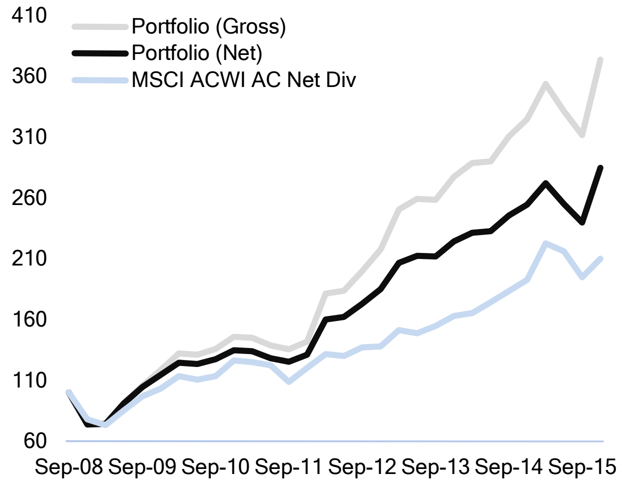
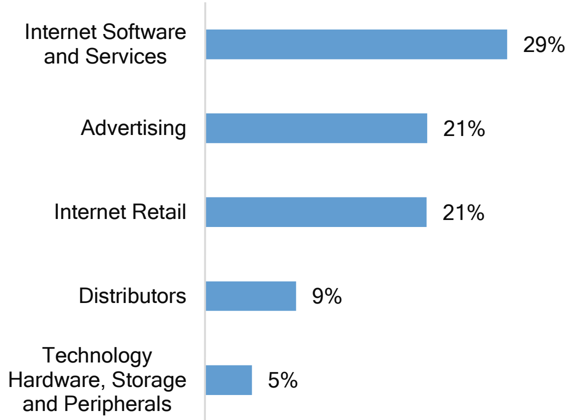
CORE PORTFOLIO — Q4 2015

		Performance (net of fees)	EUR[1]	Index[2]
Inception Date:	01 October 2008	**Quarter**	18.8%	7.8%
Portfolio Style:	Value / Total Return	**Last Twelve Months**	11.9%	9.0%
Manager:	Robert Leitz	**Since inception (annualized)**	15.5%	10.8%
		Since inception (cumulative)	184.8%	110.1%

