FATALPHA
VALUE INVESTING

"You listen good to I, because it's either education or elimination!"
- Big Mama (Pearl Bailey), from the Fox and the Hound (1981)

2014 was another great year for the FatAlpha portfolio as it rose 30% vs 11% for the S&P 500. December closed up 0.86% while the market had a horrible New Year's Eve resulting in a down month for the S&P at -0.42%.

FatAlpha did it again and I believe the foundation is there for performance to do well in all types of markets. That does not mean there will be no losses, nor does it mean the portfolio will not underperform. There is no holy grail in investing but only sound strategies/process that result in good returns over the long run. An investor can have a good process but have a bad result and another can have a bad process but get lucky. Who do you want to be?

Russo and Schoemaker in their book "Winning Decisions" have a matrix which describes this:

		Outcome	
		Good	*Bad*
Process	*Good*	Deserved Success	Bad Break
	Bad	Dumb Luck	Poetic Justice

MONTHLY PERFORMANCE		
Date	**FatAlpha**	**S&P 500**
July '12	**2.89%**	2.13%
Aug '12	**9.12%**	1.98%
Sept '12	**3.03%**	2.42%
Oct '12	**0.66%**	-1.98%
Nov '12	**5.58%**	0.28%
Dec '12	**1.79%**	0.71%
Jan '13	**6.45%**	5.04%
Feb '13	**0.71%**	1.11%
Mar '13	**5.35%**	3.60%
Apr '13	**6.47%**	1.81%
May '13	**4.19%**	2.08%
June '13	**-0.73%**	-1.50%
July '13	**7.45%**	4.95%
Aug '13	**-1.00%**	-3.13%
Sept '13	**2.78%**	2.97%
Oct '13	**6.26%**	4.46%
Nov '13	**5.50%**	2.80%
Dec '13	**4.34%**	2.36%
Jan '14	**-1.76%**	-3.56%
Feb '14	**7.64%**	4.31%
Mar '14	**0.91%**	0.69%
Apr '14	**5.08%**	0.62%
May '14	**0.97%**	2.10%
June '14	**0.83%**	1.91%
July '14	**3.17%**	-1.51%
Aug '14	**3.67%**	3.77%
Sept '14	**-2.39%**	-1.55%
Oct '14	**6.21%**	2.32%
Nov '14	**1.78%**	2.45%
Dec'14	**0.86%**	-0.42%
2012	**25.14%**	**5.60%**
2013	**59.01%**	**29.60%**
2014	**29.95%**	**11.39%**
Since Inception	**158.59%**	**52.45%**

Yankee's baseball player Lefty Gomez used to say "I'd rather be lucky than good". And some extremely lucky individuals may even last an entire career based on dumb luck. However the majority of those with a bad process will result in a bad outcome. Therefore we increase our odds by having a good process. A good process is formed through education, experience and constant improvement.

My 23-month old son loves Disney's The Fox and the Hound. In it there is a wise owl called Big Mama who advises the young fox to educate itself or risk elimination. Many investors don't

think they need to constantly educate themselves, and I am always surprised by the amount of confidence individuals have in their own knowledge.

Every year, I'm invited to a relative's house for New Year's Eve. And practically every time, I hear the most ridiculous comments on finance and economics. It shocks me how stubborn people can be and confident they are for unrelated reasons (eg. I'm a lawyer or I'm a doctor so I know everything). These people of course have lost a lot of money investing. It's not because they are not smart enough to become good investors but it is because they think they are good investors and don't need to educate themselves.

We all need to keep learning in order to adapt. We also need to keep an open mind. Fortunately there is no lack of materials for investors to read. Most of it is free! Personally, I like to read sources which are bearish. Bear's usually go into more depth and are very passionate about their view. Markets go up most of the time so most of the talking heads will support a bull market, as will the brokers and banks of the world as bull markets generate income. It's usually easier to make a bullish case. Hence by reading the bearish view investors restore balance and can better access the current market.

I would recommend readers check out these bears: Mauldin Economics (free), Ben Hunt of Epsilon Theory (free), Hussman Funds (free), and Zerohedge (bearish website). For free bear calls, Citron Research and Muddy Waters are quite popular ever since their short call on Sino Forest. But there are many other free resources investors can use, such as GMO and Seeking Alpha. In general, I recommend against paying for newsletters as I have yet to see anything of much worth. If any of my readers read anything useful then please let me know. I have seen a lot of samples and done trials but looks like my fellow Canadian and FatAlpha follower may be right. He told me (along these lines) "Newsletters are written by those who can't manage money successfully". The only subscriptions I found that are worth spending money on are Value Line, Morningstar, S&P Outlook and the AAII (American Association of Individual Investors). Beyond those sources, the WSJ, the FT and Barrons. If you disagree and really insist on a newsletter then check out Dick Davis Investor Digest (displays numerous ideas from various sources) or Value Investor Insight (interviews value fund managers every month and discuss ideas they are invested in). But better yet, spend your hard earned cash on a book. Feel free to e-mail me for suggestions.

Now on the open mind bit, I suggested above, you can't be stubborn on a position or market bias. During December, I reduced my position in GME (GameStop) as the stock continued to drop. A value play and trap is separated by a thin line and we always have to reassess on which side of the line our investment is. When it gets blurry then it's time to take some action. That usually means reducing the position. Yes, you may take some losses despite the stock's

cheapness. However a stock can always get cheaper. And how about if you are wrong? Holding on will only make things worse. If the stock goes up then you makes some money on the remaining position while having reduced the risk to the portfolio. There are always opportunities and so it is best to redeploy the money elsewhere. It's all about opportunity cost. This month's trades showed somewhat how I manage the portfolio. CSC (Computer Sciences) is a profitable position I exited because I came to the conclusion that there would be a drag on the stock. NSIT (Insight Enterprises) while still cheap has seen its valuation expand to a point where other stocks are more attractive. I do not use strict price targets but use relative valuations. Other opportunities look cheaper which means more upside and hence the switches and trades I do.

