with a note to Disney saying "I don't do business with carnival people."

Today, Berkowitz calls St. Joe's lands "the last frontier" of Florida.

Berkowitz and Fernandez's ideas for the company's land run from mining to manufacturing, forming an economic development zone to create new jobs, garnering investment from international companies, forming strategic partnerships with other real estate development companies, and making acquisitions of adjoining land.

The aim, said St. Joe director Frank, is to "take the company to the next level."

"Knowing Bruce," Frank said, "the direction he is going is to raise some capital to inject into St Joe, and to create a new business model for it."



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