Performance in EUR



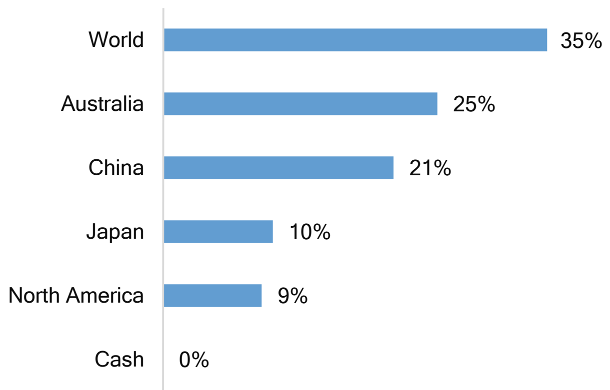
Top 5 Positions



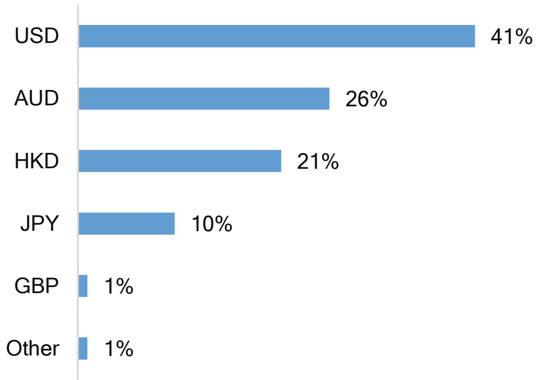
Market Review

Global equities delivered positive returns for the fourth quarter. In December, Wall Street celebrated a marginal and long-expected increase in U.S. interest rates as a historic event. At the end of 2015, U.S. 10-year Treasuries yielded 2%. It should be noted that the Federal Reserve's balance sheet is leveraged around 80:1 (with $4.5 trillion of assets invested in either Treasuries or junk assets) and U.S. debt/GDP ratios look equally unfavorable, especially when considering unfunded Medicare and social security liabilities as well as record low interest rates to support government spending levels. Also in December, an academic study revealed that European central banks had quietly – and likely illegally - bought half a trillion dollars' worth of assets. These purchases compliment the European Central Bank's well-known $1.6 trillion quantitative easing program. Despite (or because of) these highly inflationary policies, at year-end, $2 trillion of Euroland debt was trading at negative yields. Emerging market equities underperformed their developed world counterparts amid further pressure on commodity prices and the end of speculative excesses in China. The U.S. dollar kept strengthening against most other currencies, especially those of commodity-exporting nations. The high yield market was hit as the first large U.S. shale oil and coal companies entered bankruptcy.

Geographic Breakdown by Revenue Market



Geographic Breakdown by Listing Currency



[1] Net returns: no leverage, after all costs (no management fee, 25% performance fee for returns greater than 4% p.a., high watermark)
[2] MSCI All Country (DM+EM) World Index All Cap (large+mid+small+micro caps), net dividends reinvested

PORTFOLIO REVIEW

Since inception on October 1, 2008, the core portfolio has generated unleveraged net cumulative returns of +184.8% in EUR (+134.3% in USD) and annualized net returns of 15.5% in EUR (+12.5% in USD). In other words, €1.00 invested at inception has turned into €2.85 ($1.00 invested at inception has turned into $2.34).

The calendar year 2015 ended on a good note despite market headwinds caused by worries about a slowdown of the Chinese economy, weak commodity markets and declining currencies. The rebound in performance was mainly driven by company-specific events for two of the portfolio's holdings: one company started a buyback and reviewed its high-risk growth strategy, and the other used its cash reserves for a transformative acquisition at what appears to be a healthy multiple. Throughout the year's first three quarters, I kept adding to these positions as proceeds from realized gains became available. While this initially hurt performance as the share prices of the new investments kept declining, it finally did pay off in Q4. If my investment theses are right, there are further gains to come.

A smaller Australian holding was de-listed and I decided to stay on board as I consider the de-listing price to materially undervalue the company and because the company will continue to be run by what were capable owners in the past.

I exited one French family-controlled holding company with a small portfolio of stable, cash-generative businesses and good capital allocation to recycle the proceeds into what I currently consider more attractive opportunities.

In hindsight, my biggest mistake in 2015 was to overpay for companies in turnaround situations. In all but one case, profits declined faster and more severely than I deemed likely. Management guidance didn't prove to be any help, either. In one case, it was outright misleading.

The portfolio was fully invested as of year-end.

THOUGHTS ON VALUE INVESTING

Simple doesn't mean easy.

Last year, fifty thousand people made the pilgrimage to Berkshire Hathaway's annual meeting in Omaha to hear the most famous value investor, Warren Buffett, speak live. Millions more read about the meeting in the press. His ever-growing riches and brilliant Q&A sessions have turned Warren into a household name with rock star status.

If one of the most successful investors in history is giving his secrets away as openly as he seems to be doing - how many of Warren's followers are actually beating the markets and why aren't markets more efficient?

I believe successful investing requires more than subscribing to and understanding its principles. It requires a certain mentality, the right setup, and a healthy portion of luck.

A game of probabilities

Nothing is certain. Investing, like everything else in life, is a game of probabilities. Value investing doesn't guarantee high profits or protection from losses, but it is a strategy to maximize returns and minimize losses over many transactions if applied correctly and consistently. Indeed, most accomplished value investors succeeded by betting sparsely when the odds were strongly in their favor.

In my experience, pricing risk often requires going against human intuition, as humans tend to be carried away by mental shortcuts, cognitive biases or social constraints, which often lead to the wrong conclusions. It seems the greatest value investors share one characteristic: they possess a set of mental models that help them think in probabilistic decision trees. They are skilled in understanding the flaws of human cognition and they pursue a disciplined approach to overcome them personally. I strive to be one of them.