2015 will be an interesting year. There is the potential Fed hike, the geopolitics, deflation in Europe and Japan, Greece and oil. The recent drop in oil has seen two camps emerge. The bullish camp which says that cheap oil is great for the market because consumers have more free income to spend and costs drop for corporations. The bearish camp points to all the job creation in the oil industry, the growth in GDP due to the sector and all the capex spending. All of this would not be around without the boom that occurred in the U.S. Both camps have good points. My conclusion is that it could be short-term bearish but long-term bullish for the market.

Problems in growth outside of the U.S. could delay the rate hike. Structural reforms are needed in Europe, same for overleveraged Japan. Both are time bombs that could cause significant and unpredictable damage to market indices. Europe may have to face the music sooner rather than later if a change in government in Greece occurs and they demand changes from the Troika. All this at the end of January. Also see Bloomberg's Graphic where a picture is worth more than words: http://www.bloomberg.com/graphics/2015-flash-points/

So obviously a lot can go wrong. Hence by keeping an open mind, listening to all opinions and constantly educating ourselves can help us weather the storm. Wish you a great 2015!

Transaction History by Date:

Date:	**December 31st, 2014**
Ticker:	AET
Name:	Aetna
Transaction:	Sold
Price:	$90.24
Size:	Exit Position

Note:
Purchased as a cheap growth play, the stock did well rising from a purchase price of $77 to $90.24 (sell price) in four months. Its current valuation is beyond the FatAlpha acceptable relative levels and hence the position was sold. It's a shame the position was small, but this restriction was needed as the portfolio had and has two other positions in health care.

Date: **December 31st, 2014**
Ticker: NSIT
Name: Insight Enterprises
Transaction: Sold
Price: $26.31
Size: Reduce Position

Note:
Sold half the position in NSIT as the stock has appreciated and is moving out of value.

Date: **December 31st, 2014**
Ticker: CSC
Name: Computer Sciences Corp
Transaction: Sold
Price: $64.10
Size: Exit Position

Note:
Sold the entire position in CSC at a small profit at $64.10. The company announced a settlement with SEC after a four year probe. The company will pay a $190m fine, restate 2010, 2011 and 2012 results and have an independent review of its compliance policies. 2013 and 2014 were not affected. The current CEO is a 27-year IBM veteran who joined in March 2012. He changed 80% of the team. The accounting irregularities are not as dramatic as they sound as the majority is a shift of impairment charges from 2012 to 2011. The details can be seen in this filing (http://goo.gl/JCCtkC). This event is a likely obstacle for stock appreciation. While cheap, it's not cheap enough to justify holding on. Combine this event with a quarter which saw operating growth drop 11% (vs -6.5% in the previous) and a drop me margins then the

conclusion is a likely poor performer going forward. Hence a reallocation elsewhere makes more sense.

Date: **December 9th & 31st, 2014**
Ticker: DTV
Name: DirecTV
Transaction: Opportunistic Trade
Price: $83.76 & $86.95
Size: No Change Month-on-Month

Note:
With the recent market volatility, DTV traded at a bigger discount to merger value and I took the opportunity for a short-term trade. The market recognized the imbalance and the stock traded back up. I took profits and reduced the position back to its initial level.

Date: **December 3rd & 4th, 2014**
Ticker: CTB
Name: Copper Tire & Rubber
Transaction: Long
Price: $31.49 & $32.19
Size: New Position

Note:
CTB is the 11th largest manufacturer of tires worldwide. In addition, it produces inner tubes, vibration control systems and hose assemblies. This value stock has seen strong growth in the last quarter. The sale of its joint venture in China which has been problematic for the company should help the story.

Date: **December 3rd, 2014**
Ticker: ACCO
Name: ACCO Brands
Transaction: Long
Price: $9.15
Size: New Position

Note:
ACCO is a manufacturer of offices product which it then supplies for resale. Its products are marketed to around 100 countries worldwide. The stock trades at 10x earnings and appeared on my value screen. After four consecutive quarters of declining sales, the company recorded an increase of 0.6%. Operating profit rose 23% and operating margins rose to 13.1% from 10.7%. The company's restructuring plan to reduce costs has done well. Debt to EBITDA has dropped from over 5x to under 4x in less than 2 years, and it free cash flow has allowed it to initiate a stock buyback.

Date:	**December 2nd, 2014**
Ticker:	GME
Name:	Gamestop
Transaction:	Sold
Price:	$35.48
Size:	Reduce Position

Note:
While I did very well the first time around I held GME, this time it's been harder despite the new console releases which I expected to push the stock to new highs. This quarter it missed due to a delay in the release of Assassins Creed. Makes some sense, but still the company guided lower for next quarter… when the games impact should actually be positive and larger than current expectations… The stock has traded below all the key moving averages, and despite the large drop post earnings, there was no relief rally. This usually signals the market is more concerned than usual. Other issues hurting the stock are potential inventory problems as older console sales fell more than expected, the impact of the CEO's sickness may have been underestimated, and the last minute announcement of expansion of holiday sales and discounts by a week.