FATALPHA
VALUE INVESTING

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INSIDE CURRENT ISSUE

During May, the portfolio made a comeback rising 3.11% vs 1.29% for the S&P 500. That puts FatAlpha at 4.6% vs 3.6% for the benchmark for 2015. Large gains were recorded by GTS (on earnings, up 28%), CBI (Einhorn upped his stake, 14%), GME (on earnings, 13%), TRN (bounce from last month, 11%), and ANTM (11%). On earnings, CTB dropped 14%, while KSS and ANF both dropped 9%.

Volatility has increased as investors are making hasty moves, selling one day and buying on another. For example, ANF rallied on earnings only to lose it all and more on a downgrade the next day. This has been a repeated theme the last two months, and could be due to the maturing of the bull market. As I showed in last month's letter, price action has been overlapping (see repeat of chart below). Fundamentals aren't terribly exciting either with the S&P trading at around 18-20x earnings. Despite this I believe this sideways action with short-term moves taking brief peeks at the highs to continue until we have a trigger event (unknown currently but could be rising rates, a Greek default, etc).

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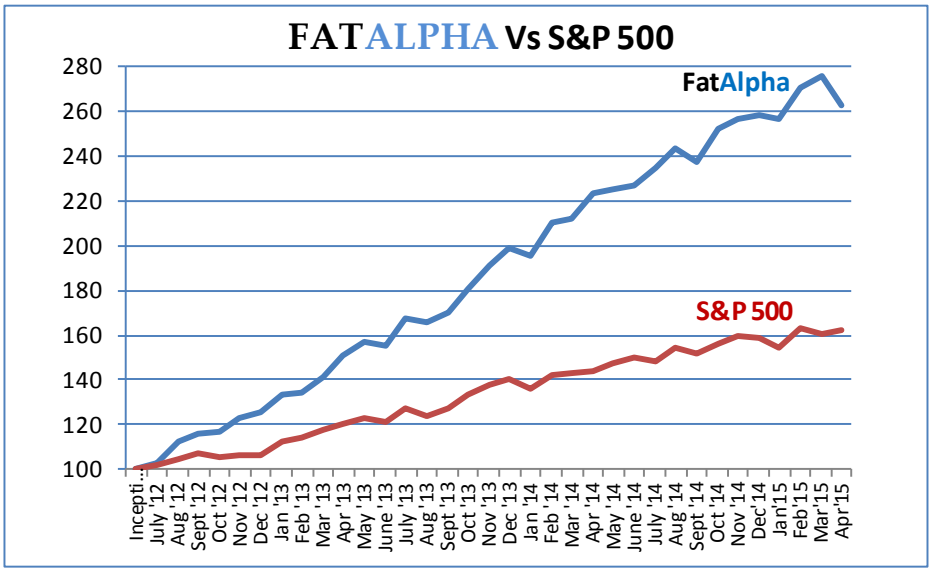
Performance

MONTHLY PERFORMANCE								
Yr/Mo	2015		2014		2013		2012	
	FatAlpha	S&P 500	FatAlpha	S&P 500	FatAlpha	S&P 500	FatAlpha	S&P 500
January	**-0.83%**	-2.51%	**-1.76%**	-3.09%	**6.45%**	5.72%		
February	**5.49%**	5.62%	**7.64%**	4.55%	**0.71%**	1.28%		
March	**1.84%**	-2.01%	**0.91%**	0.39%	**5.35%**	3.34%		
April	**-4.80%**	1.35%	**5.08%**	1.06%	**6.47%**	2.29%		
May	**3.11%**	1.29%	**0.97%**	2.32%	**4.19%**	2.36%		
June			**0.83%**	1.58%	**-0.73%**	-1.85%		
July			**3.17%**	-0.95%	**7.45%**	5.60%	**2.89%**	2.37%
August			**3.67%**	3.95%	**-1.00%**	-3.00%	**9.12%**	2.51%
September			**-2.39%**	-1.84%	**2.78%**	2.66%	**3.03%**	1.99%
October			**6.21%**	2.74%	**6.26%**	5.05%	**0.66%**	-1.36%
November			**1.78%**	2.75%	**5.50%**	2.96%	**5.58%**	0.57%
December			**0.86%**	-0.80%	**4.34%**	2.04%	**1.79%**	0.18%
Year	**4.58%**	3.57%	**29.95%**	13.08%	**59.01%**	31.97%	**25.14%**	6.36%
FatAlpha beat S&P 500 28 out of 35 months								

S&P DOWN MONTHS		
Month	FatAlpha	S&P 500
Oct-12	**0.66%**	-1.98%
Jun-13	**-0.73%**	-1.50%
Aug-13	**-1.00%**	-3.13%
Jan-14	**-1.76%**	-3.56%
Jul-14	**3.17%**	-1.51%
Sep-14	**-2.39%**	-1.55%
Dec-14	**0.86%**	-0.80%
Jan-15	**-0.83%**	-2.51%
Mar-15	**1.84%**	-2.01%
Average	**-0.02%**	-2.06%
Median	**-0.73%**	-1.98%
FatAlpha beat S&P 500 8 out 9 times		