It's an art, not a science

As most readers will know, value investing can be defined as buying a business for less than what it's worth – whereby the value of a business is defined by the value of all future cash distributions.

While most people immediately accept this definition, their understanding of what value means and how it can be measured varies greatly. Every time I speak to like-minded value investors about their interpretation of value, valuation techniques and investing styles, I get several different answers.

Although it's easy to come up with a value for a business, it's very difficult to come up with the "right" value. A study of the buy and sell recommendations of analysts and investment bankers will reveal that even "sophisticated" valuations are often wrong – in my experience more often wrong than right.

It’s a fact that the market tends to overshoot on the downside as well as on the upside, be it in short-term trading (a stock gaining momentum) or through market cycles (e.g. through temporary over-allocation of capital to a specific sector, geography or asset class). Over the last few years, I realized how important it is to watch capital flows and how capital flows can skew market prices and common valuation metrics for long periods of time.

The importance of patient capital

Most people intuitively understand that value investing works best with a loyal investor base or almost permanent capital such as insurance float. This is because an investment’s value is expected to be realized either through future cash flows or a market re-rating. The latter brings future profits forward, but only to those who sell their stakes.

Most of us understand that missteps are built into the investing equation and that illiquidity and volatility present opportunity rather than signify risk. Yet, how many funds do you know of that are free from the pressure of quarterly withdrawals?

Truly patient capital is an extremely sparse resource. Indeed, this is another reason why value investing works: having patient capital in an increasingly short term-oriented world might be the biggest edge an investor can have. Ironically, institutional pools of capital that should be most interested in value investing – pension funds and life insurances – tend to not allocate money to value funds, or they tend to pull money in a period of volatility. The other large group, retail investors, lacks the knowledge and access to invest in value funds. Regulation isn’t helping either, as it often forces institutional capital to invest into so-called “safe” products (even if this means buying Treasuries at negative yields) or it pushes retail investors into commission-driven products from large institutional firms by raising the bar for smaller players.

However, the challenge is not just finding patient capital, the challenge is to also withstand periods of higher volatility as a portfolio manager. Famed investors like Charlie Munger or Joel Greenblatt have commented on the challenge of withstanding periods of higher volatility, especially when managing outside capital. Facing temporary mark-to-market losses is painful if it’s your own money, but can be humiliating and shameful if it’s the money of friends, family and clients. Some of the most successful investors therefore decline to accept client capital.

Overcoming institutional restrictions

It needs to be questioned whether prevailing institutional setups are sufficiently tailored to support value investing strategies. In my experience, few institutions encourage sustainable, long-term risk taking as this often requires taking contrarian positions and the ability to withstand volatility.

Most portfolio managers and analysts are employees of larger firms. Hence their investment decisions are mostly driven by two factors: career risk and the next bonus package. Arguably, successfully navigating corporate politics is more important to them than generating sustainable outperformance. It's a known fact that social settings tend to favor those who know how to market themselves, individuals following the contemporary consensus or those who show spectacular results, regardless of how they were achieved. Psychological factors are leveraged by the fact that most institutional investment decisions are being made in committees, not through individual people.

Research and portfolio management roles are commonly separated into separate hierarchical functions, whereby research is in the hands of junior employees and portfolio management in the hands of senior employees. While the analyst's job and bonus package is traditionally at the mercy of the portfolio manager, the latter's fate is often tied to a specific sector, geography or asset class. As they say: "markets make (and break) managers".

Compare this to Berkshire Hathaway, where one man is managing a $500 billion balance sheet alone, without advice, and with the vast majority of his personal wealth tied to the success of the company. In the few cases where Warren Buffett hired investment managers, he gave them a pool of capital to manage at their own discretion and with a surprising degree of loyalty over the years. Granted, Warren gives the managers of his subsidiaries maximum freedom, but he could step in at any time with maximum force if he so desired.

