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MARKET BULLETIN MARCH 16, 2016

I have typically reserved writing intra-quarterly letters for dramatic and uncommon market landscapes.

At this moment such a drama is being played out in important subsectors of the market rather than being reflected in the overall indices. The S&P's -15% decline from July to February is not particularly remarkable. However, the rout in the broad commodity sector (and related areas) has been every bit as vibrant as most of the major sell-offs of the past 30 years.

I was prompted to write this letter in part because the fever pitch of the selling, the degree of disconnect between valuations and underlying asset values, and the sharp nature of the recent bounce, are each consistent with a sell-off that has finally run its course. But whether that is the case, or if that final capitulation sell-off is still some number of months in front of us it is an appropriate time to address where we are in the process, provide some guidance as to what we are doing about it in the portfolio, and offer our view of how the markets are likely to perform once the dust has settled.

First, one should be cognizant that the initial bounce for the companies in the epicenter of these crises can be exceedingly sharp and impactful. Second, after the initial bounce, those companies that are well positioned will begin gradual, multi-year advances. Those that are not may bounce initially, but then will continue to wither away. During the tech-collapse in 2000-02 it hardly mattered what you owned; virtually everything in that sector went down. On the initial bounces, most securities advanced. But through the meltdown and the first bounce there were great individual opportunities created. And being able to distinguish between those that were well positioned and those that were not was critical, because the broad technology group suffered for many years after that dislocation. After that initial jump, many companies languished and wasted away, while some offered very meaningful subsequent advances. The same could be said for the financial panic of 2008-09. Select financial company and real estate related investments that we put into the portfolio helped power a massive advance – and not just in the few months following the bottom – but for quite a number of years. But through that extended recovery, discernment mattered, because many investments in that sector never recovered. And the sector as a whole underperformed for nearly a decade.

Those examples invite a discussion of the next major point. In those cases, the melt-down in a specific sector ultimately broadened out to an overall credit crunch and historically noteworthy 50% bear markets. (Uncomfortably, they also played out in the period leading up to the end of a two-term president's tenure.) However, both the high yield bond/savings and loan meltdown of 1989-90, and the emerging markets/Long Term Capital debacle of 1997-98 appeared to me to be every bit as vibrant and deep as the current commodity oriented sell-off. But they did not resolve into wholesale declines.

Rather, as those sell-offs ran their course, new market leadership emerged to carry the broad indices higher for extended periods. As the current bull market is passing its seventh anniversary this week, it is worth noting that advances of this length almost inevitably must push through large corrections within important groups. This "rolling bear market" is part of a rotation that allows the advance to continue on "fresh legs." From both a macro-economic perspective and from a technical perspective, this recent decline strikes me as being more analogous to those sector-oriented sell-offs that did not lead to collapse than it is to those that did.

The type of rebound we have seen in the portfolio over the past several weeks is consistent with classic bounces off a market bottom. On a security specific basis, these moves have been as sharp as those we saw off the bottom of the high yield crash of 1990-91, the emerging markets meltdown of 1996-97, the Bear Market of 2000-02, and the Financial Panic of 2008-09. In the past three weeks we have seen quite a number of our individual holdings spring 50-100% higher. Clearly we do not expect this tempo of advance to continue. However, in the past these sharp bounces have typically ushered in multi-year periods of recovery. While one can never be sure, this period may well be here.

Through these tumultuous periods our strategy is consistent. We commit capital to enterprises that are battered by the market turmoil. But we do our homework first. That means identifying the enterprises that have the wherewithal to emerge from the crisis with their assets – and our investment - intact. And we do that as the crisis unfolds. That means buying things as prices contract.

The past three weeks illustrate why that is important. Over that period the recent market meltdown has reversed. As the market has melted up, liquidity has disappeared. Prices have gapped higher. At times the pace of advance has been almost disorienting. I do not find it realistic to attempt to add to exposure in these moments when issues get sucked into hollow air pockets above them. Here are a couple of examples from our portfolio of this type of activity.

	FEBRUARY LOW*	MARCH PEAK*
Cliffs 6.25% due 2040	8	24
Chesapeake 5% due 2023	14.5	28
Mesabi Trust (January low)	3.12	7.63
Bombardier	0.54	0.96
Williams Partners	13.26	23.14

A general description of our actions this year is hopefully very much what you would expect from reading our commentary over the years. Despite the recent volatile upward moves, we have still found some opportunities to add to our exposure in various instruments as they have become increasingly compelling.

Our additions to the portfolio included a new core name and increased exposure to a previous holding through the purchase of senior securities. Specifically, in January we added a 2.5% position in Cheniere Energy Partners Holdings at a cost in the 14s. In February we bought a 4.5% position in Rowan Companies 5.4% Notes due 2023 at approximately 49% of par. We expect each of these to trade 50% higher within the year.

From this overview I hope that a few things are clear. We continue to see opportunity in the markets and particularly in these turbulent times we continue to apply our process consistently. It is impossible to know when the bottom is, so we buy quality assets when they become too cheap for us not to buy them—even as we recognize that they may get cheaper before they rebound. The substance of the recent rolling bear market may be behind us and may have refreshed the bull market that has languished for the past 18months, giving it fresh legs and the opportunity to resume its march higher.

After a disappointing '15 and a very trying open to '16, we have now pulled to within yards of the S&P for the year. And while it is nice to be back in the race, we consider investing to be more of a marathon than a sprint. To us, the important point is that we are able to do well and continue this work over periods measured in years, not periods measured in months or quarters. Whether the market moves higher from here or takes some months to do so, we have historically had some of our best periods of performance after these kinds of environments have run their course. From what we see in our portfolio and in the world around us we believe we have an opportunity to see this kind of result again.

Charles Lemonides CFA

*Range based upon end-of-day internal valuations. Actual trading ranges were typically wider.