

May 2, 2016**First Quarter 2016 Investor Letter**

I wanted to use the occasion of the first quarter letter to explain White Brook Capital's ("White Brook") or ("Firm") philosophy and process. I believe these are two of the main factors that should be paramount in your decision to allocate capital with an investment manager, whether it's White Brook or another firm.

I expect that White Brook will mean different things to different clients. First and foremost, I am a stock picker. Therefore, White Brook is an asset manager. These quarterly letters, the monthly commentaries, and any other missives will generally focus on providing clients with a better understanding of my views on market related matters. I believe I have a different voice, and investing in the markets is what I love to do. Even as the Firm and our capabilities grow, I will take full responsibility for the investment performance. These forums will be my method of explaining what is going on in the equity markets, how your portfolio has performed, and why.

More broadly I would like White Brook to be your first point of contact as you more generally think about your financial well-being. Feel free to reach out as you consider financial plans – tax and estate planning, starting a business, investing in real estate, etc. If someone at White Brook doesn't have the answer to your question or is not an expert, we'll find someone you can trust to provide expert advice in order for you to make an informed decision.

The vision/purpose of White Brook is to provide high quality financial advice, at a reasonable price, with the clients' best interests in mind at all times. As I picked vendors to support White Brook's efforts, I chose Box for document management because the quality and completeness of its encryption and its ease of use are unsurpassed. The financial planning engine White Brook offers is quite simply the best, and our custodian has the best customer service for both client and advisor. As I continue to build our technological and human capabilities, compiling the Best will be the priority.

In terms of investing your capital, I will structure each client's portfolio to best fit their investment objectives - whether that means restricting a portfolio due to insider restrictions or building customized income producing portfolios, including high dividend paying stocks or fixed income portfolios. However, my belief is that the model portfolio I construct and personally invest in is the best way to generate a long term return on capital.

I describe my investing philosophy as "Mid-Down" in contrast to the traditional "Bottom-Up" and "Top-Down" approaches of many of my contemporaries. Bottom-Up investors start by ascertaining whether a particular company is "cheap", while Top-Down investors start with asset class analysis. In contrast, "Mid-Down" emphasizes industry level analysis with a focus on the health of the industry, the company's customer, and the necessity of the company's product in the future. I am focused on micro trends, their impact on customers' decision making, and whether that micro trend can create a strong sustained trend moving forward that elevates a company's relationship with its customer. I believe that while a "diet" version of this analysis is engaged in by others on the street, the process is underappreciated and summarized by a check next to an item on a list, rather than focused on, flushed out, and thought of as needing to be significant enough a change that it can form the basis for a

multiyear thesis. Finally, I focus on how a company turns a dollar of revenue today into Free Cash Flow (“FCF”) tomorrow. In that analysis, I’m able to analyze the intellectual property that defines a company and judge whether it improves or degrades over time.

In addition to my analysis of a company’s ability to generate wealth, I also focus on whether the company is a “Good” corporate actor. By my definition, most companies that operate outside of industries associated with vice, defense, and high interest loans are socially responsible, but occasionally a company will do wrong even while pursuing admirable goals. The U.S.’s pharmaceutical industry is currently being admonished in the press and by Congress because they raised prices on needed drugs with little competition. I agree with Congress that they deserve admonishment. I believe there is a distinction between a drug used for discretionary plastic surgery and an orphan drug. While a company that so dramatically increases the prices of its goods would cross a line for me, I would find the makers of the plastic surgery drug to be within their rights while those who developed orphan drugs to be exploiting a populace, and therefore uninvestable. This is antithetical to Impact Investing, but I believe companies should be “Good” corporate actors, not just corporations who do good. I won’t always discover potential impropriety and won’t always agree with clients about what is an offense, but I will make qualified moral judgements that are separate from my judgements about the quality and valuation of the business but carry the same weight. I believe this is a defining and differentiating characteristic of White Brook.

In terms of portfolio construction, I believe it’s a fruitless exercise to project the direction of the S&P500, so client portfolios will usually be over 90% invested. I’m also dismissive of the sector weightings of the S&P500 and will strongly overweight certain sectors if companies in those sectors are attractive – up to ~30%. The model portfolio will recommend between 20-30 companies at any one time with a maximum threshold of a 6% weighting in any one stock. The investment horizon for any particular stock is usually one year to forever. I will keep the beta of the portfolio below 1.2x and normally closer to 1. The portfolio is reviewed on a regular basis, primarily from a risk management perspective with the intent to ensure diversity of end markets and index inclusion as well as to enforce that hurdles on valuation, beta, and performance are achieved. By being overweight sectors, and being fairly concentrated, I would expect that the performance of White Brook will be somewhat uncorrelated with the performance of the S&P500.

I’ll leave you with a thought experiment that I believe differentiates how I think about investing. My expectation is that I’ll lead with one of these every 2 or 3 months in my monthly commentaries as I believe they illuminate how my thought process differs from my contemporaries and provides insight as to how I analyze the stocks I choose for your portfolio. Many investors look for “good management” before investing in a company’s stock. The belief is that management is the most direct steward of investor capital and therefore, has the greatest ability to create or destroy value. Furthermore, there is compelling evidence that good management teams lead to good stock performance. I believe, however, that most investors when applying this logic get the process backwards, believing good past stock performance means the management team are good, and lack a process for determining the quality of a management team before the stock begins to move. For years, I struggled with developing a process to reliably evaluate management before, inspired by the opening scenes of *“Catch Me if You Can”*, I developed a thought experiment that places management as player on *“To Tell the Truth”* and me as the contestant determining whether management is who they represent they are. In a situation where one third are right for the job and the other two thirds are trying to fool me, I developed several steps to



determine the real thing. First, I read management transcripts over a very long period of time looking for a change in message, priority, or philosophy. Second, I look for congruence in that message being disseminated throughout the organization. If the Company professes to make conservative projections and didn't before, I look for a change in accounting policy in the financial reports, a write down of goodwill, or another action that would confirm that assertion. If management professes a belief the stock is cheap, that sentiment carries more weight if there's proof that they lobbied their board for a higher blend of stock based compensation and not just additional salary that includes stock based compensation. Third, I may speak with management to gain a better understanding as to how the business works at the initial stages of an investment, but after those initial conversations, I limit my interaction. Between the limits of Regulation FD that prevents material financial disclosure in non-public venues and general bias of accomplished people, I find it difficult to have a frank and true discussion of the risks to a business or company endeavor. I, therefore, think that not speaking directly to a management team is a great way to evaluate a management team. These beliefs are the exact opposite of many Wall Street professionals, but I believe they have served me well in the past and will continue to serve my clients' portfolios well in the future.

I hope you enjoyed this first letter and now have a better understanding of White Brook Capital's investment philosophy. Please call or email me with any questions, comments, or opinions. I appreciate your interest and look forward to us working together in the near future.

Regards,

Basil Alsikafi
Portfolio Manager
White Brook Capital