It should further be noted how Warren's investing style has changed over the years. Initially, he bought minority stakes in small, heavily discounted companies. Over time, as his portfolio grew, he was able to take control of the companies he invested in to reallocate cash flows at his discretion. Once his portfolio reached considerable size and he became a public figure managing a public vehicle, he changed his investing style again by adding structural leverage (insurance float) to acquire solid cash generators. His ability to raise cash when needed and take control of cash flows, reallocate and leverage them materially contributed to the growth of Berkshire Hathaway. That's a bit more than just "buying shares of high-quality businesses at a fair price".

How many fund setups do you know of that provide a similar degree of flexibility and structural benefits?

PORTFOLIO OUTLOOK

The commodity sector continues to be under pressure, high yield markets have recently sold off, emerging-market currencies have weakened, and monetary policies around the world remain highly inflationary. Such an environment usually provides good hunting opportunities.

Here is a bit of color on the portfolio's key positions (in order of magnitude):

1. A company going through a turnaround that recently spent its huge cash reserves on a transformative acquisition of a growing, profitable and capital-light business at what appears to be a healthy valuation. The impact of the acquisition will only become visible in the numbers in 2016. I consider the company greatly undervalued given its current profitability and potential. However, the company is in need of a new, more credible CEO.
2. A great compounder with shareholder-friendly management trading at a significant discount to intrinsic value.
3. A small company investing all the cash it generates from a good business into a new – and thus far unprofitable – geography. The market seems to only value the company based on the heavily depressed profitability of the combined (old + new) business without giving any credit to the cash-gushing established business or the growth opportunity of the new business.
4. A basket of profitable Japanese companies trading below net cash and at healthy earnings multiples.
5. A small, profitable distribution business trading below net working capital that is an obvious takeover target in a consolidating industry and trading well below historic M&A valuations. I expect the business to benefit from lower fuel prices. Unfortunately, the significant upside is mitigated by dilutive management compensation (the chairman/CEO is also a material shareholder).
6. A technology company that was slow to respond to a market shift. The company is trading at a low multiple to current earnings and buying back shares with cash reserves that equal 50% of market capitalization. I expect the company to benefit from continued market growth (cloud services) and a wide client base as management is repositioning the product offering.
7. A (now delisted) company operating in a cyclical industry but with a flexible cost structure and low capital requirements. The near-term market outlook is much more challenging than I originally assumed (I underestimated the size and severity of industry overcapacities).

As always, I am happy to receive feedback and answer your questions.

Robert

PERFORMANCE & BENCHMARKING

%	in EUR							in USD		
	Q1 Net	Q2 Net	Q3 Net	Q4 Net	Portfolio Gross	Portfolio Net	MSCI ACWI AC Net Div[2]	Portfolio Gross	Portfolio Net	MSCI ACWI AC Net Div[2]
2008	-	-	-	-26.2	-26.2	-26.2	-21.9	-26.3	-26.3	-22.7
2009	0.7	22.6	14.7	9.5	60.6	55.0	32.3	64.5	58.0	36.6
2010	8.8	-0.7	3.2	5.7	22.9	17.8	22.5	14.7	11.8	14.5
2011	-0.5	-4.3	-2.3	4.6	-2.7	-2.7	-4.9	-5.8	-6.7	-8.0
2012	22.1	1.2	6.8	6.9	53.4	41.1	14.6	56.3	45.9	16.4
2013	11.7	2.8	-0.3	5.8	27.6	21.2	18.3	32.9	25.2	23.6
2014	3.3	0.5	5.5	3.7	17.0	13.6	18.2	3.0	2.3	3.8
2015	6.9	-6.3	-6.0	18.8	15.0	11.9	9.0	3.2	3.2	-2.2
Annualized					19.9	15.5	10.8	15.8	12.5	6.9
Total Since Inception					273.7	184.8	110.1	189.5	134.3	62.5

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Net returns: no leverage, after all costs (no management fee, 25% performance fee for returns greater than 4% p.a., high watermark)
Index: MSCI All Country World Index All Capitalizations with net dividends reinvested