SINCE INCEPTION:	FatAlpha	170.4%	Vs	S&P 500	64.4%

Google sends kids on virtual field trips:
http://finance.yahoo.com/news/students-see-the-world-for-a-few-bucks-151214753.html

Stiglitz: EU policy flawed:
http://bloom.bg/1B9jt1A

Pick the outlier :)
http://www.zerohedge.com/news/2015-05-21/shake-shock-spot-fast-food-outlier

WSJ recap of Ira Sohn Conference:
http://blogs.wsj.com/moneybeat/2015/05/04/from-einhorn-to-ackman-live-from-the-ira-sohn-conference/

Einhorn - Ira Sohn Conference:
http://www.valuewalk.com/2015/05/david-einhorn-at-2015-ira-sohn-conference-presentation-live/

Ackman – Ira Sohn Conference:
http://www.marketfolly.com/2015/05/bill-ackmans-sohn-conference_4.html

GMO: The Idolatry of Interest Rates
https://www.gmo.com/docs/default-source/research-and-commentary/strategies/asset-allocation/the-idolatry-of-interest-rates-part-1-chasing-will-'o-the-wisp.pdf?sfvrsn=6

Margin Debt Breaks Out: Hits New Record 50% Higher Than Last Bubble Peak
http://www.zerohedge.com/news/2015-05-29/margin-debt-breaks-out-hits-new-record-50-higher-last-bubble-peak

Trades

Date: **May 29th, 2015**
Ticker: JEC
Name: Jacobs Engineering
Transaction: Bought
Price: $43.25
Size: New position

Note:
JEC is an international engineering and construction company with major revenues (60%) from government, chemicals, and refining. The stock is cheap both relatively and compared to its own history. The weakness is based on potentially lower capex spending with falling oil and commodity prices. Despite the drop in oil, less than 10% of its business is directly related to oil & gas. The company has guided for $2.90-3.20 for the year while management believes they can grow EPS by 15% annually over the next 3-5 years.

Date: **May 29th, 2015**
Ticker: SANM
Name: Sanmina
Transaction: Sold
Price: $21.24
Size: Reduced position

Note:
SANM was one of the largest positions in the portfolio the last few months. Its small size (<$2B) has brought with it some volatility. More importantly, the industry (Electronic Equipment, Instruments & Components) is too heavily weighted in the portfolio. Hence it was reduced, making room for JEC.

Date: **May 22nd, 2015**
Ticker: SAFM
Name: Sanderson Farms
Transaction: Bought
Price: $83.95
Size: New position

Note:
Sanderson is the 3rd largest poultry producer in the US with annual sales at around $3 billion. Practically debt-free, SAFM, besides being a value play is also cheaper than its two larger competitors PPC and TSN. At an EV/EBITDA of 3.5x, the market appears to be pricing in a lot of bad things (i.e. lower chicken prices, higher

corn/soy prices, lower exports, and impact from Avian flu). So far the company has increased sales and operating profit for the last 4 quarters in a row, so I'm pretty comfortable with current valuation.

Date: **May 22nd, 2015**
Ticker: RS
Name: Reliance Steel & Aluminum
Transaction: Bought
Price: $65.32
Size: New position

Note:
The company provides metals processing to over 125k customers. In other words, RS is a fabricator of metals with carbon steel products accounting for around 50% of sales, aluminum products around 15%, and stainless steel products at 14%. The company has increased sales in the last 8 consecutive quarters, operating profit was up in 5 out of 8 quarters, and EPS was up for the last 5 consecutive quarters. Considering that RS is among 40 cheapest stocks in the Russell 3000 that is decent performance. The decline is the energy sector has hurt this stock as well, however the energy business is only 8-10% of sales. It should be noted that the company does not have any direct exposure to the underlying price of any commodity because they are a fabricator. Basically, the client buys the material and RS bends, shapes it, cuts it, etc. They are more exposed to the large macro economies as their products serve a number of industries. Hence a greater economic decline would result in an industrial decline and hence affect RS.

Date: **May 21st, 2015**
Ticker: ARW, AVT, NSIT
Name: Arrow Electronics, Avnet, Insight Enterprises
Transaction: Sector Rebalance

Note:
While technology distributors, the industry group is the same as Sanmina which the portfolio is overweighted – hence the 1st reason to rebalance. Secondly, ARW and AVT viewed as separate positions does not add value as they are both direct competitors and performance is similar while both being cheap. So to improve the risk profile, I reduced both ARW and AVT and added a smaller position in the even cheaper NSIT to add diversification.

Date: **May 13th, 2015**
Ticker: CBI
Name: Chicago Bridge & Iron
Transaction: Sold
Price: $51.16
Size: Reduced position

Note:

On the 13th the stock rallied despite pretty bad news that there would be further delays in the Georgia nuclear plant which costs about the company about $4m a day in financing and other costs. I took the opportunity to reduce, waiting for a pullback to re-enter. Two days later the stock still held and Greenlight announced they increased their position. This pushed the stock even higher. It looks like either Greenlight was holding it up or there was some insider activity, as the company also announced the success in getting additional projects…

Date: **May 12th, 2015**

Ticker: IMKTA
Name: Ingles Markets
Transaction: Bought
Price: $47.71
Size: New position

Note:
The company is a regional supermarket chain based in the Southeastern US where is operates over 200 supermarkets. Its relative cheapness makes it a potential acquisition. Regardless, this is an interesting opportunity. The company owns a lot of the land around its stores so essentially it controls the competition. It is expanding through complimentary services such as gas stations and pharmacies. The market fell in love with recent results (increased margins and comparable store sales up 1.2%) pushing the stock to $50+.

Date: **May 11th & 19th, 2015**
Ticker: XRX
Name: Xerox
Transaction: Sold
Price: $11.25, $11.42
Size: Reduced position

Note:
Please see May 11th rational for the reduction in this stock in the blog article I wrote found here: http://goo.gl/rMtc8m. Upon further study of XRX, I further reduced the position on May 19th. Operating cash flow has drop significantly vs last year. Operating margin is down from 6.5% to 5.5%. Management can't be trusted with outlook and will be happy with just dragging things out it appears. Cash reduction at company is further at risk with possible acquisitions.

Date: **May 6th & 7th, 2015**
Ticker: PXD
Name: Pioneer Natural Resources
Transaction: Sold Short & Covered
Price: $161.50, $160.12
Size: No position (entry/exit same month)

Note:
Einhorn's presentation (see: "Check This Out!" section) brought this company to my attention. Basically, the argument is that this oil and gas exploration and production company is blowing through a lot of cash without making enough in return. He makes a strong argument for a failed business model. I took the short, but reconsidered it after no instant follow through. Basically feared a bounce post the event. This now looks like a mistake as the stock is now over $10 low, however shorts can be dangerous in a rising market. This remains on my watch list.

Date: **May 4th, 2015**
Ticker: ACCO
Name: Acco Brands
Transaction: Bought
Price: $7.99
Size: Added to position

Note:
The stock remains cheap and some interest has recently emerged with a rally from $7.19-8.75. On a pullback to the 200-ma, I added to the position.

Date: **May 1st & 7th, 2015**
Ticker: LNKD
Name: LinkedIn
Transaction: Sold Short & Covered
Price: $206.74, $201.40
Size: No position (entry/exit same month)

Note:
Bubbles like LNKD live on expectations and "stupid" projections. The EPS miss is a lot worse for the stock than it appears as analysts are reducing their EPS on the company. So year-on-year EPS growth turns negative. The only thing keeping this alive is the revenue growth. For now though this looks like a decent short play until at least next quarter. I took profits early as I had expected an additional violent move downwards which did not happen. For now the market appears happy to wait and see.

Commentary (Continued from page 1)

In the meantime, you have to be careful not to overtrade and to stick to your strategy. It's tough being a value investor but it's also the reason value will continue to outperform in the long run. Who wants to hold shares in a company with declining sales and profits? Tough to get excited about that. It's much easier to look through all the great companies that are doing well, but that's what everyone is doing. And that's why they are no longer

cheap. If we look at the Russell 3000, we will find that only 525 companies have increased sales and operating profits in the last eight quarters consecutively. Every other company either had one or more down quarters in either sales or operating profits. Furthermore, if we look at that short list, we will find that only 24 of those companies are in the cheapest decile (not a very popular group). In contrast, around half of the 525 companies are in the 33% most expensive stocks in the market.

So as value investor we lean against the cheapness and not the fantastic company operating performance to help us make our return. As a result our biggest risk is always the value trap. The Radioshacks and BlockBuster Videos of the world. There are ways to help filter out the risks but it's a significant risk that constantly needs work at. This is what I've been thinking about, this past month as I have reduced my position in HPQ and XRX. Your ideal scenario is ANTM (ex WLP) when it gets extremely cheap but operating performance is still there and continues. But ANTM is more of an exception rather than the rule. Value stocks are cheap because of the increased uncertainty and unpredictability of what is to come. Reflecting on XRX, the stock reached $14+ in late 2014. I was long the stock from $10-11. I wasn't satisfied with the operating side of the business but my models still gave it as cheap. So I took the view that if I sold it what would I be replacing it with? And to hold on until it moved out of value. The stock is still in value but in the $11-12 range. Now applying this same approach to ANTM and holding on was gold, as the stock more than double from my entry. So lesson is that sometimes you need to be a little flexible. But at the same time, you need to be careful when to apply one approach and when not too as you may leave too much on the table. Not to mention potential overtrading….